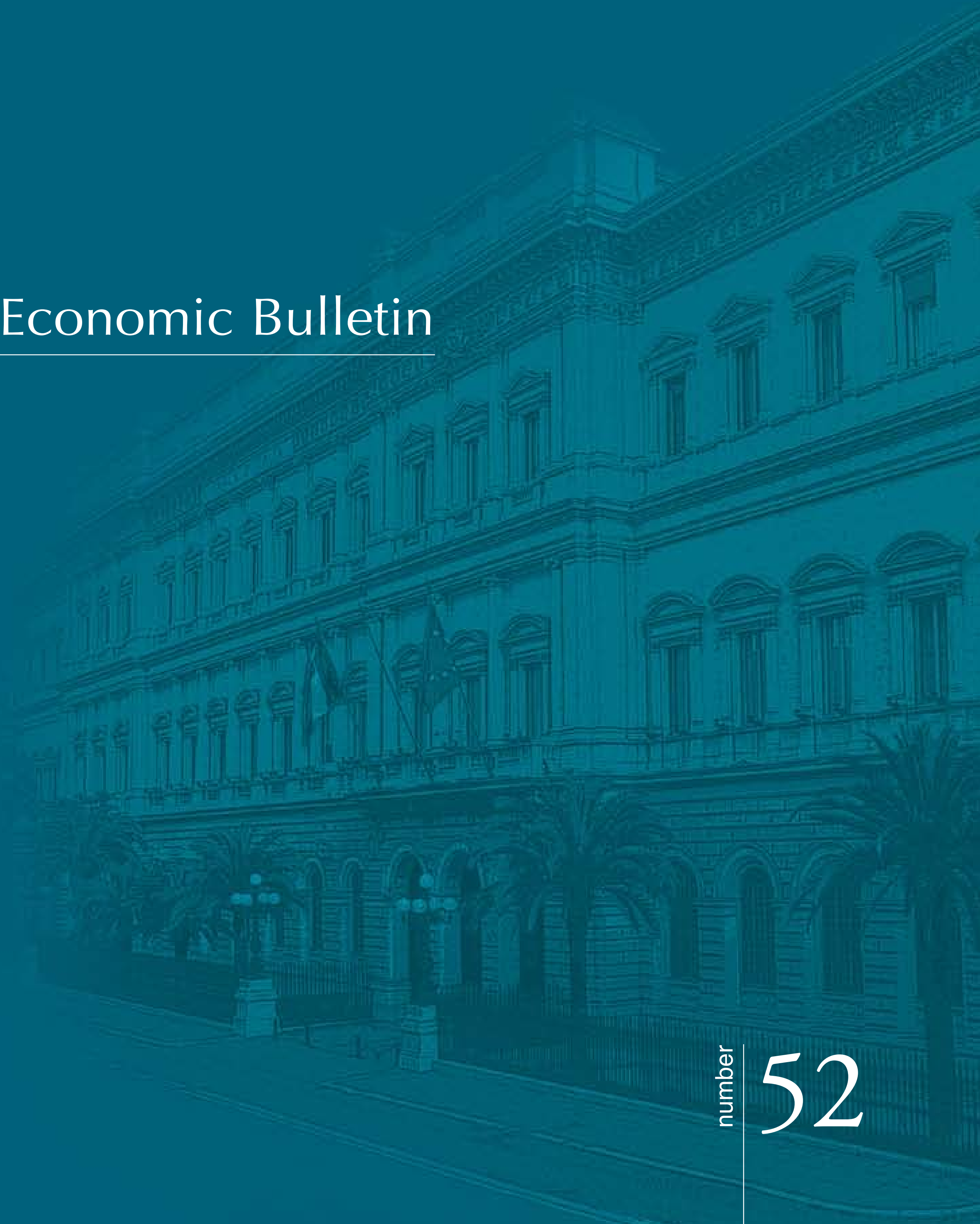
BANCA D'ITALIA

EUROSISTEMA

Economic Bulletin



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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

The financial crisis is affecting the real economy

The effects of the financial crisis on the real economy are proving highly virulent. The sharp reduction in wealth, the slowdown in lending and the deterioration in consumer and business confidence are holding back demand and output in the advanced economies, where there have been significant job losses. The consequences are serious for the emerging and developing economies, where the volume of international credit inflows is down by more than two thirds compared with 2007. The decline in international trade is affecting economic activity, with the risk of the banking system being weakened further. International organizations and the analysts consulted by Consensus Economics *have been adjusting their forecasts downwards.*

Some signs that pressures are easing should be verified

More recent data, whose importance and robustness will be assessed in the coming weeks, suggest that the fall in economic activity may be slowing in the United States, particularly as regards the real estate market and consumption. The effects of the extraordinary policy measures adopted to stimulate aggregate demand by almost every country will have to be examined.

The response from governments and monetary authorities has been intense ...

Governments and central banks have stepped up their efforts to keep liquidity abundant, contribute to strengthening the banking systems' capital base and foster the recovery of lending and aggregate demand. The cuts in official rates have been unprecedented both in size and in rapidity. The main central banks have launched unconventional monetary operations with the aim of increasing the supply of money, influencing long-term interest rates and guaranteeing well-functioning lending markets to the benefit of the economy. The size of central banks' balance sheets has increased considerably. Beginning in the second half of 2008, almost all countries have taken a decidedly expansionary fiscal policy stance, with measures to support demand on a scale also unprecedented since the Second World War. The estimates of international organizations point to a widening of the budget deficit by almost 4 percentage points of GDP in the advanced countries and by over 3 points in the emerging economies. The intensity of the discretionary measures varies from country to country, reflecting differences in the impact of the crisis, the magnitude of automatic stabilizers and the level of government debt. In the United States, measures have recently been announced to remove the troubled assets from banks' balance sheets.

... but banking systems continue to face difficulties

The difficulties of the international banking system have persisted in the first few months of 2009, even if it appears that interbank markets are gradually returning to partial normality. The problems have been reflected in share prices, whose fluctuations are primarily determined by uncertainty over developments in the financial sectors. Bond spreads remain wide. Strains also persist in the financial markets of the emerging economies.

At the end of 2008 the recession worsened in the euro area

The economic situation in the euro area deteriorated sharply towards the end of 2008. The collapse of exports in the fourth quarter (-6.7 per cent compared with the previous quarter), together with that of investment, led to a fall in the rate of productive activity, with a further contraction expected at the beginning of this year. Household consumption also slowed, despite the sharp decline in inflation, *probably dampened by uncertainty over employment prospects. The unemployment rate in the euro area has been rising, and accelerating, since the beginning of 2008. The European Central Bank has continued the policy of cutting official rates begun last autumn, lowering its reference rates by 50 basis points in January and a further 75 basis points between March and April. The reduction in inflation has gradually spread to the core components, while the downward pressures of external origin have abated. Inflation expectations, while lower than those formulated at the end of 2008, do not envisage a generalized and lasting fall in prices.*

GDP is falling sharply in Italy too

In Italy the contraction in GDP, under way since the spring of 2008, became more pronounced in the last quarter of 2008, with a fall of 1.9 per cent from the previous quarter, the largest since the 1974-75 recession. The slump in exports and investment contributed. The decline in employment that began in the third quarter of last year has continued, with an increase in the recourse made to the Wage Supplementation Fund. On a seasonally adjusted basis, the number of unemployed has increased almost without interruption since the third quarter of 2007. The uncertainty over employment prospects has offset the positive effect on consumption of the fall in inflation. The cyclical indicators point to the continuation of the contraction in economic activity in the first quarter of this year, the fourth in succession. There are signs of a prospective easing of the force of the recession, for example in the recent survey of firms conducted by the Bank of Italy in cooperation with Il Sole 24 Ore*, although not yet sufficient to presage an end to the fall in output.*

Bank lending and funding are slowing

Bank lending is continuing to slow in response to demand factors and, in the case of lending to firms, of supply factors as well. Loan quality is being influenced by the worsening of economic conditions. Funding is slowing. Starting last year the Government and Parliament have adopted measures to protect depositors, support banks' liquidity and capital and strengthen intermediaries' ability to satisfy the demand for credit.

The recession is worsening the public finances

The recession is worsening the public finances. In 2008 the deficit began to grow again, to 2.7 per cent of GDP. Total revenue slowed sharply; indirect tax receipts diminished. Primary current expenditure grew at a higher rate than the average of the two preceding years. The ratio of the public debt to GDP rose, returning to its level at the end of 2005. In February the Government estimated a further increase of one percentage point in the deficit for 2009, due to the worsening economic situation. A forecast update is expected in April. In the first three months of the year tax revenue on a cash basis diminished by 5.4 per cent compared with the same period of 2008. The size of the public debt limits the scope for discretionary measures to support aggregate demand. In February the Government strengthened them by introducing demand-side incentives, especially for durable goods, and tax reductions for firms. For the most part the measures are financed by reducing other expenditures.

2 THE WORLD ECONOMY

2.1 THE FINANCIAL MARKETS AND ECONOMIC DEVELOPMENTS

The financial crisis is having repercussions on the real economy

The financial crisis is having repercussions on the world economy; by causing a fall in wealth and in the supply of credit and a deterioration in consumer and business confidence, it is generating a contraction in output in the advanced economies, accompanied by large job losses, and a sharp slowdown in emerging economies, which are also being affected by an appreciable reduction in international capital inflows. World trade is falling considerably for the first time in a quarter of a century, partly as a reflection of a reduction in the availability of trade credit.

The economic policy response has been intense

On 2 April the Summit of the Group of Twenty countries decided to increase the resources of the International Monetary Fund in order to ease the financing difficulties of emerging economies; it announced the allocation of $250 billion to support trade credit over the next two years; it endorsed the countercyclical macroeconomic policies and the policies to support financial systems that have already been adopted by monetary and fiscal authorities at national level; it expressed the countries' intention to strengthen the supervision and regulation of financial systems. The decisions of the G20 are part of an unprecedented series of actions implemented by policymakers in recent months to counter the crisis. In the leading economies new extraordinary measures have been adopted to support financial systems (see the box "The recent measures to support the banking system and stimulate lending: the United States and the United Kingdom"); financial institutions in the leading euro-area countries have made use of government guarantees for their bond issues (see the box "The recent measures to support the banking system in the main industrial countries", *Economic Bulletin* No. 51, January 2009). Budgetary policy has been deployed to counter the downturn; the measures that have been adopted should provide a substantial boost to growth in 2009 and 2010 (see the box "The anti-crisis fiscal measures in the main advanced and emerging countries"). Central banks have pursued expansionary monetary policies, in some cases including non-conventional measures aimed at having a more direct impact on the long-term borrowing costs of households and firms.

THE RECENT MEASURES TO SUPPORT THE BANKING SYSTEM AND STIMULATE LENDING: THE UNITED STATES AND THE UNITED KINGDOM

The United States. – The authorities' actions to support the banking system continued along the main lines set out in the measures of previous months, which address the need to bolster the capital of the institutions worst affected by the crisis and to tackle the difficulties they are having raising funds in the markets.

The Financial Stability Plan. – On 10 February the US Treasury announced the outlines of a broad and comprehensive set of measures to strengthen the capital of banks (the Capital Assistance Program, or CAP), to remove from their balance sheets impaired assets for which there is no liquid market (the Public-Private Investment Program, or PPIP, defined in detail on 23 March) and to stimulate lending to small businesses.

By means of the CAP, the Treasury intends to strengthen the capital of banks so that they will be able to withstand a worse-than-expected recession and thus be in a position to continue to lend to the economy. For banks with assets in excess of $100 billion, the potential losses and possible need for recapitalization will be assessed in relation to various macroeconomic scenarios using a stress testing procedure. The granting of fresh public funds under the CAP is subject to a series of conditions requiring recipient institutions to comply with limits on executive remuneration and the distribution of dividends, present a plan showing how the use of the new resources will enable them to maintain or expand their lending capacity, and submit to the Treasury a detailed monthly report on their lending activity, which will be published.

The PPIP provides for the creation of mixed public-private investment funds to purchase problem assets from banks in order to remove the uncertainty still burdening their balance sheets. The funds will mainly purchase portfolios of mortgage loans and securitized products linked to such loans for which there is no liquid market, such as mortgage-backed securities (MBSs); they will finance such purchases either with their own funds or by borrowing. In the case of purchases of loan portfolios, the debt issued by the funds (in a ratio of up to six times their capital) will be guaranteed by the Federal Deposit Insurance Corporation (FDIC). In the case of purchases of securitized products, the funds will receive loans direct from the Treasury and will be able to access the Term Asset-Backed Securities Loan Facility (TALF), set up by the Federal Reserve in November 2008 to finance the purchase of securities tied to consumer credit and loans to small and medium-sized businesses. The Treasury will provide 50 per cent of the funds' capital, using between $75 billion and $100 billion of the troubled Assets Relief Program (TARP), approved in September 2008 with the aim of supporting banks' balance sheets (see the box "The crisis of some US financial institutions and the support action of the authorities", *Economic Bulletin* No. 50, October 2008). Combined with the contribution from private investors and thanks to financial leverage, these resources will make it possible to purchase assets worth about $500 billion, a figure that could double as a result of the subsequent expansion of the plan. The purpose of inducing competition between several investors, which in the case of loan portfolios occurs through participation in the auctions conducted by the FDIC, is to establish the underlying value of the problem assets, thereby reducing the risk of losses for taxpayers and uncertainty about the size of the losses that will remain on banks' balance sheets.

In order to foster an increase in lending to households and businesses and reduce the cost of credit, the Financial Stabilization Plan (FSP) also provides for a significant expansion in the TALF: the amount of lending that the Federal Reserve can grant under this scheme may be increased from the original $200 billion to $1,000 billion, and there is provision for a gradual widening of the range of assets that can be purchased using TALF financing.

On 16 March the Treasury announced two further temporary initiatives to stimulate lending to small and medium-sized firms guaranteed by the Small Business Administration (SBA), in general new start-ups, firms undergoing expansion and non-profit businesses operating in the construction industry. The Treasury will purchase in the secondary market a total of up to $15 billion of securities backed by certain categories of loan guaranteed by the SBA. The SBA will also eliminate the fee for access to its guarantees, which for some categories of loan will be increased to up to 90 per cent of the loan amount, compared with 75-80 per cent at present. In order to facilitate the monitoring of lending in this sector and assess the effectiveness of the measures adopted, all banks will be required to report to the Treasury each quarter the amount of loans granted to small and medium-sized firms.

Other measures to support financial institutions. – Between mid-January and the beginning of March the US authorities also announced new measures to support certain financial institutions of systemic importance. The Treasury and the FDIC will grant Bank of America a guarantee on a portfolio of assets worth around $120 billion and will inject $20 billion of capital into the bank from the TARP. In order to improve the quality of the capital and financial leverage of Citigroup and the AIG insurance group, the Treasury announced that it intended to convert the preference shares it had recently acquired in the two institutions into ordinary shares ($25 billion and $40 billion respectively). In addition, AIG will receive $40 billion of fresh public capital and its debt to the Federal Reserve will be restructured, in order, among other things, to reduce its interest payments.

The Homeowner Affordability and Stability Plan. – On 18 February the Administration announced a plan to assist households in difficulty with the repayment of mortgages in order to stem the rapid growth in foreclosures and stabilize house prices. The plan establishes a series of incentives to encourage the restructuring of mortgages where there is a risk of debtor insolvency, with the aim of reducing the ratio of monthly repayments to income to 31 per cent; the Treasury will bear 7 percentage points of the reduction; in the absence of agreement, the bankruptcy courts may impose a fair restructuring. The plan also provides for mortgages held or guaranteed by Freddie Mac or Fannie Mae to be renegotiated at lower interest rates, even if the ratio between the residual debt and the value of the home had risen above the ceiling of 80 per cent as a result of the fall in the value of the property. A total of $75 billion has been allocated for the plan, which aims to offer support to between 7 and 9 million households.

In order to support the mortgage market, the Federal Reserve decided to increase its purchases of MBSs guaranteed by Fannie Mae and Freddie Mac from $500 billion to $1,250 billion and to double to $200 billion its purchases of the agencies' bonds, while the Treasury increased from $100 billion to $200 billion the maximum amount of capital that it undertakes to grant to the two agencies if required; hitherto the agencies have received far less than the previous limit.

The United Kingdom. – On 19 January the authorities announced new measures to support the banks and stimulate lending. A new guarantee scheme (The Asset Protection Scheme) was established to protect the banks' balance sheets from the risk of exceptional future losses on portfolios of financial assets, which include residential and commercial mortgages, structured credit assets and commercial, industrial and leveraged loans. Under the scheme, losses of up to around one-tenth of the value of the assets will be borne by the banks, while the remainder will be covered almost entirely by government guarantees for a minimum of five years. In return, the Government receives shares in the beneficiary banks, which must also make specific undertakings to increase lending to households and firms and regarding executive remuneration. Under the new scheme the Government has already reached agreement with two large banks. Royal Bank of Scotland will receive a guarantee in respect of assets worth £325 billion in exchange for £6.5 billion of preference shares and a commitment to grant £25 billion in loans during 2009; the Government, which is already the majority shareholder in the Group, will inject a further £13 billion of capital, again through the acquisition of preference shares. The Lloyds Group will receive guarantees in respect of assets worth £260 billion in exchange for £15.6 billion in preference shares and a commitment to grant new loans amounting to £14 billion over the next twelve months; the Treasury also undertook to replace its £4 billion of preference shares with ordinary shares, taking its holding in the Group to 65 per cent.

In order to stimulate a recovery in lending, the Government will offer guarantees on asset-backed securities (ABSs) linked to mortgages and corporate and consumer debt, while the Bank of England will purchase up to £50 billion of corporate bonds, commercial paper, syndicated loans, ABSs and banks' debt instruments guaranteed by the Government under the plan launched last October (see the box: "The recent measures to support the banking system in the main industrial countries", in *Economic Bulletin* No. 51, January 2009), the expiry of which has been extended to the end of 2009.

Commodity prices have stabilized

Oil prices (represented by the average for the three main grades) fluctuated between $40 and $50 a barrel during the first three months of 2009. The progressive implementation of production cuts by the OPEC cartel of around 2 million barrels a day between December and February has offset the price effect of expectations of a fall in world demand this year. On the basis of futures contracts, the price of WTI grade oil is expected to rise gradually over the coming months from the current level of $52 to around $61 at the end of the year (Figure 1). The dollar prices of the other main commodities remained broadly unchanged in the first two months of 2009.

Banking systems continue to face difficulties

The serious difficulties in the international banking system eased only slightly in the first few months of 2009. The spread between the rates on unsecured three-month interbank deposits and those on overnight index swaps for the same maturity – which provide a measure of strains in interbank markets – is still fluctuating at around 100 basis points for the US dollar; it has fallen to about 70 basis points for the euro (Figure 2). Risk premiums on credit default swaps for leading international banks – a measure of the probability of insolvency – increased up to 11 March but decreased slightly thereafter.

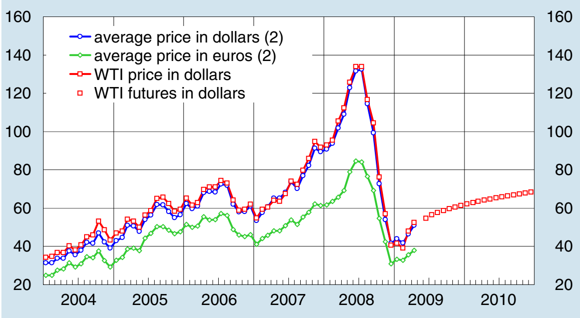
Central banks continue to support the markets ...

Central banks continued to provide support to the financial markets by bolstering the supply of liquidity. The Federal Reserve increased its support for lending to households and small and medium-sized firms by raising the ceiling on its purchases of securities from the securitization of such loans from $200 billion to $1,000 billion, equal to about 7 per cent of GDP. The Bank of Japan announced that it intended to purchase shares from banks totalling ¥1,000 billion (equivalent to about 0.2 per cent of GDP) in order to reduce the riskiness of banks' portfolios; it is also considering action to strengthen the capital of the banking system by granting the banks subordinated loans amounting to ¥1,000 billion.

Figure 1

Crude oil: spot and futures prices (1)

(dollars and euros per barrel)

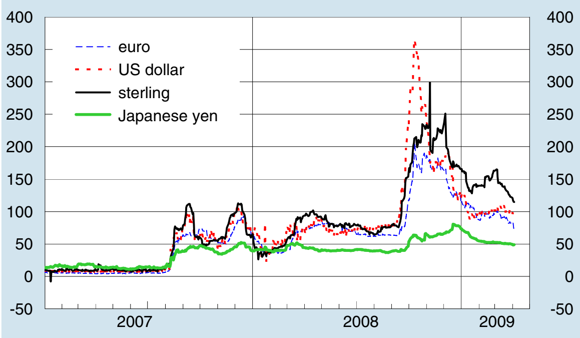


Sources: IMF and Thomson Reuters Datastream.
(1) Monthly averages for spot prices; the last data refer to 3 April 2009. – (2) Average price per barrel of the three main grades (Brent, Dubai and WTI).

Figure 2

Three-month LIBOR spread to overnight index swaps

(basis points; daily data)

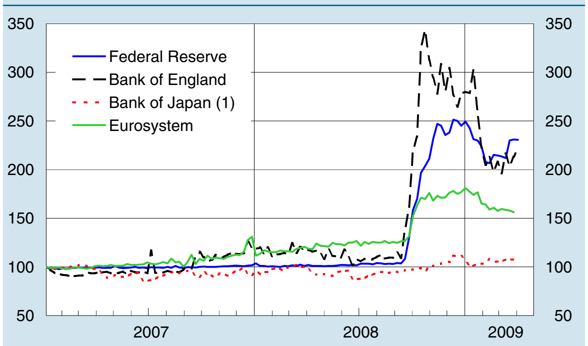


Sources: Thomson Reuters Datastream and Bloomberg.

Figure 3

Size of the balance sheets of selected central banks

(indices, 5 January 2007 = 100; weekly data)



Source: Thomson Reuters Datastream.
(1) The original data for the Bank of Japan relate to ten-day periods.

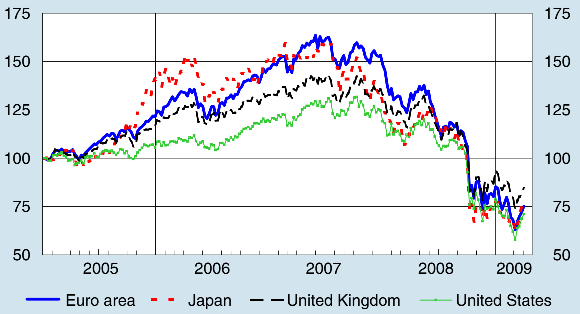
... by further expanding their balance sheets

The balance sheets of the central banks of the leading advanced economies, which had increased substantially between September and December 2008 in response to the need to supply liquidity to the markets, decreased slightly in the first few months of this year (Figure 3). In the coming months the assets of the central banks that have now reduced their policy rates to virtually zero (the Federal Reserve, the Bank of Japan and the Bank of England) will begin to increase again owing to the adoption of strategies aimed at having a more direct impact on long-term interest rates.

Figure 4

Stock market indices (1)

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



Source: Thomson Reuters 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.

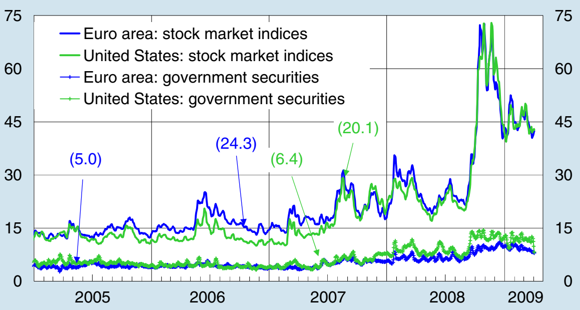
Stock markets are affected by uncertainty in the financial sector

The main stock markets suffered large losses in the early months of 2009, generally led by the steep fall in the prices of financial stocks. In the last few weeks the expectation of an accentuation of official intervention to support financial systems has contributed to a partial recovery, again mainly in the financial sector (Figure 4). In the first few days of April the Standard & Poor's 500 Index was around 7 per cent lower than at the beginning of the year; the losses in the share markets of the euro area and the United Kingdom were comparable, amounting to about 9 and 7 per cent respectively; they were less marked in Japan. The implied volatility of share prices in the United States and the euro area remained high by historical standards, albeit significantly below the peaks of last November (Figure 5).

Figure 5

Implied volatility in the prices of shares and government securities (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 securities: 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.

Bond spreads remain wide

In the first few months of 2009 risk premiums on all the main classes of corporate bonds remained high (Figure 6). In particular, premiums on high-yield bonds began to increase again, so that by 11 March they were not far from the peaks recorded in the first half of December; at the beginning of April they were about 1,650 basis points for dollar bonds and 2,000 basis points for bonds denominated in euros.

Yields on ten-year US Treasury securities were highly volatile until mid-March, then on 18 March they fell sharply, from 3 to 2.5 per cent, following the announcement by the Federal Reserve that it would purchase medium and long-term Treasury securities; they subsequently rose back to 2.9 per cent. At the beginning of March, in response to the announcement of a similar programme of purchases by the Bank of England, yields on ten-year government bonds in the United Kingdom fell sharply, from 3.6 to 3 per cent, before rising to 3.4 per cent. Fluctuations in yields on ten-year government bonds were much less pronounced in the euro area and Japan, where in the first few days of April they stood at 3.2 and 1.4 per cent respectively (Figure 7).

The financial markets of emerging economies also remain under strain

The emerging economies continued to have difficulty raising funds in international financial markets throughout the first quarter of 2009, as evidenced by the wide yield differential between their sovereign long-term dollar-denominated securities and US Treasury bonds. The differential measured by the EMBI Global Index generally fluctuated at around 700 basis points, before falling to 600 basis points in recent weeks. The differential for Asian economies remains smaller, benefiting from their lesser dependence on external borrowing and their more developed domestic financial markets. The stock markets of the emerging economies experienced mixed fortunes; at the beginning of April share prices expressed in national currencies were on average about 10 per cent higher than at the beginning of the year.

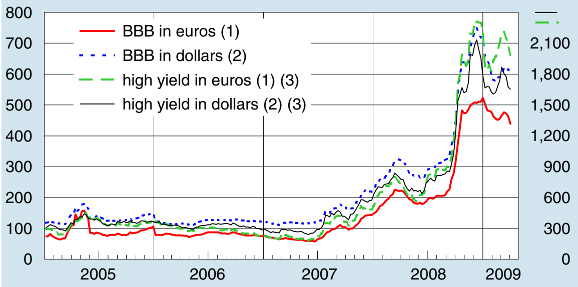
The appreciation of the dollar resumed in January and February and then halted in March

The appreciation of the dollar during the second half of 2008 slowed in December but resumed in the first two months of 2009. Signs of a reversal of trend appeared in March, and at the end of the month the dollar was barely 2 per cent higher in nominal effective terms than at the end of 2008. Its performance against the other leading currencies in the first few months of 2009 was mixed (Figure 8). Against the euro it began to depreciate in the first few days of March, probably after it became clear that the Federal Reserve was pursuing a more aggressive monetary policy than the Eurosystem; in the first few days of April its appreciation against the euro since the end of 2008 amounted to 4 per cent. The dollar/yen exchange rate, which had continued to fall in January and the first half of February, showed a sharp reversal of trend when Japan's national accounts estimates revealed the depth of the recession in the Japanese economy; at the end of March the dollar showed an appreciation of about 10 per cent against the yen since the end of 2008. The dollar fluctuated very little against sterling, partly owing to the very similar monetary policies being pursued by the Federal Reserve and the Bank of England.

Figure 6

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

(end-of-week data; basis points)

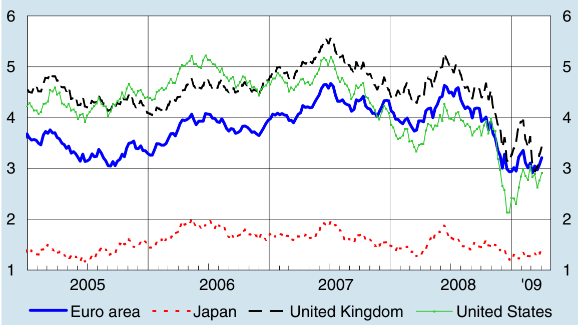


Source: Merrill Lynch.
(1) Fixed-rate bonds denominated in euros with a residual term to maturity of not less than one year issued in the Euromarket; yield differentials are calculated with respect to French and German government securities. – (2) Fixed-rate bonds denominated in dollars with a residual 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.

Figure 7

Yields on ten-year government bonds

(end-of-week data; percentages)

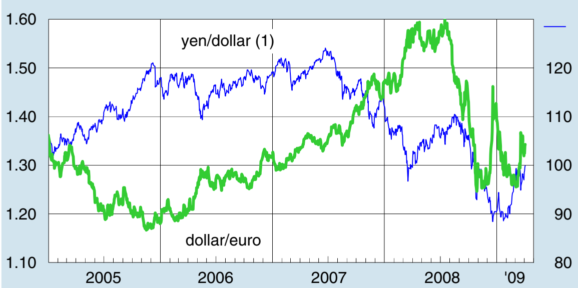


Source: National statistics.

Figure 8

Exchange rates

(daily data)



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

2.2 THE DECISIONS TAKEN AT THE G20[1] SUMMIT

New measures were discussed to tackle the crisis ...

On 2 April the Heads of State and Government of the G20 countries met in London to examine progress in the implementation of the plan announced in November 2008 and to decide on further measures to resolve the crisis and reform the international financial system. The leaders of the G20 repeated their commitment: to support demand and employment by means of highly expansionary monetary and fiscal policies (as regards the latter, see the box "The anti-crisis fiscal measures in the main advanced and emerging countries"); to ensure the resumption of lending by injecting liquidity, recapitalizing financial institutions where appropriate and taking measures to resolve the problem of impaired assets. The stimulus programme must not jeopardize the sustainability of public finances or long-term price stability and must be dismantled once the crisis has been overcome. The leaders also expressed their intention to carry out a far-reaching reform of the current financial system in order to eliminate problems and gaps in financial regulation and supervision and to lay the foundations of a new system to operate in the years to come (with regard to the initiatives taken in this field at European level, see the box "The reform of financial regulation and supervision in Europe: the informal Ecofin meeting in Prague").

... increase financial assistance to emerging countries, ...

The G20 expressed itself in favour of trebling to $750 billion the lending capacity of the IMF, which constitutes the maximum amount of non-concessional loans that the institution can lend and includes, as well as the quotas of countries with a sound balance-of-payments position, the additional resources provided under bilateral loan agreements and the New Arrangements to Borrow (NAB). Half of the increase in the IMF's lending capacity will initially be funded by bilateral loans from a number of countries ($200 billion has already been offered in equal parts by Japan and the EU countries); those resources will subsequently be incorporated into the NAB with further contributions of $250 billion. Finally, it was decided to bring the next general review of IMF quotas forward to January 2011 in order to ensure that the Fund continues to have adequate resources to meet member countries' borrowing requirements over the medium term.

A few days before the London Summit the Executive Board of the IMF approved the creation of a new lending window, the Flexible Credit Line. This instrument enables the Fund to make substantial loans for a period of one year, even in the absence of crisis and hence for precautionary purposes, to countries that have strong fundamentals and sound policies and which apply for loans under this facility. Mexico has expressed interest in using the new lending window; it is currently discussing a loan of 32 billion Special Drawing Rights (SDRs), equal to $47 billion, ten times its IMF quota.

The G20 also agreed on the need to increase the international liquidity available to emerging countries by making a new allocation of SDRs worth $250 billion. The allocation of new SDRs, which would enable recipient countries to increase their foreign exchange reserves, would be based on their IMF quotas. As a consequence, emerging and developing countries would benefit from only part of the increase in liquidity, equivalent to about $100 billion. The G20 also decided to bring forward ratification of a previous one-off allocation of SDRs, equal to about SDR 21 billion ($32 billion) that was decided by the IMF in 1997 but which has not yet come into force as the related amendment to the Articles of Agreement has not been approved by the required three fifths of countries with 85 per cent of the total voting rights. The allocation of these further SDRs will directly benefit countries that joined the IMF after 1981, the great majority of which are emerging and developing countries.

[1] Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Mexico, Russia, Saudi Arabia, South Africa, South Korea, Turkey, the United Kingdom and the United States. The EU also participates. The Netherlands and Spain were also present at the 2 April summit.

Finally, it was decided to carry out a far-reaching reform of the governance of the Bretton Woods institutions and of the representation of member countries within them. In particular, the relative voting power of emerging and developing countries will be increased at the next general review of IMF quotas; in parallel, by the time of the spring meetings in 2011, the World Bank will have to identify the criteria and methods for reforming the representation of member countries. It was also agreed that the heads and senior leadership of both institutions should be appointed through an open, transparent, and merit-based selection process.

... support world trade and increase development aid ...

The G20 countries will ensure the availability of at least $250 billion in the next two years to support trade finance. They will make bilateral contributions of between $3 billion and $4 billion to the Global Trade Liquidity Pool of the International Finance Corporation in order to mobilize $50 billion of resources in conjunction with the private sector. The remaining $200 billion will be granted by other multilateral development banks and the national export credit and investment agencies of the G20 countries. In addition, the G20 countries extended to the end of 2010 their pledge to refrain from raising new barriers to movements of capital and trade in goods and services; the World Trade Organization was invited to monitor adherence to these undertakings on a quarterly basis. Finally, the participants confirmed their intention to reach an effective conclusion of the negotiations under the Doha Round.

Over the next three years lending by multilateral development banks to low-income countries will increase from $200 billion to $300 billion; the capital of the Asian Development Bank will be trebled and increases in the capital of the other banks will be considered. The IMF's capacity to lend to the poorest countries will also be increased, by around $6 billion. The IMF will finance the new concessional loans out of the proceeds of investing the capital gains on sales of part of the its gold reserves and any budget surpluses. Finally, the G20 countries reaffirmed their commitment to achieve the Millennium Development Goals.

... and strengthen financial regulation and supervision

It was decided to place the Financial Stability Forum, renamed the Financial Stability Board (FSB), on a stronger institutional basis and to broaden its mandate. Participation in the Forum was extended to include all the G20 countries, Spain and the European Commission. The FSB will consist of a Chairperson, an enlarged Secretariat, a Plenary Board (in which all member countries will participate) and a Steering Committee, the members of which will be selected by the Chairperson in order to achieve a balance between representation and operational effectiveness. The FSB will (1) monitor developments in the financial markets and identify their implications for regulatory policies; (2) assist countries in implementing regulatory standards; (3) assess the adequacy of the work being undertaken by standard-setting bodies; (4) set guidelines for the establishment of colleges of supervisors for cross-border financial institutions; (5) produce contingency plans for managing crises at cross-border financial institutions of systemic importance; and (6) collaborate with the IMF in the conduct of early warning exercises. The results of such exercises will be presented by the FSB Chairperson and the Managing Director of the IMF to the meetings of the International Monetary and Financial Committee and the Ministers of Finance and central-bank Governors of the G20 countries. In addition, three new Standing Committees will be established within the FSB, for vulnerabilities assessment, supervisory and regulatory cooperation, and the definition of international standards and codes of conduct.

With regard to regulation and supervision, the G20 decided first to concentrate on regulation able to identify and neutralize systemic risks. All systemically important financial institutions, markets and instruments will be subject to appropriate regulation and supervision; the authorities will have to be granted the necessary powers to gather adequate information. In order to avoid regulatory arbitrage, internationally coordinated guidelines will be laid down to ascertain the systemic nature of institutions, markets and financial instruments. Hedge funds or their management companies will be required to register with the financial authorities and to report relevant information for assessing risk. Registration and supervisory requirements will be applied to credit rating agencies to verify that they comply with international codes of conduct, particularly as regards the prevention of conflicts of interest.

Secondly, the system of macroprudential supervision will be improved to prevent and effectively counter the emergence of systemic risk in financial markets. As soon as conditions in the financial system allow, the banks' minimum capital requirements will be reviewed, the quality of capital improved and the definition of capital harmonized internationally. Standards will be developed to promote the formation of capital reserves in excess of the regulatory minimum during periods of economic expansion, to be used when conditions deteriorate. Alongside the measures of risk-weighted capital, simple indicators will be introduced that will preclude the possibility of employing excessive financial leverage. The G20 countries undertook progressively to adopt the Basel II regulatory system, which will be further improved over time. The authorities will also encourage financial institutions, including cross-border institutions, to bolster their liquidity reserves.

On the question of remuneration, the G20 countries welcomed the FSF principles to ensure that the compensation systems adopted by large financial institutions are consistent with their long-term objectives and with prudent risk-taking.

The bodies responsible for setting international accounting standards will have to cooperate with the supervisory authorities in order to improve valuation standards, strengthen techniques for recognizing loan loss provisions so as to incorporate a wider range of available credit information, and move towards a single set of global accounting standards.

Finally, various measures were agreed to strengthen international cooperation: colleges of supervisors will be formed for the leading cross-border financial institutions for which such bodies are not already in operation; the principles developed by the FSF for cross-border crisis management will be implemented; action will be taken against jurisdictions that fail to comply with international standards for prudential supervision and information exchange for tax purposes.

The Ministers of Finance and central bank Governors of the G20 countries will discuss progress in the implementation of these measures before the end of this year.

THE ANTI-CRISIS FISCAL MEASURES IN THE MAIN ADVANCED AND EMERGING COUNTRIES

Since the middle of 2008 the fiscal policies of almost all countries have taken on a strongly expansionary hue, with measures to support demand on a scale not seen since the Second World War in addition to the measures undertaken to stabilize the banking and financial sector.

When cyclical fluctuations are modest, the use of automatic stabilizers and monetary policy is considered sufficient to contain the divergence of aggregate demand from potential GDP and mitigate the social costs of higher unemployment. Discretionary countercyclical fiscal measures are generally thought to be inappropriate, given the lag with which they take effect and the difficulty of assessing the true state of the economy.

The current crisis, which is exceptionally acute, protracted and globally extensive, necessitates the adoption of discretionary measures, preferably coordinated internationally. Moreover, the scope for monetary policy is limited – in some countries official rates are already close to zero – and the turmoil in the financial markets is making the transmission mechanisms more uncertain.

The importance of joint action on government budgets was also emphasized at the G20 summit at the beginning of April. Coordination may reduce the volatility of macroeconomic variables, enable each country to benefit from positive externalities and discourage opportunistic behaviour (free riding and protectionist policies). It was also noted that action needed to be adapted to suit the specifics of each country as regards the impact of the crisis, the state of the public finances and the extent to which the public accounts react automatically to changes in output, which depends on the size of the budget and its characteristics (for example, the coverage and generosity of the social safety net and the progressiveness of the tax system). The automatic stabilizers are more extensive in the countries of the European Union (EU) than in other economies.

The international institutions have stated that it is desirable for discretionary fiscal measures to be targeted and temporary. On the one hand, effectiveness and fairness demand that the fiscal stimulus involve the areas of the economy whose response to public intervention is greatest and most immediate and the sections of the population worst affected and needy. On the other, measures that are transitory and easily reversible are needed so as not to jeopardize the medium-term outlook for the public accounts; in order to ensure the sustainability of the public finances, action can also be taken to strengthen the procedures for controlling expenditure and the fiscal rules and institutions and to introduce structural reforms that would raise potential economic growth and curb the increase in spending over the medium and long term.

In line with the conclusions of the international fora, the measures to combat the crisis that have been launched so far in the various countries differ in composition and size. In particular, taking account of differences in the impact of the crisis, high-debt countries such as Japan and Italy have introduced more modest measures than others in order to ensure the sustainability of the public accounts.

According to recent estimates from the International Monetary Fund for the G20 countries, the budget deficits of advanced countries will deteriorate by an average of almost 4 percentage points of GDP in 2009 and that of emerging countries by more than 3 points, to 7.9 and 3.2 per cent respectively. The ratio of debt to GDP of the two groups of countries will increase by 10 and almost 2 percentage points respectively, to 93.2 and 37.6 per cent, partly as a result of the measures to aid the financial system.

The United States. – The American Recovery and Reinvestment Act, which was approved in mid-February, sets out measures for the three years from 2009 to 2011. Its overall impact on the federal budget deficit is estimated at just over 5 percentage points of GDP, of which 2 points will be incurred in 2009 and 1.8 points in 2010.[1] Around two thirds of the measures relate to spending on infrastructure, energy saving and environmental protection, public transport, scientific research and the health sector, as well as transfers to states and local authorities. The latter transfers are designed to forestall tax increases at the state and local level by enabling decentralized governments to comply with the balanced budget requirement to which many are subject by law. The Act also includes measures to assist households (unemployment benefits, support for those on low incomes and tax cuts) and, to a lesser extent, firms (temporary tax deferrals).

Japan. – The fiscal stimulus measures enacted by the Government amount to about 1.5 percentage points of GDP in 2009 and about 0.5 points in 2010. More than three quarters of the measures consist in higher expenditure, mainly one-off transfers to households and local authorities (subsidies to support the development of local economies and regional employment policies). On the revenue side, the most important measures are aimed at reducing labour costs (welfare contributions) and providing tax relief to small and medium-sized firms and certain strategic sectors (accelerated depreciation of investment to foster energy saving and alternative energies; reduction in taxation on cars with low emissions).

The European Union. – Last December the Council of the EU approved the European Economic Recovery Plan, a macroeconomic support programme that calls for measures totalling 1.5 per cent

[1] The calculation of the impact on the 2009 budget omits certain tax cuts on higher incomes equal to about $70 billion (some 0.5 per cent of GDP) that are included in the Act but linked to the periodic renewal of a measure to offset fiscal drag.

of the GDP of the EU in 2009 (the contribution from the Community budget is put at around 0.3 per cent of GDP). The Council emphasized that discretionary measures should be adopted that are timely, targeted and temporary and take account of the state of the public finances in each country.

The measures outlined so far by the major EU countries (France, Germany, Italy, the United Kingdom and Spain) affect both revenue and expenditure. In its assessments of the latest updates of stability and convergence programmes, the EU Commission has judged the measures to be broadly consistent with the guidelines set out in the European support programme.

France has launched anti-crisis measures that will increase the budget deficit by 0.8 per cent of GDP in 2009; their impact in 2010 is essentially nil. They provide for increases in public investment, incentives for firms – in particular in the automobile and construction industries – and assistance for families with low incomes.

Germany has launched expansionary measures that will have an impact on the budget balance of around 1.5 per cent of GDP in 2009 and one of 2 per cent in 2010. The measures for 2009 are designed to support the incomes of the most vulnerable sections of the population (reduction in personal income tax, tax relief and benefits for dependent children), investment (infrastructure, tax relief) and the automobile industry, and to limit the effects of the crisis on employment (on-the-job training measures). Although the majority of the measures are temporary, certain permanent measures also play a significant role.

In Italy the total resources allocated for countercyclical purposes in 2009 are equivalent to about half a percentage point of GDP, financed by countervailing measures so as to leave the balance unchanged (see the boxes "The anti-crisis decree" in *Economic Bulletin* No. 51, January 2009, and "February's anti-crisis decree" in this issue). In addition, the use of resources that had already been allocated has been revised to apply them to purposes that are more effective in stimulating aggregate demand. The scale and composition of the measures reflect the prudence necessitated by the size of the public debt.

In the United Kingdom the measures to combat the crisis relate mainly to the current year; they amount to about 1 percentage point of GDP and consist predominantly of tax relief for households (reduction in the rate of VAT). In addition, public investment planned for future years will be brought forward. The Government indicates steps to begin reducing the deficit as early as 2010.

The measures decided in Spain also relate mainly to 2009 and cause the budget balance to deteriorate by around 2 per cent of GDP. Almost half of the resources are allocated to public investment and to sectors of strategic importance for economic growth. The other measures are designed to support households (tax relief for purposes of personal income tax) and firms (mainly by modifying the time limits for applying for refunds of VAT).

The emerging countries. – China has announced fiscal measures that should amount to around 3 per cent of GDP in both 2009 and 2010.[2] The fiscal stimulus package involves mainly infrastructure investments, which will absorb more than 80 per cent of the increase in spending planned over the two years.

In India the measures to support the economy are temporary and affect the budget balance by about 0.6 per cent of GDP in the 2009 fiscal year. Intervention on the expenditure side, which is twice as large as that involving revenue measures (reduction in indirect taxes), includes higher spending on infrastructure, support for small and medium-sized firms, subsidies for export credit and an easing of budgetary requirements for federal states.

[2] Last November the Chinese Government announced a package of anti-crisis measures amounting to 4 trillion renminbi ($586 billion), equal to 13.3 per cent of GDP for 2008; the package is reported to include some measures that had already been included in previous plans or partly implemented and provisions that have no impact on the central and local governments' fiscal balances. According to the latest IMF estimates, the fiscal stimulus measures announced to counter the crisis should total around 2 trillion renminbi in 2009-10.

Brazil's measures amount to about 0.3 per cent of GDP in each of the next two years. More than two thirds relate to the revenue side (permanent reduction in personal income taxes and a temporary reduction in the tax on car sales). The bulk of the expenditure measures concern infrastructure.

In Russia the expansionary fiscal measures total almost 2 per cent of GDP both this year and in 2010. For the most part they consist of cuts in corporate tax rates, some of which are permanent (reduction in the tax rate on corporate profits and lower taxation on small and medium-sized firms) and others temporary (lower oil export taxes for 2009). Support to households will also be provided in the form of government aid to first-time homebuyers, measures to combat rising unemployment and subsidies for pensioners.

THE REFORM OF FINANCIAL REGULATION AND SUPERVISION IN EUROPE: THE INFORMAL ECOFIN MEETING IN PRAGUE

At the informal Ecofin meeting of EU economy and finance ministers and central bank governors in Prague on 3 and 4 April an agreement was reached on the fundamental principles for the reform of financial supervision at European level. The meeting also discussed matters regarding the procyclicality of financial systems and the valuation of financial assets in illiquid or inactive markets, in connection with the measures taken by EU countries to support financial institutions.

Reform of the organization of supervision in the EU. – The meeting discussed the proposals of the report by the EU Commission's high-level expert group on financial supervision to make macroprudential analysis more effective and enhance the integration of regulatory and supervisory activity at European level. In particular, to strengthen macroprudential oversight, the report calls for a new body, the European Systemic Risk Council,[1] charged with identifying the risks and vulnerabilities that threaten the stability of the financial system and recommending counter-measures. In the field of regulation and supervision of individual cross-border institutions, the report recommends establishing a new European System of Financial Supervision, composed of three European sectoral authorities (banking, securities and insurance) to replace the current Level Three technical committees of the Lamfalussy procedure (the Committee of European Banking Supervisors, Committee of European Securities Regulators and Committee of European Insurance and Occupational Pensions Supervisors). In the future, the system could be simplified by having only two separate authorities – one for prudential supervision, the other for transparency and conduct of business. The new system would still be based on decentralizing operational tasks to national authorities and strengthening the colleges of supervisors for cross-border institutions. The new authorities would act as coordinators, performing some tasks at European level. These would include issuing common supervisory standards, introducing mechanisms of mediation between authorities and, in the event of disagreement between them, adopting technical decisions directly applicable to financial institutions (for example, approval of internal systems to calculate capital requirements), and authorizing and supervising certain institutions of pan-European relevance (rating agencies and post-trading systems).

At the meeting, the informal Council agreed on the need to develop a macroprudential supervisory approach and to create the European Systemic Risk Council, assigning an important role to the central banks in coordination with national supervisory authorities. The meeting also reaffirmed the need to harmonize supervisory rules and standards, give supervisory authorities uniform powers and strengthen their independence. In addition, there was agreement on the recommendation that the role of Level

[1] The ESRC would be composed of the members of the General Council of the ECB, the chairs of the Level Three technical committees of the Lamfalussy procedure and a representative of the European Commission. It would be chaired by the president of the ECB, which would also supply the logistical structures and staff.

Three committees be strengthened by creating an appropriate legislative framework. The Economic and Financial Committee and the Committee on Financial Services were asked to study the proposals with a view to reaching a common solution to be submitted for discussion by the Ecofin meeting in June.

Procyclicality of financial systems. – The meeting endorsed the agreement reached at the 2 April meeting of the G20 on a range of actions to mitigate the procyclicality of financial systems by creating incentives for the formation during economic expansions of buffers of resources for use during recessions. At European level a number of regulatory options have been discussed. The Committee of European Banking Supervisors is preparing a proposal based on the possibilities for intervention offered by the second pillar of the Basel II capital adequacy scheme. The proposal is that European supervisors adopt a common, automatic rule to supplement banks' internally developed stress tests and allow assessment of the adequacy of banks' reserves of capital. The mechanism suggested is to adjust the probabilities of default estimated under the banks' internal models by a scaling factor to take account of the difference between the current cyclical conditions and those that would prevail during economic recessions. Automatic mechanisms are preferable to discretional instruments because they alleviate the possible external pressures on supervisors in times of market exuberance and eliminate the need to justify the employment of the reserves during recessions, when risk perception is greatly heightened.

National measures to support the financial system. – In the light of the European Commission's February communication on the treatment of impaired assets in the banking sector, the meeting paid special attention to the plans for action to sustain deteriorated bank assets, so as to avoid competitive disparities between member states. These plans attach special importance to the problem of asset valuation, and the meeting accordingly endorsed the G20 agreement to improve the accounting standards for valuation of financial assets by considering instruments' degree of liquidity and investors' time horizon. Specifically, in reaffirming the fair value standard the meeting emphasized that it is essential to make sure that the application of accounting standards does not accentuate the procyclical behaviour of financial intermediaries. With reference to the persistent difficulties of the financial industry, the meeting underscored the urgency of solving the problem of asset valuation when markets are in turmoil or inactive. In such phases market prices are a less significant measure of value. The Council accordingly asked the International Accounting Standards Board, whose standards the EU applies directly, to work together with the US Financial Accounting Standards Board to achieve uniform treatment and application of accounting standards. The Presidency invited the Commission to review the functioning of the 2002 Regulation on international accounting standards.

2.3 THE MAIN INDUSTRIAL AND EMERGING COUNTRIES

In the United States the contraction in economic activity has intensified

In the fourth quarter of 2008 the GDP of the United States fell at an annual rate of 6.3 per cent. The appreciable acceleration in the fall in output in relation to the third quarter was due to a sharp contraction in non-residential private fixed investment and exports; moreover, there were further reductions in both private consumption, which had begun to fall in the third quarter, and in residential investment, which has been in decline for three years. Economic activity probably continued to contract in the first few months of 2009; pointers in that direction are to be seen in the pronounced fall in exports in January and the decline in shipments of capital goods in January and February. Consumption picked up slightly on average over the first two months of the year in relation to the fourth quarter of 2008. Non-farm payroll employment, which had fallen by about 1,650,000 in the fourth quarter of 2008, declined by more than 2 million in the first three months of this year. In the OECD forecasting scenario, economic activity is expected to continue to contract throughout 2009, albeit at a gradually slowing pace, falling by 4.0 per cent on average during the year (Table 1).

Consumption is affected by the steep fall in net wealth and the reduced availability of bank credit

Households' spending decisions are being affected by the deterioration in the outlook for incomes, the steep fall in net wealth and the reduced availability of bank credit. By the end of December households' net worth had fallen to around 480 per cent of disposable personal income, about 50 percentage points less than at the end of September and 170 points below the peak recorded in June 2007 (Figure 9). Households have reacted by raising their saving rate, to 4.2 per cent in February. The tightening of credit conditions had already contributed to a reduction in the stock of consumer credit in the fourth quarter of 2008, the first such reduction in almost twenty years.

Firms increase their recourse to the bond markets

The retrenchment of corporate investment reflected mainly great uncertainty about the intensity and duration of the recession, but also the reduced availability of bank credit. The recovery in gross bond issues by non-financial corporations in the first three months of 2009 indicates that firms – especially those with a high credit rating – are able to turn to the bond markets to offset part of the effect of the drying-up of bank credit.

The crisis in the housing market persists but with signs of a possible easing

House prices in the ten largest cities, measured by the Case-Shiller index, continued to fall: in January they were 30.2 per cent below the peak of June 2006 (Figure 10), and futures prices imply that prices will not stabilize until 2011. Foreclosures initiated on residential mortgages decreased slightly, but were still running at a high level in the fourth quarter of 2008 (Figure 11). Signals have emerged in recent weeks which, if confirmed in the months to come, point to an easing of the crisis. The sharp drop in building licences in the second half of 2008 came to a halt in February; unlike the Case-Shiller, in January the Federal Housing Finance Agency's house price index showed an increase on the previous month. Lastly, although the number of transactions involving new houses has been unprecedentedly low in recent months too, the

Table 1

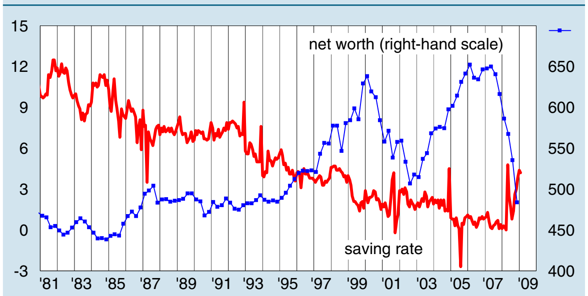
Selected macroeconomic projections
(percentage changes on the previous year)

		OECD		Consensus Economics	
	2008	2009	2010	2009	2010
GDP					
Advanced countries					
Euro area	0.8	-4.1	-0.3	-2.6	0.5
Japan	-0.6	-6.6	-0.5	-5.8	0.7
United Kingdom	0.7	-3.7	-0.2	-3.0	0.5
United States	1.1	-4.0	0.0	-2.8	1.7
Emerging countries					
Brazil	5.1	-0.3	3.8	-0.1	2.9
China	9.0	6.3	8.5	7.0	8.3
India (1)	6.0	4.3	5.8	5.2	7.8
Russia	5.6	-5.6	0.7	-1.5	2.5
Consumer prices					
Advanced countries					
Euro area	3.3	0.6	0.7	0.6	1.5
Japan	1.4	-1.2	-1.3	-1.1	-0.4
United Kingdom	3.6	2.0	1.7	1.0	1.8
United States	3.8	-0.4	0.5	-0.9	1.5
Emerging countries					
Brazil (2)	5.9	4.3	4.3	4.3	4.3
China	5.9	-1.0	-1.5	0.2	1.7
India (1)	8.8	4.5	3.0	5.3	5.3
Russia (2)	13.3	8.0	6.0	12.6	9.8
World trade (3)	2.5	-13.2	1.5	–	–

Sources: National statistics; *OECD Economic Outlook, Interim Report,* March 2009; Consensus Economics, March 2009.
(1) Changes in the course of the financial year, beginning in April of the year indicated and ending in March of the subsequent year; OECD forecasts for the 2008 financial year. – (2) Changes from December to December. – (3) OECD estimates for 2008.

Figure 9

Household saving rate and net worth (1)



Sources: Bureau of Economic Analysis and Federal Reserve.
(1) Net worth (quarterly end-of-period data) is expressed as a percentage of disposal personal income (moving average of 4 quarters ending in the quarter indicated). Seasonally adjusted monthly data for the saving rate.

stock of unsold new builds has decreased steadily and is now at the same level as before the crisis.

The slowdown in inflation comes to a halt

Inflation, as measured by the consumption deflator, fell in the second half of 2008 but remained almost unchanged in the first few months of 2009; in February it stood at 1 per cent, compared with 0.8 per cent in December. Excluding energy and food, the rate was 1.8 per cent, the same as in December. The Federal Reserve forecasts that the inflation rate will be between 0.3 and 1 per cent at the end of 2009.

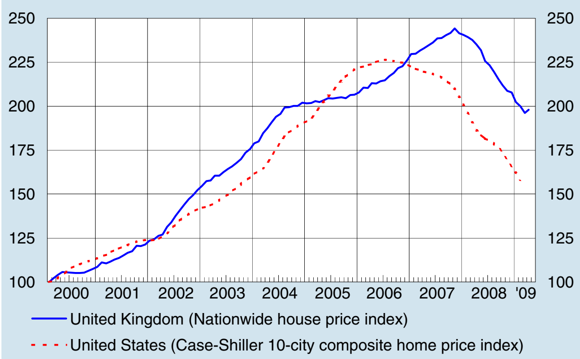
The Federal Reserve announces measures to influence long-term interest rates more directly

The Federal Reserve, which had already set a target range for the federal funds rate of between 0 and 0.25 per cent on 16 December, confirmed on 18 March that it intended to keep rates at this level for an extended period. Futures prices reveal expectations that policy rates will remain essentially unchanged throughout 2009. At the same time, in order to reinforce its action to support the economy, the Federal Reserve adopted measures to impinge more directly on long-term interest rates and, by that means, on borrowing conditions for firms and households. In particular, it formalized its intention to purchase up to $300 billion of longer-term Treasury bonds over the next six months; it also raised the limit on purchases of agency mortgage-backed securities from $500 billion to $1,250 billion (equal to just under 9 per cent of GDP), estimating that purchases made so far had helped reduce the cost of mortgages from 6 per cent in November to 5 per cent in February.

Figure 10

Real estate market: house prices

(indices, January 2000=100)

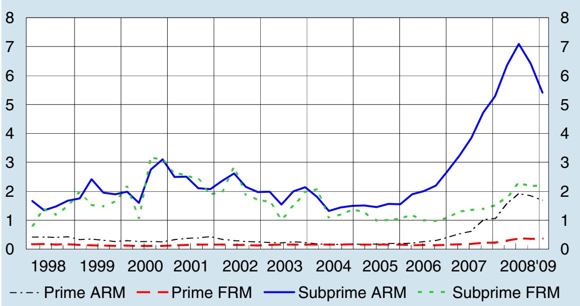


Source: Thomson Reuters Datastream.

Figure 11

Residential mortgages in the United States: foreclosures initiated as a proportion of outstanding mortgages, according to type of mortgage (1)

(seasonally adjusted quarterly data; percentages)



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

In Japan the contraction in economic activity intensifies

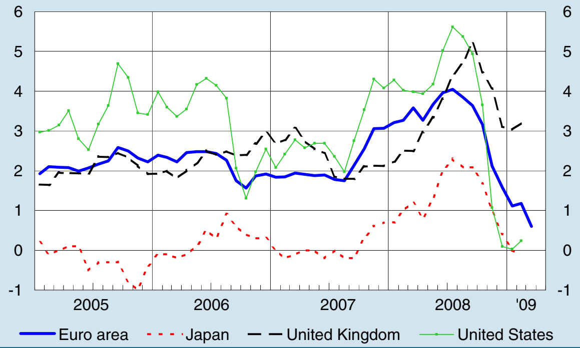
In Japan the decline in GDP that had begun in the second quarter of 2008 accelerated dramatically in the fourth quarter to an annual rate of 12.1 per cent owing to a worsening of the fall in investment and especially the collapse in exports. This was the consequence of the strong rise in the real effective exchange rate of the yen by about 25 per cent over the last seven months and the high proportion of exports from sectors that are particularly vulnerable to the reduced availability of credit in overseas markets, such as the automobile industry. Indications consistent with a continued rapid contraction in economic activity in the first quarter are to be seen in the large fall in industrial output in January and February and the marked deterioration in business confidence reported in the Tankan Survey. Consumer price inflation continued to fall, reaching zero in February (Figure 12).

The Bank of Japan, which had already reduced its reference rate to 0.1 per cent in the last few months of 2008, reacted to the worsening of the crisis by adopting measures to alleviate companies' funding difficulties; in particular, it purchased corporate bonds and commercial paper in the open market. In addition, in March the Bank announced that it was raising its annual planned purchases of government bonds by ¥4.8 trillion, equal to about 1 per cent of GDP.

Figure 12

Consumer price inflation (1)

(monthly data; twelve-month percentage changes)



Source: Thomson Reuters Datastream.
(1) For the euro area and the United Kingdom, harmonized consumer prices.

The Bank of England also adopts non-conventional monetary policies

In the United Kingdom as well the contraction in economic activity intensified in the fourth quarter of 2008, accelerating to an annual rate of 6.1 per cent, owing to a steeper fall in consumption and a large reduction in inventories. Consumption was affected by the fall in net financial wealth and a more pronounced reduction in lending to households. The Credit Conditions Survey published by the Bank of England on 2 April reported expectations of a small improvement in the availability of credit to households and firms in the second quarter. The first hesitant signs that house prices were stabilizing emerged in recent months; in March they were about 19 per cent below the peak of October 2007. The Bank of England tackled the deepening of the crisis by reducing its monetary policy rate by a total of 100 basis points in February and March. Judging that a strategy relying solely on adjustments in monetary policy rates – which now stand at 0.5 per cent – was insufficient to achieve the Bank's medium-term inflation target, at the beginning of March the Bank announced its intention to purchase gilts and private sector securities, including corporate bonds and commercial paper, totalling £75 billion (about 5 per cent of GDP) between March and May by creating monetary base. Consumer price inflation, which had reached 5.2 per cent last September, steadily declined to 3 per cent in January; in February it rose again to 3.2 per cent.

The crisis afflicts the main emerging economies in different ways ...

The significant weakening of the emerging economies in the last few months continues to be due mainly to the fall in world demand and the decrease in inflows of foreign capital, which can be ascribed partly to the reduction in lending by the international banking system in the throes of reducing its financial leverage. Growth forecasts for the emerging economies have been revised downwards. According to the latest assessments by the OECD, China and India are likely to expand by 6.3 and 4.3 per cent respectively in 2009, Brazil will essentially stagnate (-0.3 per cent) and Russia will suffer a contraction of 5.6 per cent. The continuation of positive growth in China and India rests on their lower reliance on flows of bank credit and, in the case of China, on the adoption of more actively countercyclical monetary and fiscal policies. In Russia, and to a lesser extent in Brazil, economic activity is being affected by the deterioration in the terms of trade due to the collapse in commodity prices.

... especially some economies in Central and Eastern Europe

The economies of Central and Eastern Europe are among the emerging economies worst affected by the crisis. They are suffering from a fall in demand from the euro area and greater sensitivity to the outflow of foreign capital, since in the recent past they adopted a model of development that relied heavily on external finance to sustain the growth in domestic demand. In March Romania had to seek financial support from international organizations; Hungary and Latvia had already done so in late 2008. Banking systems have also proved to be highly vulnerable, and will require substantial recapitalization. On 26 March, following a meeting with a number of international financial institutions, nine large European banks which account for about 70 per cent of the Romanian banking system stated their interest in maintaining their exposure to Romania and undertook to recapitalize their Romanian subsidiaries if that proved necessary.

Important signs emerge of a reduction in international trade imbalances

The precipitous fall in the price of oil was a significant factor in the reduction in global balance-of-payments disequilibria in the fourth quarter of 2008. In particular, the decrease in the United States' current account deficit from 5 per cent of GDP in the third quarter to 3.7 per cent in the fourth was almost entirely due to that in the energy deficit. The contraction in Japan's current account surplus from 3 to 1.8 per cent of GDP, on the other hand, appears to be attributable to the real appreciation of the yen and the particular sensitivity of Japanese exports to the fall in world demand. No signs have yet emerged of a decline in China's surplus.

2.4 THE EURO AREA

The recession worsened in late 2008 ...

The GDP of the euro area grew by 0.8 per cent in 2008, compared with 2.6 per cent in 2007. The economic climate deteriorated abruptly during the year: in the last quarter GDP fell by 1.6 per cent in relation to the preceding period, the largest variation in the existence of the monetary union. The breadth and depth of the global crisis were reflected in a sharp fall in exports in the fourth quarter (-6.7 per cent), causing a decline in industrial output; the value added of services also fell slightly. Domestic demand contracted, especially in gross fixed investment (-4.0 per cent). Despite the substantial fall in inflation, household consumption decreased by 0.3 per cent, hit by the deterioration in the labour market and spreading uncertainty about the duration and intensity of the recession. The build-up of stocks of finished products intensified; on the basis of survey results, at the end of last year inventories were substantially higher than normal. Among the major countries of the area, the contraction in economic activity in the fourth quarter of 2008 was particularly pronounced in Germany (-2.1 per cent in relation to the third quarter, the worst result since reunification) and Italy (-1.9 per cent), but less marked in France (-1.1 per cent), as household consumption held up.

... and continues in the first few months of 2009

The economic indicators point to a further slowdown in activity in the first few months of this year comparable to that observed in the final quarter of 2008. The index of industrial production for the area, adjusted for the number of working days and seasonal factors, continued to decline in January (-3.0 per cent in relation to the preceding quarter) after having fallen abruptly in the preceding three months (-6.0 per cent on average in the fourth quarter of 2008); our estimates indicate that activity contracted again in February. The economic surveys by the European Commission in March recorded a further deterioration in business confidence; however, the findings of interviews with purchasing managers conducted in that month (Purchasing Managers Index) reveal slightly less negative assessments of the short-term outlook. The €-coin indicator, which provides a synthesis of all the available economic data adjusted for short-term fluctuations, after indicating that the downward trend under way for about two years intensified in February (-0.6 per cent) stopped falling in March (Figure 13).

The downward revision of the area's growth prospects, at a time of substantial idle capacity and strained financial conditions, is likely to bear down on firms' investment plans. The contraction in household consumption is expected to be mitigated by the fall in inflation and the implementation of the incentives introduced by major countries for the purchase of motor vehicles, which were at the root of a recovery in vehicle registrations from February onwards. Looking ahead, however, consumers' spending plans may be affected by the deterioration in the labour market and the decrease in wealth due to the steep fall in stock prices and, in some countries, in the prices of residential property.

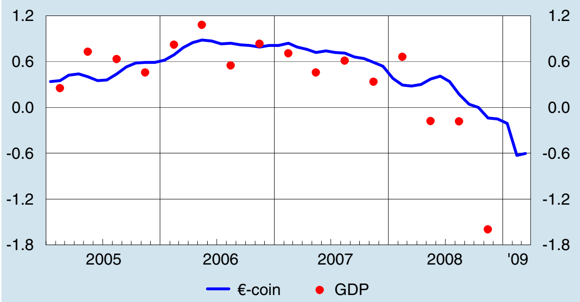
Growth forecasts have been adjusted downwards

The GDP forecasts for the area from the main international organizations and those from analysts interviewed by Consensus Economics were revised sharply downwards at the beginning of the year (Table 2). The staff estimates by the European Central Bank (ECB) published at the beginning of March point to a variation in activity of between -3.2 and -2.2 per cent on average this year and between -0.7 and +0.7 per cent in 2010; the estimates published by the OECD at the end of that month foresee a particularly sharp fall in world trade and a larger contraction in GDP (-4.1 per cent), which is expected to extend into 2010 as well (-0.3 per cent).

Figure 13

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

(percentage changes)



Sources: Eurostat and based on Thomson Reuters 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, October 2007. For GDP, quarterly data; change in relation to the preceding quarter. For €-coin, monthly data; change over three months.

Annual inflation falls below 1 per cent

The fall in inflation in the euro area on a twelve-month basis intensified at the beginning of this year. According to provisional Eurostat data, the harmonized index of consumer prices rose by 0.6 per cent in March, compared with 2.3 per cent in the fourth quarter of 2008. The three-month variations in the index, on a seasonally adjusted annual basis, which had been negative since last autumn owing to the exceptional fall in energy prices, turned slightly positive again in March as oil prices stabilized (Figure 14). The fall in inflation gradually spread to the core components – non-food and non-energy consumer goods and services – although there is no evidence of large and widespread price reductions. The seasonally adjusted three-month variations in the index for these items are still positive, although at an annual rate of around 1 per cent they are only just above half those recorded for a good part of 2008. Core inflation may continue to fall in the coming months; pointers to that effect as regards the goods component are to be seen in the slowdown in the rise in the producer prices of non-food and non-energy goods for final consumption to around 0.5 per cent in February. On the cost side, the decline in the dollar prices of non-energy raw materials and oil came to a halt in the first few months of this year; according to available data, the rise in unit labour costs for the economy as a whole accelerated further in late 2008 owing to a fall in labour productivity.

Table 2

Forecasts of the growth in euro-area GDP (1)

(percentage changes on preceding year)

	IMF	OECD	European Commission	Consensus Economics
For 2009				
Q1 2008	1.2	–	–	1.8
Q2 2008		1.4	1.5	1.4
Q3 2008	1.2	–	–	0.9
Q4 2008	-0.5	-0.6	0.1	-0.9
Q1 2009	-3.2	-4.1	-1.9	-2.6
For 2010				
Q4 2008	0.2	1.2	0.9	–
Q1 2009	0.1	-0.3	0.4	0.5

Sources: European Commission, IMF, OECD and Consensus Economics.
(1) Forecasts for the average of the year indicated, published in one of the months of the reference quarter; for the forecasts collated by Consensus Economics, the expectations expressed in the last month of each quarter are reported.

Forecasters do not see the fall in inflation turning into deflation

The professional forecasters interviewed in mid-March by Consensus Economics revised their inflation expectations sharply downwards by comparison with the opinions expressed at the end of 2008; according to the new assessments, however, it will not come to a general and lasting fall in consumer prices. They expect the pronounced slowdown in prices to be confined to 2009 (0.6 per cent on an annual average basis, against an expectation of 1.4 per cent in December). During the summer the twelve-month inflation rate may temporarily turn negative owing to the statistical comparison with the same period of last year, which was affected by the soaring increases in food and energy prices. The average inflation rate for the euro area is expected to rise to an annual average of 1.5 per cent in 2010, on the assumption that the economy will gradually come out of the current recession. The ECB staff estimates published at the beginning of March were also revised downwards significantly and foresee a barely positive annual average variation in prices this year (between 0.1 and 0.7 per cent) and a pick-up in 2010 (between 0.6 and 1.4 per cent).

Money supply and credit growth continue to slow

Bank lending to the private sector in the euro area slowed further from November onwards, to 5.9 per cent in the twelve months ending in February and taking account of the accounting effect of securitization operations. Lending has essentially stagnated in the last three months. The slowdown was evident in all the main branches of economic activity and across the various types of lending; it reflected primarily the weakness of activity and the deterioration in the outlook for the real estate market. Replies to the Bank Lending Survey carried out by the Eurosystem in January indicate that supply factors probably also played a part. The rate of growth in the M3 aggregate fell to 5.9 per cent in February owing to the slowdown in the less liquid components and, in particular, the deposits of non-financial corporations.

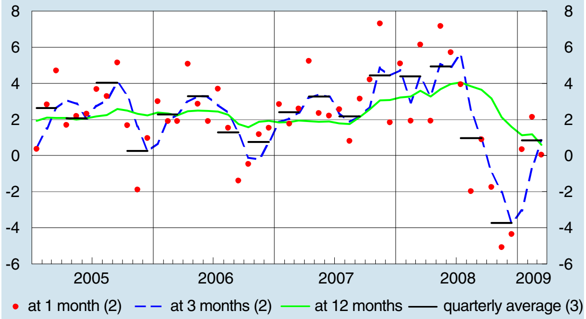
The ECB has further reduced official rates

Confirmation of the sharp slowdown in prices and the further deterioration in economic prospects prompted the ECB to continue with the policy of reducing official rates initiated last autumn; it made two cuts of 50 basis points (on 15 January and 5 March) and a further one of 25 basis points (on 2 April), bringing the rate on the main refinancing operations down to 1.25 per cent (Figure 15). The markets continue to repute the Eurosystem's monetary policy credible; this is borne out by the indicators of long-term inflation expectations which, excluding inflation risk premia, remain compatible with the objective of

Figure 14

Harmonized index of consumer prices in the euro area (1)

(percentage changes)

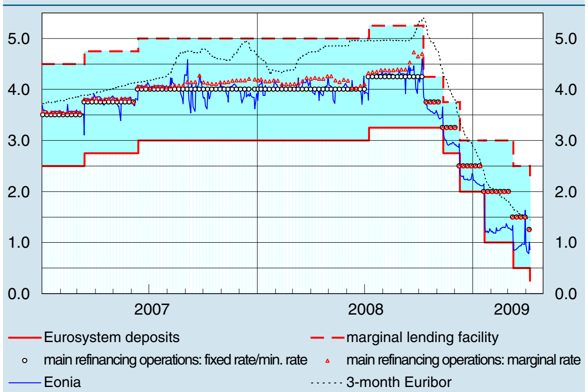


Sources: Based on Eurostat and ECB data.
(1) Provisional data for March. – (2) On a seasonally adjusted and annual basis. – (3) Average, in the reference quarter, of monthly growth rates, on a seasonally adjusted and annual basis.

Figure 15

Official interest rates and money and financial market rates in the euro area

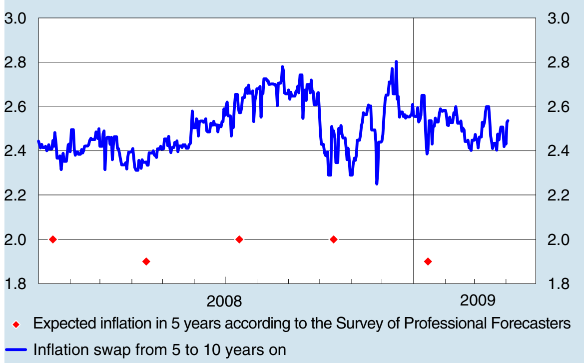
(daily data; percentages)



Sources: ECB, Thomson Reuters Datastream.

Figure 16

Long-term inflation expectations in the euro area



Sources: Based on ECB, Bloomberg and Bank of Italy data.

price stability (Figure 16). The ECB is also continuing to provide ample liquidity to the banking system at fixed rates, with demand being met in full, and has confirmed that the arrangements will remain in force until the end of 2009. The widening of the interest rate corridor back to 200 basis points, which was announced in December, came into operation on 21 January. The banks reduced both their demand for longer-term liquidity and recourse to the deposit facility at the ECB; the volume of transactions on the interbank overnight market increased slightly. The differentials between rates on unsecured loans (Euribor) and their secured equivalents (Eurepo), which provide a measure of the risk premium on the interbank market, showed a further gradual decline, though remaining high: the differential on three-month contracts fell under 70 basis points, about 30 below the level of mid-January.

3 THE ITALIAN ECONOMY

3.1 THE CYCLICAL SITUATION

GDP has been falling for a year now ...

In 2008, alone among the leading euro-area countries, Italy's economy contracted by 1.0 per cent following growth of 1.6 per cent in 2007 (Figure 17). During the year, the decline in GDP growth, which began in the spring, worsened as tensions heightened in the financial markets. There was a marked decline in the fourth quarter of 2008 when GDP fell by 1.9 per cent from the preceding period, the worst decline since the 1974-75 recession (Table 3). The deepening international crisis caused a sharp reduction in exports, by 7.4 per cent in the last three months of 2008, and in investments, especially in machinery, equipment and transport equipment (-8.9 per cent). Household consumption also fell, by about 1.0 per cent. As in the rest of the euro area, the recession continued into the early months of this year. Over the first two months, according to the information available, export sales were still very weak. The deterioration of the outlook for world growth and the uncertainty about the timing of the recovery are making firms more pessimistic and discouraging investment. Households are still very cautious in their spending decisions, reflecting fears of a further worsening of conditions in the labour market.

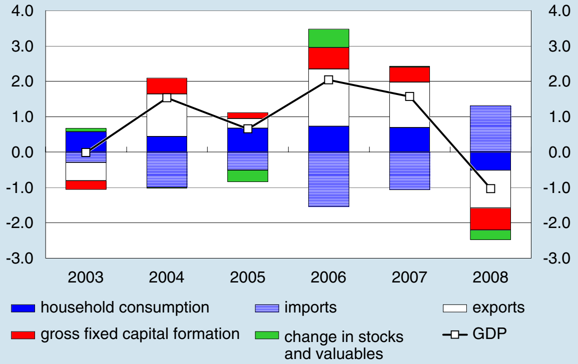
... and the outlook for 2009 is deteriorating

The available economic indicators foreshadow a pronounced decline in economic activity in the first quarter of this year, for the fourth time running, about the same as in the previous quarter. In the recessions of 1974-75 and 1992-93, exports rapidly relaunched the economy thanks, respectively, to the fast recovery of world trade and the devaluation of the currency. The global nature of the present recession makes uncertain the timing of a return to a growth path, which according to the main international organizations and private forecasters, may only

Figure 17

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 on the Istat website: www.istat.it.

Table 3

GDP and its main components

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

	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2008 (1)
GDP	0.3	-0.6	-0.7	-1.9	-1.0
Total imports	-1.2	-1.1	-0.7	-6.0	-4.5
National demand (2)	..	-0.7	-0.2	-1.5	-1.3
National consumption	-0.1	-0.4	0.2	-0.6	-0.5
households	*-0.1*	*-0.8*	*0.2*	*-0.8*	*-0.9*
other (3)	..	*0.5*	*0.1*	..	*0.6*
Gross fixed capital formation	-0.3	-0.5	-1.8	-6.9	-3.0
construction	*0.6*	*-1.1*	*-0.4*	*-5.1*	*-1.8*
other goods	*-1.1*	*0.1*	*-3.2*	*-8.9*	*-4.2*
Changes in stocks and valuables (4)	0.2	-0.2	0.1	0.4	-0.3
Total exports	-0.2	-1.0	-2.4	-7.4	-3.7

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.

begin next year. The analysts interviewed in mid-March by Consensus Economics expect an average contraction of economic activity of 2.8 per cent this year (with downside risks) and barely positive growth (0.3 per cent) in 2010. OECD forecasts published at the end of March indicate a fall of 4.3 per cent in 2009 (assuming an unprecedented reduction in world trade) and of 0.4 per cent in 2010.

The deepening of the recession can be seen in the reduction in the number of the employed, which fell by 0.1 per cent in the fourth quarter of 2008 compared with the previous period, adjusted for seasonal factors (-0.5 per cent in industry excluding construction). The contraction was more marked in terms of standard labour units. In the first few months of 2009, the evident increase in the number of applications for unemployment benefit made to INPS and the hours authorized by the ordinary Wage Supplementation Fund signals a further deterioration in labour market conditions.

Inflation is falling more rapidly

In 2008 as a whole, the consumer price index for the entire resident population rose by 3.3 per cent, compared with 1.8 per cent in 2007. The rapid decline in inflation in the last part of 2008, driven by sharp falls in the prices of raw materials, continued at the beginning of this year; the rate fell to 1.2 per cent in March, with the trend expected to gain strength until next summer. The slowing of price increases is gradually spreading to the core components of the consumer and producer price indices. In Italy, as in the rest of the euro area, the expectations of the analysts interviewed in March by *Consensus Economics* do not suggest that the process will turn into to deflation, assuming that cyclical recovery will begin next year: on average in 2009 the growth in prices is expected to be 0.9 per cent, rising to 1.6 per cent in 2010.

3.2 FIRMS

Industrial production is falling ...

In the fourth quarter of 2008 the index of industrial production, adjusted for seasonal and calendar effects, fell by 8.1 per cent from the third quarter (Figure 18). With the sole exception of the autumn of 1969, this was the worst quarterly result since the Second World War. For 2008 as a whole, production fell by 3.1 per cent. The trend continued in the first part of the new year. In the first two months activity fell by an average of about 5 per cent with respect to the preceding period, and our estimates for March based on electricity consumption indicate a further decline. Most industrial sectors are in difficulty. The proportion of sectors in which activity has contracted for at least two consecutive quarters is well above that registered in the recession of the early 1990s and not far below the historic peak of 1975. The automobile industry, one of the hardest hit, could rebound partially in the coming months thanks to the introduction of incentives for the purchase of ecological vehicles (from mid-February through the rest of the year), which caused an upswing in new car registrations starting in February and a substantial rise in new orders to dealers.

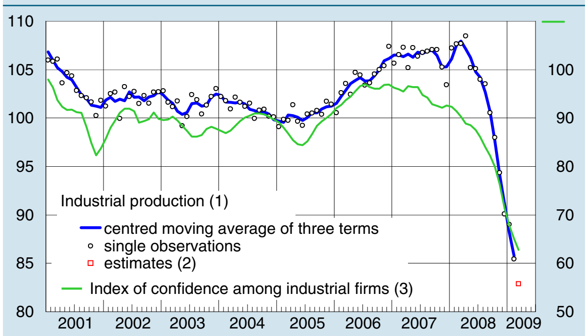
... and firms remain pessimistic on the short-run outlook

Firms are still pessimistic. Their assessments of the level of orders, both domestic and export, have worsened further (Figure 19), as have their short-term output expectations. On the other hand, on average for the first quarter the number of firms reporting that their inventories were higher than

Figure 18

Industrial production and index of business confidence

(monthly data)

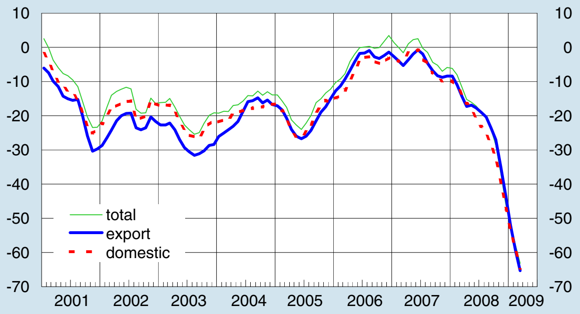


Sources: Based on ISAE, Istat and Terna data.
(1) Adjusted for seasonal and calendar effects; index: 2005=100. – (2) Based on electricity consumption and the indicators of ISAE surveys of industrial firms. – (3) Average of the seasonally adjusted percentage balances of the responses to questions regarding the level of demand, production expectations and stocks of finished products; index: 2000=100; moving average of three terms (right-hand scale).

normal decreased slightly. According to the quarterly survey conducted in the first 20 days of March by the Bank of Italy and *Il Sole 24 Ore*, 88 per cent of the respondent firms found the overall economic situation to be deteriorating with respect to the previous quarter. However, a comparison with the previous survey shows some initial signs of an attenuation of pessimism on the short-term outlook, although expectations remain negative for the majority of firms.

Figure 19

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.

Investment has been affected by uncertainty ...

The contraction in businesses' gross fixed investment worsened significantly from 1.8 per cent in the third quarter to 6.9 per cent in the fourth (and to 8.9 per cent for machinery, equipment and transport equipment). Uncertainty over the timing of the recovery, idle capacity at historic high levels and financial strains underlie the very poor prospects for investment this year. Some signals of this come from the survey of machine tool orders by the Italian association of machine tool makers towards the end of 2008. And the quarterly Bank of Italy-*Il Sole 24 Ore* survey in March found that 56 per cent of firms considered that investment conditions had worsened in the last three months, while 12 per cent saw an improvement. Even so, the gap between negative and positive judgments was narrower than in December, and more markedly so in industry than in services.

... including construction investment ...

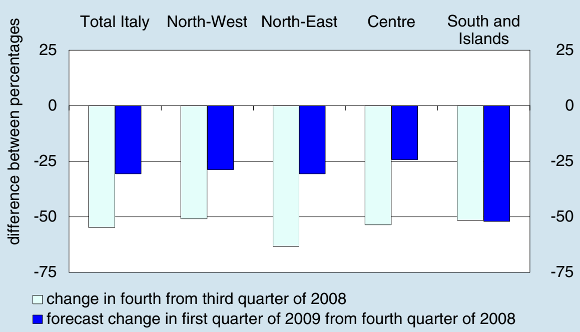
The investment decline in construction intensified in the fourth quarter, with a contraction of 5.1 per cent from the third. The situation looked likely to remain difficult in the first few months of 2009. In January and February business confidence in the construction industry fluctuated around its lowest level in a decade.

... as the Bank of Italy-Tecnoborsa survey confirms

In residential building, according to a new quarterly survey conducted jointly by the Bank of Italy and Tecnoborsa between 12 January and 13 February, 77 per cent of a representative sample of real estate agents expect unfavourable conditions to prevail in the market in which they do business in the first quarter of 2009. Over a longer time frame (2009-2010) and with reference to the entire national market, 45 per cent expect an improvement, against 34 per cent who foresee a further deterioration. By comparison with the most recent quantitative data (available half-yearly), which showed a slight rise in prices for the second half of 2008, the new survey provides the first sign of a decline in house prices in the fourth quarter; 58 per cent of the agents gave a negative evaluation of price trends in the fourth quarter, while just 3 per cent reported an increase. In the expectations for the first quarter of 2009 the negative balance

Figure 20

Evaluation of price trends in the Italian real estate market (1)
(balance between percentages of positive and negative assessments of price trends in the respondent's market)



Sources: Based on Bank of Italy and Tecnoborsa data.
(1) Real estate agencies that reported making sales in the fourth quarter, weighted by total number of agencies taken from Istat-ASIA files (2006). For details, see "*Sondaggio congiunturale sul mercato delle abitazioni in Italia*", *Supplementi al Bollettino Statistico*, vol. XIX, no. 15, 23 March 2009.

between "rising" and "falling" responses narrowed to 31 points (Figure 20). Over half the agents responding reported that late in the year the average time it took to sell a house had increased since the summer (to about seven months), and only 11 per cent said it had decreased.

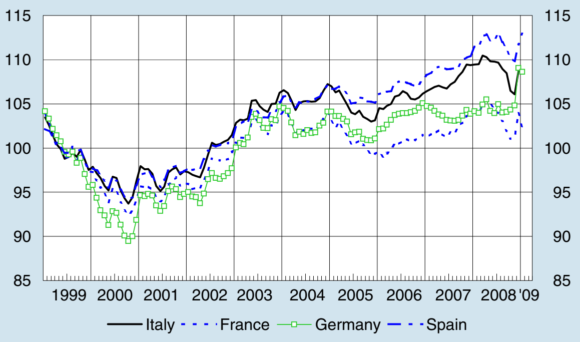
Competitiveness deteriorates slightly

First-quarter estimates of Italian competitiveness calculated with reference to producer prices indicate that firms' gains in competitiveness between the spring and the autumn of 2008 were mostly wiped out between November and March by the euro's nominal effective appreciation of more than 5 per cent against the other main currencies (Figure 21).

Figure 21

Indicators of competitiveness based on producer prices of manufactures (1)

(monthly indices, 1999=100)



Sources: Based on IMF, OECD and Eurostat data.
(1) In relation to 61 competitor countries; latest available data refer to January 2009; an increase in the index indicates a loss of competitiveness.

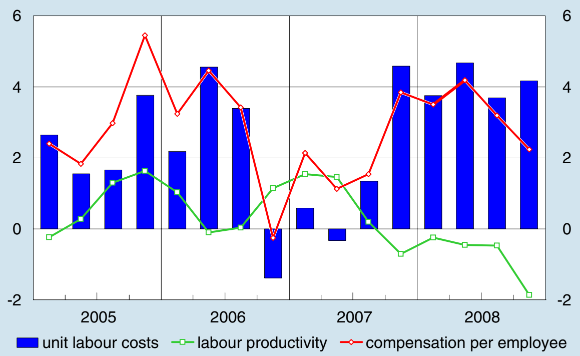
The sharp acceleration in unit labour costs in 2008 was due to transitory factors

According to the national accounts, unit labour costs in the whole economy rose by 4 per cent on average in 2008, compared with 1.4 per cent in 2007. This substantial increase was due to the last major round of labour contract renewals, which produced per capita wage gains of 3.3 per cent for the year as a whole, up from 2.2 per cent in 2007, and to the marked deterioration in productivity, which after the 0.7 per cent gain of 2007 fell by 0.8 per cent, reflecting a decline in value added and broadly stable employment (Figure 22). This year, however, there should be a marked deceleration in unit labour costs as the impact of contract renewals fades away against the backdrop of a weak labour market. As always, together with the national accounts for 2008 Istat released the revised accounts for the three previous years. In particular, the revised data show faster growth in value added in industry excluding construction in 2006-07, more closely in line with the sector's employment growth. The consequent revision of labour productivity growth by about 2 percentage points in 2006 and 1 point in 2007 curtailed the loss of competitiveness as measured by the index based on unit labour costs; the rise in this indicator was revised downward from 2.5 per cent in each of the two years to 0.6 and 1.8 per cent, respectively.

Figure 22

Labour costs and productivity in the economy as a whole

(twelve-month percentage changes)



Source: Based on Istat data.

Corporate profitability continues to worsen ...

Estimates based on the national accounts indicate that the downward trend in firms' operating profit, underway since 2004 and steepening in 2008, intensified further in the fourth quarter. Corporate self-financing continued to shrink, owing in part to the increase in net financial costs. Self-financing fell below 10 per cent of value added, the lowest ratio in fifteen years.

... and firms' borrowing requirement rises

The reduction in self-financing was more pronounced than that in investment, so the borrowing requirement (defined as the difference between gross investment, including stocks, and self-financing) rose sharply, especially in the second half of the year. Owing in part to the contraction in output, at the end of the year the financial debt of firms came to 76.2 per cent of GDP, about a percentage point higher than at the end of the third quarter. By comparison with 2007, corporate debt increased by more than 3 percentage points in relation to GDP (Figure 23), but the ratio is nevertheless significantly below the euro-area average of 94 per cent.

Bank debt growth slows down

The rate of growth in firms' debt to banks, which had continued high over the first three quarters, fell significantly in the fourth, to an annual rate of 7 per cent in December (Figure 24). The slowdown involved all sizes of firms and all parts of the country. In February bank lending to small firms remained practically flat. With the slackening of economic activity, there was also an abrupt slowdown in lending against the transfer of trade credits. Lateness of payment on these credits increased considerably over the previous year.

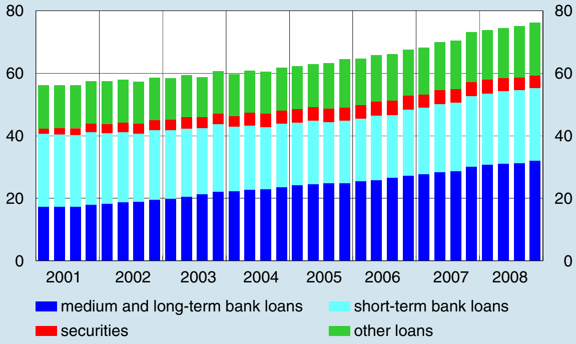
Fund-raising on the market is restricted to bond issues

Net bond issues by Italian non-financial firms came to some €2 billion in the fourth quarter, an increase with respect to the third. In the first half of the year there had been net redemptions of more than €1.5 billion. In the early months of 2009, according to Dealogic data (available only for gross issues), there were substantial placements by ENI and Telecom Italia totalling €3 billion. Capital increases on the Italian stock exchange amounted to €1.5 billion in the fourth quarter. In the first part of 2009, not counting a €3 billion issue by the Unicredit group, they came to a halt. Mergers and acquisitions remained rare and small in size. Thomson Reuters reports that 23 M&A transactions were announced in the fourth quarter for a total value of €1.6 billion, and in the first part of the new year this activity diminished still further.

Figure 23

Corporate debt (1)

(as a percentage of GDP)

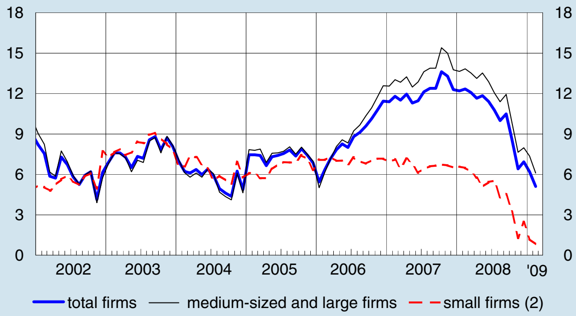


Sources: Based on Bank of Italy and Istat data.
(1) The figures for the fourth quarter of 2008 are provisional.

Figure 24

Bank lending to firms by size of firm (1)

(monthly data; twelve-month percentage changes)



(1) Adjusted for the accounting effect of securitizations. Loans exclude repos, bad debts and other minor items included in the Eurosystem harmonized definition of the aggregate. The data are also adjusted for 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

Household spending declines, including on non-durable goods...

In the fourth quarter of 2008, household consumption fell by 0.8 per cent on the previous period, decreasing in all the main components except services, which stagnated. In 2008 the fall averaged 0.9 per cent, compared with an increase of 1.2 per cent in the previous year (Figure 25). This contraction mainly reflected the drop in spending on durable goods (equal to around 7 per cent based on the quarterly accounts), which was joined by a slight decline in spending on non-durable goods, food especially. The latter is part of a downward trend already under way, and is an even more serious development than in the recession of the early 1990s. Factors in these developments were the sharp increases in prices during 2008 and the decline in real disposable income.

... as does real disposable income

By our estimates, based on data that are still largely incomplete, households' real disposable income fell slightly less than consumption in 2008. Compared with the substantial stagnation in the first nine months, as reported in the previous issue of the *Economic Bulletin* in January, the fall-off reflects both a significant downward revision made by Istat to the growth in salaried employment income on the occasion of its recent update of the quarterly national accounts and the sharp deterioration in the economic situation during the last part of the year, with a drop in payroll labour units and a more marked decline in self-employment. Weak consumer spending was further compounded by the effects of falling share prices on the value of financial assets held by households.

The outlook for 2009 is uncertain

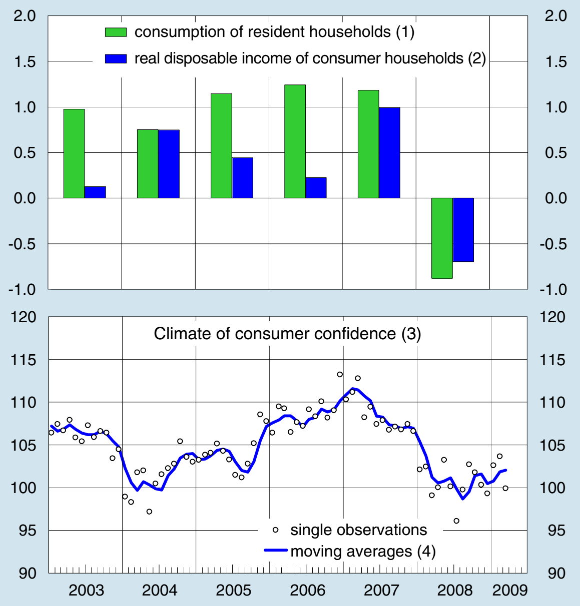
Following the slight improvement in the first two months of 2008, the ISAE survey in March reported a new slide in household confidence. Despite the positive effects on households' budgets and prospects for saving produced by the rapid fall in inflation and in interest rates, judgments on the overall economic situation deteriorated. In particular, there are growing concerns over employment: between June 2008 and March 2009 the percentage of households that expect unemployment to increase in the coming months rose by around 45 percentage points, to 80 per cent, in line with the record high during the recession of the early 1990s. The launch in February of incentives to support durable goods consumption should ease the markedly negative trend underway since the start of 2008; automobile orders, picking up strongly, point in this direction. In January the retail sales index recorded a slight recovery.

Household debt falls and the rise in debt servicing slows

Italian households' debt fell last year from 49.9 per cent of disposable income in the fourth quarter of 2007 to 49.4 per cent in the fourth quarter of 2008 (Figure 26). The ratio remains very low by international

Figure 25

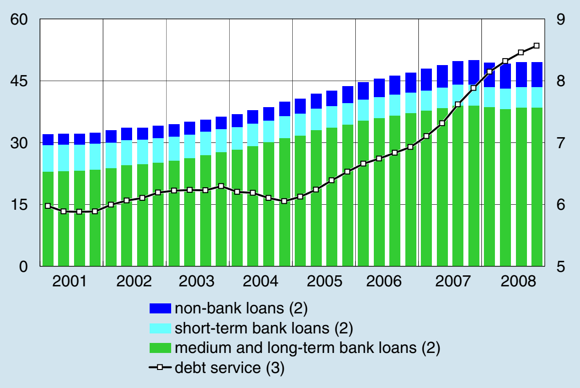
Household consumption and income and consumer confidence in Italy
(percentage change on previous year; indices)



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

Figure 26

Household debt (1)
(as a percentage of gross disposable income)



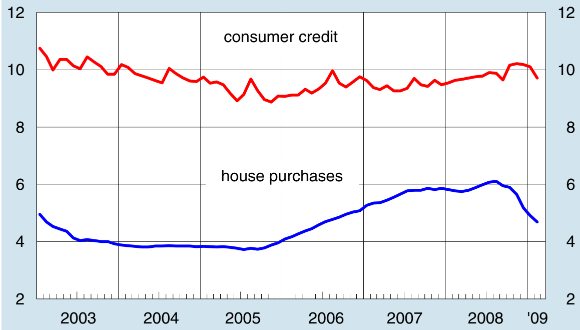
Sources: Based on Bank of Italy and Istat data.
(1) Disposable income for 2008 is estimated on the basis of quarterly national accounts data. Data on loans in 2008 are provisional. – (2) End-of-period stocks. – (3) Right-hand scale. Refers only to consumer households and to the twelve months ending in 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.

standards, around half the euro-area average and just one third of the level recorded in the United States and the United Kingdom. Households' debt servicing costs (interest and principal) continued to rise, but at a slower rate, to 8.6 per cent of disposable income at the end of the year. Two thirds of the increase was due to larger repayments of principal and the remainder to interest. However, between late 2008 and early 2009 the interest rates on mortgage loans dropped significantly (Figure 27), dragging debt servicing costs down, with an effect that will become clear in the course of the year.

Figure 27

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.

3.4 FOREIGN DEMAND AND THE BALANCE OF PAYMENTS

In 2008 exports declined...

Exports of goods and services in volume terms declined by 3.7 per cent in 2008. In the course of the year the intensifying fall-off was greater than the contraction of demand in Italy's main outlet markets, partly owing to the delayed effects of the appreciation in the real exchange rate between early 2006 and spring 2008. The fall in sales intensified sharply in the fourth quarter (-7.4 per cent on the previous period), especially for intermediate goods, corresponding to a significant contraction in demand. The overall reduction in the exports of goods last year was due almost entirely to sales in European Union countries, while exports to non-EU countries held substantially stable. In the fourth quarter the difficulties extended to every major outlet market. In 2008 all the manufacturing industries, except food products, contributed to the contraction in exports, especially traditional Italian products and the machinery and mechanical equipment sector, reflecting weakening global demand for investment goods after the growth of the previous two years.

...less than imports

The reduction in total imports in volume terms (-4.5 per cent) exceeded that in exports; the decline was concentrated in the goods sector (-5.4 per cent), which weakened markedly in the last quarter of the year, falling 7.4 per cent from the third quarter. Purchases of goods from the EU accounted for around half of the overall reduction in import volumes in 2008, owing in particular to the slump in demand for new automobiles in Italy.

In 2009 trade continues to decline in value terms

The data on foreign trade in the first two months of the year point to a further contraction in both exports and imports in value terms.

The current deficit increases, mainly due to net income

In 2008 the deficit on the current account of the balance of payments rose to €53 billion (3.4 per cent of GDP; Table 4), from €37.3 billion (2.4 per cent of GDP) in 2007. The trade balance worsened only slightly and was basically in equilibrium (€0.2 billion). The strong increase in the surplus on non-energy products substantially offset the greater energy deficit, which rose by €12.4 billion compared with 2007 to €57.1 billion. The widening deficit on the income account, which reached €28.7 billion or 1.8 per cent of GDP in 2008, accounted for over half the overall current account deterioration; it mainly reflected the effect, on a growing net debtor position, of the increase in the first nine months of the year in interest rates paid on liabilities: outward interest payments on Italian government securities and on the foreign funding of banks increased. At the end of September 2008 the net international investment debtor position was equal to 8.6 per cent of GDP. The deficit on services grew again, to €8.6 billion, especially within the transport sector, whose structural deficit was aggravated by the increase in the average price of oil in 2008 and the troubles of Alitalia. In January the current deficit remained at the levels of the previous year, despite the contraction of the energy deficit.

The equity component in the foreign portfolios of Italians is shrinking

In 2008, both Italian direct investment abroad and foreign direct investment in Italy slowed considerably compared with 2007; there was a net outflow of €21.4 billion. Portfolio investment registered historically high net inflows (€122.6 billion), reflecting large-scale disposals by residents of foreign equities and investment fund units, in a context of plunging share prices on stock exchanges the world over. The disposals began in mid-2007 and accelerated in the last part of 2008, reaching €85.9 billion for the year, equal to around 22 per cent of the stock of foreign portfolio equity at the end of 2007 and slightly exceeding purchases in the entire period between 2001 and 2006. Given that the share of government securities in external liabilities is structurally much larger than in assets, the general "flight" to government bonds throughout the world has favoured net portfolio inflows into Italy, with net purchases of government securities (in particular of BOTs and BTPs) by foreign investors equal to €86.3 billion in the first eleven months of the year.

Table 4

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

	2007	2008	Jan. 2008	Jan. 2009
Current account	**-37.3**	**-53.0**	**-6.7**	**-7.2**
Goods	3.2	0.2	-3.3	-3.1
non-energy products (2)	*47.9*	*57.3*	*1.6*	*0.8*
energy products (2)	*-44.7*	*-57.1*	*-4.9*	*-3.9*
Services	-7.0	-8.6	-1.1	-1.4
Income	-19.7	-28.7	-1.4	-2.2
Current transfers	-13.9	-15.8	-0.9	-0.5
Capital account	**2.8**	**2.4**	**0.4**	**0.3**
Financial account	**26.1**	**45.0**	**4.9**	**4.0**
Direct investment	-37.0	-21.4	0.2	-0.6
Portfolio investment	18.1	122.6	21.3	19.0
Financial derivatives	0.4	6.8	-0.1	..
Other investment	46.1	-57.5	-15.7	-14.6
Change in official reserves	-1.5	-5.6	-0.8	0.1
Errors and omissions	**8.4**	**5.6**	**1.4**	**2.9**

(1) Provisional data for December 2008 and January 2009. – (2) Based on Istat data on foreign trade.

3.5 THE LABOUR MARKET

Labour input and employment are falling

According to the national accounts, the number of people in employment in the fourth quarter of 2008 (seasonally adjusted) declined by 0.1 per cent with respect to the preceding period – and by 0.5 per cent in non-construction industry – following the trend under way since the summer. The labour input, measured by standard labour units, fell more sharply, by 0.4 per cent overall and by 1 per cent in industry excluding construction, partly owing to the increase in use of the Wage Supplementation Fund.

The progressive worsening of conditions on the labour market is borne out by the results of Istat's labour force survey. This shows a 1.1 per cent decline, seasonally adjusted, in employment between the third and fourth quarters of 2008 in the South, while the North recorded no change and the Centre a rise of 0.5 per cent.

On a twelve-month basis employment grew by 0.1 per cent (Table 5). This result was the outcome of a decline in male employment (-88,000 workers) and an increase in female employment (111,000), as well as a drop of 162,000 in the number of self-employed workers and a growth of 185,000 in payroll employees.

Fixed-term jobs decline

During the same period, fixed-term employment declined by 1.2 per cent, equal to 27,000 workers, owing to the sharp drop in full-time jobs, down by 2.9 per cent. According to the quarterly survey of inflation and growth expectations conducted by the Bank of Italy in collaboration with *Il Sole 24 Ore* in March on a sample of firms with 50 or more employees, the cost of the present recession will be borne mainly by workers on fixed-term contracts. About a third of the firms interviewed expect to cut staff in the next three months. Of these, around 70 per cent will do so by not renewing fixed-term contracts or by reducing working hours (if necessary using the Wage Supplementation Fund), while 90 per cent plan to suspend recruitment and labour turnover. Few declare an intention to resort to collective dismissals or early retirement incentives.

Table 5

Labour force status of the population in Italy

	Average 2007	Average 2008	Q4 2007	Q4 2008	Change Q4 2008/ Q4 2007 (1)
	thousands of persons				
Total persons in work	**23,222**	**23,405**	**23,326**	**23,349**	**0.1**
Employees	**17,167**	**17,446**	**17,350**	**17,535**	**1.1**
of which: fixed-term contracts	*2,269*	*2,323*	*2,282*	*2,255*	*-1.2*
part-time contracts	*2,422*	*2,577*	*2,504*	*2,565*	*2.4*
Self-employed	**6,055**	**5,959**	**5,976**	**5,814**	**-2.7**
Labour force	**24,728**	**25,097**	**24,981**	**25,125**	**0.6**
men	*14,779*	*14,884*	*14,856*	*14,887*	*0.2*
women	*9,949*	*10,213*	*10,124*	*10,238*	*1.1*
Population	**58,880**	**59,336**	**59,045**	**59,504**	**0.8**
	percentages				
Unemployment rate	**6.1**	**6.7**	**6.6**	**7.1**	**0.5**
men	*4.9*	*5.5*	*5.3*	*6.0*	*0.7*
women	*7.9*	*8.6*	*8.6*	*8.6*	*0.0*
Participation rate (age 15-64)	**62.5**	**63.0**	**63.0**	**63.0**	**0.0**
men	*74.4*	*74.4*	*74.6*	*74.4*	*-0.2*
women	*50.7*	*51.6*	*51.4*	*51.6*	*0.2*
Employment rate (age 15-64)	**58.7**	**58.7**	**58.7**	**58.5**	**-0.2**
men	*70.7*	*70.3*	*70.6*	*69.8*	*-0.8*
women	*46.6*	*47.2*	*46.9*	*47.2*	*0.3*
North	*66.7*	*66.9*	*66.9*	*66.8*	*-0.1*
Centre	*62.3*	*62.8*	*62.0*	*62.7*	*0.7*
South	*46.5*	*46.1*	*46.7*	*45.6*	*-1.1*

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

The unemployment rate rises

The employment rate in the 15-64 age group fell to 58.5 per cent in the fourth quarter, that is 0.2 percentage points down on a year earlier. The decline was more marked among the male component (-0.8 percentage points) and in the South (-1.1 points). The labour supply expanded by 0.6 per cent, while the unemployment rate rose by 0.5 percentage points to 7.1 per cent. The number of unemployed workers has risen, on a seasonally adjusted basis, almost without a break since the third quarter of 2007.

In the first three months of 2009 there was a further increase in the number of hours authorized for the Wage Supplementation Fund in industry excluding construction, ascribable almost entirely to the ordinary scheme (Figure 28). In the first quarter the number of equivalent workers on ordinary wage supplementation reached 3.3 per cent of the total, the highest level since 1993. According to the ISAE survey, expectations of non-construction industrial firms regarding employment in the next three months, which had already deteriorated in the course of 2008, diminished further in the first quarter of 2009 to values close to those recorded during the crisis of the early 1990s. One sign that conditions on the labour market have continued to worsen is the sharp increase, compared with a year earlier, in the number of requests for unemployment benefits submitted to INPS in the first three months of this year.

Real earnings show no change

De facto per capita earnings grew by 3.3 per cent between 2007 and 2008 (3.0 per cent in industry, 2.7 per cent in private services and 4.0 per cent in public services), partly due to the one-off payments associated with contract renewals. The increase was larger than the one recorded in 2007 (2.3 per cent) and was in line with the rise in the consumer price index. The growth in real earnings should slow in 2009, although remaining above the rate of increase in consumer prices.

3.6 PRICE DEVELOPMENTS

Inflation continues to slow...

Consumer price inflation measured by the index for the entire resident population (CPI) averaged 3.3 per cent in 2008, up from 1.8 per cent in 2007. Since the end of the summer, the abrupt reversal in the trend in raw materials prices caused by the global economic slowdown has cut the twelve-month growth in the CPI to a rate of 1.6 per cent in January and February of this year (Table 6). According to provisional figures from Istat, the CPI continued to slow in March, falling to 1.2 per cent, the lowest level since 1969. The seasonally adjusted monthly variations give a clearer picture of the decline in inflation in the second half of 2008, mainly due to the substantial fall in fuel prices.

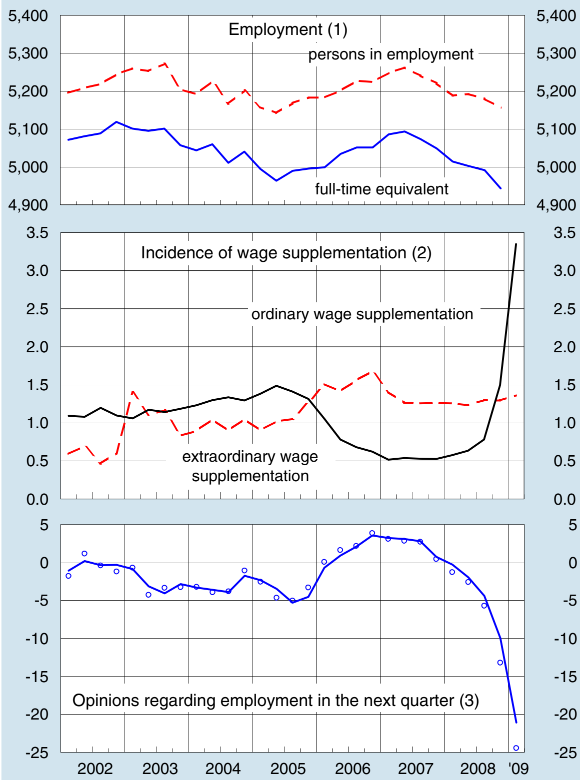
...and the trend is gradually spreading to core inflation

Core inflation, measured by the twelve-month changes in the CPI excluding fuel and food products, fell slightly at the beginning of the current year, to 1.9 per cent in February; it was just over 2 per cent during 2008. On the basis of seasonally adjusted data it is expected to slow further over the coming months. An analysis of the prices of the single items making up the CPI basket does not show any large or generalized reductions to date, except in energy products. The easing of pressures on food and energy items caused the price inflation for goods and services purchased most frequently by Italian households (which are more significant for households with lower levels of consumption) to decline from a peak of 6.1 per cent in July 2008 to 1.4 per cent in February of this year. In February, producer prices fell by 3.3 per cent on a twelve-month basis as a result of further, large reductions in the prices of intermediate goods, which represent more than 50 per cent of the basket. Price inflation for final consumer goods, which anticipates movements in the corresponding retail prices, also slowed to almost nil. In the fourth quarter of 2008 a renewed gap, of 0.6 percentage points, emerged between consumer price inflation in Italy and the average for the euro area (measured by the HCPI), whereas it had been virtually zero from 2004 to 2007. This development was largely due to the delay with which the prices of some food products and air travel in Italy responded to the easing of pressures on raw materials markets in the second half of 2008. The gap was partly reabsorbed in the early months of this year, narrowing to 0.3 points.

Figure 28

Employment and wage supplementation in industry excluding construction

(seasonally adjusted; thousands of persons and percentage points)



Source: Based on Istat, INPS, national accounts, and ISAE data.
(1) Total employment (persons in employment) and standard labour units (full-time equivalents) as defined in the national accounts; quarterly data. – (2) Average number of equivalent workers on ordinary or extraordinary wage supplementation in the quarter as a percentage of the number of equivalent employees as defined in the national accounts; quarterly data. Partial estimates for the first quarter of 2009. – (3) Percentage of total firms expecting employment to increase/decrease in the next three months. Exact values and three point moving averages; quarterly data.

Inflation should continue to slow until the summer

The effects of the worsening economic outlook are evident in the sharp downward adjustment of inflation expectations by the professional forecasters surveyed by *Consensus Economics*. In March, average inflation was set at 0.9 per cent in 2009 and at 1.6 per cent in 2010. In line with expectations for the euro area as a whole, consumer price growth in Italy should continue to slow until the summer; contributory factors will be the reduction in electricity and gas prices in response to the fall in world energy prices and statistical comparisons with the year-earlier period, when prices reflected the sharp increases in the prices of raw materials. The survey carried out in March by the Bank of Italy in collaboration with *Il Sole 24 Ore* revealed that firms continue to adopt extremely cautious pricing policies during this period of falling demand. This finding is in line with the responses concerning firms' pricing plans recorded by the ISAE monthly economic survey, which point to a continuation of the marked slowdown in producer prices.

Table 6

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

	HICP (1)		CPI (2)			PPI (5)
	Overall index	Excl. energy and food	Overall index	1-month (3)	Core component (4)	Overall index
2007	2.0	1.8	1.8	–	1.6	3.3
2008	3.5	2.2	3.3	–	2.1	5.7
2008 – Jan.	3.1	2.1	3.0	0.4	1.9	5.9
Feb.	3.1	2.0	2.9	0.1	1.8	6.2
Mar.	3.6	2.4	3.3	0.5	2.1	6.4
Apr.	3.6	2.1	3.3	0.1	2.0	6.2
May	3.7	2.2	3.6	0.5	2.0	7.2
June	4.0	2.3	3.8	0.5	2.2	8.1
July	4.0	1.9	4.1	0.4	2.2	8.7
Aug.	4.2	2.5	4.1	0.1	2.3	8.1
Sept.	3.9	2.3	3.8	-0.1	2.1	7.3
Oct.	3.6	2.4	3.5	0.1	2.2	4.6
Nov.	2.7	2.2	2.7	-0.4	2.1	1.2
Dec.	2.4	2.3	2.2	-0.1	2.1	-0.7
2009 – Jan.	1.4	1.5	1.6	-0.2	1.9	-2.0
Feb.	1.5	1.7	1.6	0.1	1.8	-3.3
Mar.	(1.0)	....	(1.2)	(0.0)	....	....

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) Seasonally adjusted overall index. – (4) Overall index excluding food and energy products. – (5) Index of producer prices of industrial products sold on the domestic market.

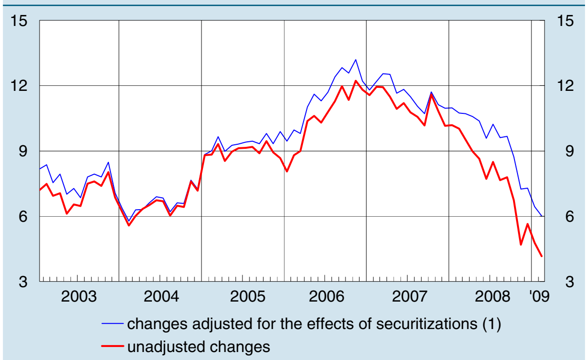
3.7 BANKS

Bank lending continues to slow ...

The growth of credit in Italy slowed down in every sector of economic activity. At the end of February the twelve-month expansion in lending to the private sector, adjusted for the effect of securitizations, was 6 per cent (Figure 29). The three-month growth rate, calculated using seasonally adjusted data and with account taken of the postponement of tax deadlines at the end of November 2008 (see *Economic Bulletin*, No. 51, January 2009), fell to 2.5 per cent on an annual basis. According to preliminary indications based on a broad sample of intermediaries that also report data at ten-day intervals, the slowdown continued in the first twenty days of March.

Figure 29

Loans to the private sector
(monthly data; twelve-month percentage changes)



Source: Based on Bank of Italy data.
(1) Includes securitizations as well as other true sales (to non-MFIs) of loans granted to resident non-MFIs. The adjustment for the effect of securitization is based on estimates of repayments of securitized loans

In the twelve months to February 2009, the loans disbursed by the banks belonging to the five largest groups stagnated. In particular, there was a contraction of 4.9 per cent in their lending to small enterprises, while total lending to this category grew by 0.8 per cent. The largest banks' share of lending to smaller firms has fallen by 3 percentage points over the last twelve months, to 46 per cent.

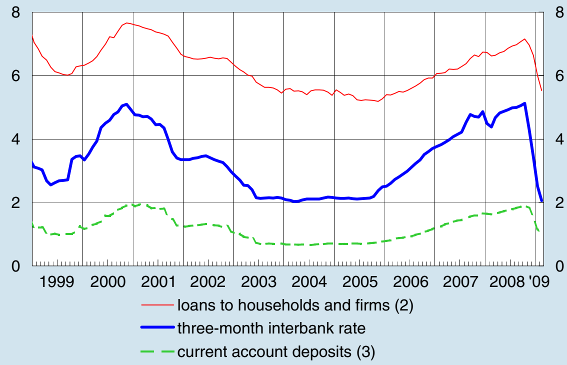
... due to demand weakening and, in the case of firms, to supply restrictions

The slowdown in credit was mainly due to the weak demand for loans of firms and households, but also reflected greater caution on the part of intermediaries. The responses of the Italian banks participating in the Bank Lending Survey covering the last quarter of 2008 show a further slight tightening of the criteria used to grant loans, especially to firms (see the box "Credit Supply and Demand in Italy"). The March quarterly survey by the Bank of Italy and *Il Sole 24 Ore* on the inflation and growth expectations of businesses with more than 50 employees in industry and services provided similar indications: the difference between responses indicating a worsening in credit supply conditions and those indicating an improvement was 34 percentage points, a small decrease compared with the figure for December.

Figure 30

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.

The lines of credit granted by banks have undergone a small contraction; the ratio of credit drawn to credit granted accordingly increased, as is normal at times of credit restriction, and at the end of February was 43 per cent, the highest value of the last five years. The increase in the ratio was most pronounced for manufacturing firms. Another sign of a tightening of the supply of credit is provided by the conjunction of the slowdown in lending to firms with the growth in their financing needs and the fall in interest rates.

Bank interest rates have adjusted to the recent large reductions in official rates about as gradually as they rose in the upward phase that began at the end of 2005 (Figure 30). Between November 2008 and February 2009 the cost of firms' short-term borrowing, including current account loans, and that of new variable rate mortgage loans to households fell by more than one and a half percentage points to 5.2 and 3.9 per cent respectively. The differential between Italy and the euro-area average in terms of the cost of new fixed rate mortgage loans, equal to one percentage point in the middle of 2007, has disappeared. According to preliminary indications, the fall in interest rates continued in the first two ten-day periods in March.

Looking ahead, the supply of credit is likely to benefit from the measures to promote the recapitalization of Italian banks recently made operative by the Government (see the box "The instruments for recapitalizing Italian banks").

CREDIT SUPPLY AND DEMAND IN ITALY

The responses provided by the Italian banks participating in the quarterly euro-area Bank Lending Survey point to a further moderate tightening of credit standards in the fourth quarter of 2008 for loans to **firms** (Figure A). [1] The tightening was more pronounced for long-term loans and affected both large firms and small and medium-sized enterprises. Although it involved all the terms and conditions applied to new loans, the tightening was mainly reflected in a reduction in the quantities disbursed and an increase in the margins applied and can be attributed to the deterioration in the economic situation and the related heightening of risk.

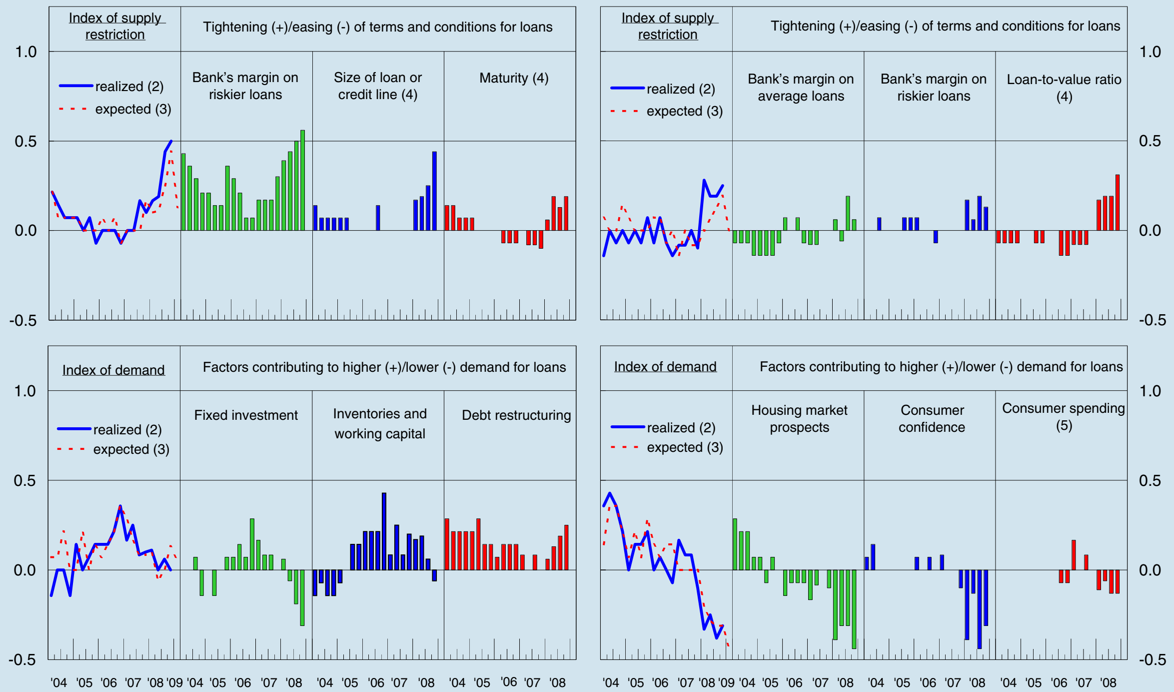
Firms' demand for credit remained at the low level of recent quarters as a result of their reduced financing needs for fixed investments, inventories and working capital, which more than offset the increased demand for loans for debt restructuring.

[1] Eight leading banking groups took part in the survey, which was completed on 7 January; 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 on the first quarter of 2009 and expectations for the second quarter are not yet available; they will be released on 29 April.

Figure A

Supply conditions and trends in credit demand in Italy (1)

A. *Lending to firms* B. *Lending to households for house purchases*



Source: Quarterly Bank Lending Survey for the euro area.
(1) Diffusion indices constructed by aggregating the qualitative responses 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 lesser (greater) 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 house purchases had an expansive (restrictive) effect on the demand for mortgages.

The respondent banks declared that they expected an attenuation of the tightening of credit standards for loans to firms in the first quarter of 2009, against a background of virtually unchanged growth in demand.

Banks reported a moderate tightening of their supply policies for loans to **households**. The terms and conditions for mortgage loans and consumer credit became less accommodating in connection with the unfavourable outlook for the economy and the housing market and with the deterioration in households' creditworthiness. Fund-raising difficulties continued to exert an influence, although attenuated by the monetary policy measures adopted; perception of the risk associated with the value of the collateral provided by households grew. The banks stated that they had increased the margins they applied to loans and boosted the guarantees they required (for mortgage loans there has also been a reduction in the loan-to-value ratio).

Demand for mortgages was reported to have decelerated sharply since the end of 2007. Demand for consumer credit slowed.

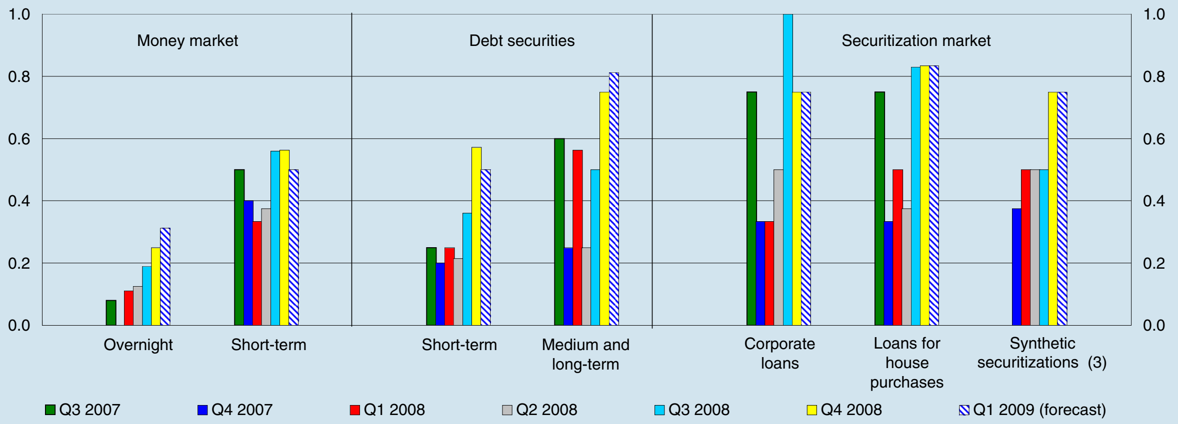
For the first quarter of 2009 the banks surveyed forecast basically unchanged terms and conditions for the supply of loans to households, with a further slowdown in the demand for loans for house purchase and a modest recovery in that for consumer credit.

On the funding side, the difficulty in procuring funds on the wholesale market remained considerable in the fourth quarter of 2008 for nearly all the technical forms and became especially acute for issues of debt securities (Figure B). Banks continued to report that the crisis had increased the costs associated with capital requirements and in this way had affected credit supply. Banks' expectations for the first quarter of 2009 pointed to ongoing repercussions of the crisis on access to wholesale funding and the supply of credit.

The Italian banks' responses to the survey were broadly in line with those observed for the euro area as a whole, although the demand for credit in Italy slowed less in connection with the greater need for funds for debt restructurings and the larger reduction in self-financing.

Figure B

Difficulty of obtaining funds in the wholesale market (1)(2)



Source: Quarterly Bank Lending Survey for the euro area.
(1) Diffusion indices constructed by aggregating the qualitative responses to the special questions on the effects of the subprime mortgage crisis added to the basic quarterly bank lending questionnaire. – (2) 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. – (3) These imply recourse to credit derivatives. Data for the third quarter of 2007 are not available for this indicator.

THE INSTRUMENTS FOR RECAPITALIZING ITALIAN BANKS

The Government and Parliament have taken measures since last October to protect depositors, support banks' liquidity and capital and strengthen their ability to satisfy the demand for loans. The measures, initially adopted as a matter of urgency in the form of decree laws, were confirmed with Law 190/2008 and Law 2/2009. They were described in the last two issues of the *Economic Bulletin* (see the boxes "The Italian authorities' measures for the stability of the financial system" and "The measures adopted in Italy for the stability of the financial system", respectively in No. 50, October 2008, and No. 51, January 2009).

The recapitalization of fundamentally sound banks was made operational on 25 February with an implementing decree of the Minister for the Economy and Finance. It involves the issue of non-voting securities that can be subscribed by the Ministry up to 31 December 2009 and count as regulatory capital.

Eligibility for recapitalization extends to listed Italian banks and bank holding companies whose soundness has been ascertained by the Bank of Italy, taking account of available risk indicators such as the spreads on credit default swaps on subordinated debt (whose median value must not have exceeded 100 basis points in the period from January 2007 to August 2008) and credit ratings (as a rule, the rating must not be lower than A- or the equivalent). The amount of the public intervention must be limited to the minimum needed to achieve the objectives and ordinarily is not to exceed 2 per cent of risk-weighted assets.

The securities are perpetual and may be converted into ordinary shares at the request of the issuer. The conversion ratio, which determines the number of shares underlying the issue, is fixed on the basis of the average share price in the ten trading days before the announcement date of the issue. The issuer may exercise its conversion right after three years have passed from the issue date, provided that the market value of the underlying shares on the conversion date is at least 110 per cent of the initial value. The issuer may also redeem the securities at any time under certain conditions and subject to prior authorization by the Bank of Italy.

The securities have the same degree of subordination as ordinary shares (and thus the same ability to absorb losses) not only in the case of insolvency but also under going-concern conditions, if there are losses that reduce the total capital ratio below the regulatory minimum of 8 per cent. Interest is non-cumulative and is paid by the issuer only if there are distributable earnings (and up to the amount of those earnings), provided the total capital ratio is at least 8 per cent. Given these characteristics, the instruments qualify as regulatory capital of the best quality (core tier 1).

The economic terms of the issues comply with the EU guidelines on state aid. The remuneration is in line with market conditions and such as to render the public intervention as temporary as possible; there are built-in incentives for banks to redeem the instruments as soon as conditions permit. The method of determining the yield is designed to protect the interests of taxpayers and the state as far as possible.

The interest payable by the issuer is equal to the highest of the following: a) a predetermined annual coupon, increasing in time; b) an amount equal to the product of the dividend per share distributed to ordinary shareholders (on any basis and in any form) and the number of shares underlying the issue; this amount is increased by a rising percentage over time; c) the average yield on thirty-year Treasury bonds (a proxy for the Italian state's borrowing cost), increased by a spread. In addition, if the issuer decides to redeem the instruments, it will pay a premium on their face value that may increase in time in relation to the market value of the issuer's shares.

Two alternative remuneration schemes have been established. One envisages lower coupon payments and higher redemption prices up to 2014. The other, designed to encourage recourse to recapitalization by intermediaries intending to redeem their instruments relatively soon, has higher coupons and lower redemption prices up to 2014. From 2015 onwards the two schemes are identical. The table below summarizes the characteristics of the two instruments for a time horizon which for illustrative purposes does not extend beyond 2023.

Provision has also been made for the remuneration offered to the Ministry for the Economy and Finance to be less if the issuer places at least 30 per cent of the issue on the same terms with private investors (at least two thirds of which with investors other than shareholders owning 2 per cent or more of the share capital). In any case, the yield must be at least 200 basis points above the average yield of thirty-year Treasury bonds.

Banks that decide to avail themselves of the recapitalization measure undertake to sign a memorandum of understanding with the Ministry, defined on the basis of a framework agreement between the Ministry and the Italian Banking Association. The aim of the agreement is to create conditions for the growth of credit supply to small and medium-sized enterprises (SMEs) and to households, consistently with the need to maintain a high level of systemic stability and prudent standards of credit allocation.

Under the framework agreement banks will undertake to: make available to SMEs for the next three years a non-decreasing volume of resources at non-disadvantageous terms compared with the last two

Table

Characteristics of the recapitalization instruments

Financial year (1)	Interest: the highest of				Redemption price (% of face value) (5)			
	Annual coupon (% of face value) (2)		Dividends (2) (3)	State's borrowing cost (4)	Minimum		Maximum	
	Option 1	Option 2			Option 1	Option 2	Option 1	Option 2
2009	7.50	8.50	1.05 * DIV		110	100	120	100
2010	7.75	8.50	1.10 * DIV		110	100	120	100
2011	8.00	8.50	1.15 * DIV	BTP30 + 300bps	110	100	120	100
2012	8.25	8.50	1.15 * DIV	BTP30 + 300bps	110	100	120	100
2013	8.50	9.00	1.15 * DIV	BTP30 + 350bps	110	110	130	110
2014	8.50	9.00	1.15 * DIV	BTP30 + 350bps	110	110	130	110
2015	9.00		1.15 * DIV	BTP30 + 350bps	110		130	
2016	9.00		1.15 * DIV	BTP30 + 350bps	110		140	
2017	9.50		1.15 * DIV	BTP30 + 350bps	110		140	
2018	9.50		1.25 * DIV	BTP30 + 350bps	110		140	
2019	10.00		1.25 * DIV	BTP30 + 350bps	110		150	
2020	10.00		1.25 * DIV	BTP30 + 350bps	110		150	
2021	10.50		1.25 * DIV	BTP30 + 350bps	110		150	
2022	10.50		1.25 * DIV	BTP30 + 350bps	110		160	
2023	11.00		1.25 * DIV	BTP30 + 350bps	110		160	
ecc.								

(1) For purposes of the (deferred) payment of interest and determination of the redemption price, the financial year runs from 1 July of the year shown in the table to 30 June of the following year. – (2) Interest calculated on the basis of the annual coupon or the amount of dividends cannot be greater than 15 per cent of the issue's face value. – (3) For each financial year, DIV corresponds to the product of the dividend per share distributed to ordinary shareholders (on any basis and in any form) and the number of shares underlying the issue. – (4) BTP30 is the average of the yields at issue of thirty-year Treasury bonds recorded in the first quarter of the year in which interest is paid; pbs = basis points. – (5) The redemption price is equal to the average market value of the shares underlying the issue in the thirty days preceding the redemption date if that value is between the minimum and maximum shown in the table. If the market value is below the minimum, the redemption price is the minimum; if the market value is above the maximum, the redemption price is the maximum.

years; contribute to the guarantee funds for SMEs and apply terms to guaranteed firms that reflect the lower risk of the transactions; and support the liquidity of creditors of general government by discounting their receivables. As regards households, banks must agree to suspend mortgage loan repayment instalments, for at least 12 months at no cost to the customer, for borrowers who have lost their jobs and been beneficiaries of public income-support measures, and to assist agreements for advances of Special Wage Supplementation Fund benefits. In addition, banks pledge to give their customers adequate information on the initiatives taken to implement the memorandum. Issuer banks will have to provide the aggregated data necessary for monitoring application of the memorandum on a quarterly basis.

Banks benefiting from recapitalization will also have to follow dividend policies consistent with a sufficiently strong capital base and adopt a code of ethics concerning, among other matters, compensation of top management and of some categories of staff (such as traders). Compensation policies must be consistent with the principles of prudent risk management and long-term corporate strategies. In this connection, if they have not done so already and are required to because of their size and business complexity, banks will also need to establish a compensation committee a majority of whose members must be independent persons.

Loan quality is suffering from the deterioration in cyclical conditions

The fourth quarter of 2008 saw a further worsening in the quality of credit. The flow of adjusted new bad debts rose to 1.5 per cent of outstanding loans (from 1.2 per cent in the third quarter). This was the highest value since 1999, excluding the peak recorded in the fourth quarter of 2003 after the collapse of the Parmalat group (Figure 31). New bad debts were the highest proportion of outstanding loans for non-financial corporations (2 per cent, compared with 1.5 per cent in the third quarter), in particular among those located in the Centre and North. Despite a slight increase, the consumer household bankruptcy rate remained at a historically low level (1 per cent). Preliminary data indicate that the quality of banks' assets deteriorated further in the early months of this year.

Fund-raising slows

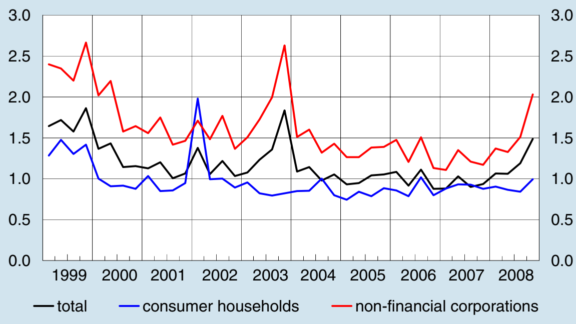
After continuing to grow rapidly until September, bank fund-raising has rapidly decelerated, with the rate of increase falling to 4.6 per cent for the twelve months ending in February 2009, more than 5 percentage points below the peak recorded in September (Table 7). The deposits of non-financial corporations are contracting, presumably as a consequence of the more difficult financial conditions. The growth in consumer households' deposits is also slowing, especially the less liquid component, where interest rates have come down in line with money-market rates; by contrast the expansion of current accounts was greater. The growth in bond fund-raising continues at a rapid pace (12.4 per cent in February). Between November and February, the cost of newly issued securities came down by 70 and 90 basis points for fixed and variable rate bonds respectively. The latter's yield differential with respect to CCTs has widened, exceeding one percentage point in February. By contrast, the yield differential of fixed rate bonds with respect to BTPs narrowed slightly to about 10 basis points. Italian banks' net external liabilities rose again, above all as a result of the significant reduction in assets vis-à-vis banks located in other euro-area countries.

Banks' profitability decreased in 2008

According to the information contained in consolidated quarterly reports, although the profitability of the main Italian banking groups remained positive, it deteriorated markedly. Net of non-recurring items of income, banks' profits were down by about one third compared with 2007; their ROE decreased by 4 percentage points to about 7 per cent. Although their net interest income showed a large increase, it was not enough to offset the fall in fee income and the losses on the trading portfolio in

Figure 31

New bad debts in relation to outstanding loans (1)
(seasonally adjusted and annualized quarterly data; percentages)



Source: Based on Bank of Italy data.
(1) Annualized flow of bad debts in the quarter in relation to the stock of adjusted outstanding performing debts at the end of the previous quarter. Seasonally adjusted data.

Table 7

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

	2007	2008	February 2009	
				Stocks (2)
Assets				
Securities other than shares	7.3	45.0	38.9	363,257
Loans	10.1	5.6	4.5	1,764,432
up to 12 months	*7.5*	*4.1*	*2.6*	*604,962*
beyond 12 months	*11.3*	*6.3*	*5.5*	*1,159,470*
External assets	12.5	-1.5	-8.3	354,494
Liabilities				
Total funding (3)	11.0	12.1	10.8	1,878,022
Deposits of Italian residents	4.2	7.3	6.1	1,109,831
of which: (4)				
current accounts	*2.9*	*6.6*	*8.9*	*684,304*
with agreed maturity	*14.3*	*13.5*	*8.1*	*62,816*
redeemable at notice	*-0.5*	*7.0*	*8.2*	*250,822*
repos	*12.1*	*10.4*	*-14.0*	*98,069*
Deposits of non-residents	22.9	-8.1	-6.5	490,857
Bonds	11.4	11.6	12.4	598,062
Memo: Total bonds	11.9	20.3	18.4	768,191

(1) The figures for February 2009 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) Does not include liabilities with resident MFIs. – (4) Does not include those of central government.

connection with the crisis; in fact gross income contracted by about 7 per cent. While operating costs remained basically stable, provisions and value adjustments nearly doubled, as the larger writedowns in relation to the deterioration in the quality of credit were accompanied by significant adjustments to the book value of goodwill and equity investments. The amendments made to the International Accounting Standards concerning the classification of financial instruments and those made to tax law concerning the realignment and exemption from taxation of goodwill have attenuated the fall in banks' profitability. Banks' dividend policies and the capital management measures recently adopted by the major banking groups have strengthened the banking system's capital adequacy. Preliminary data in the quarterly reports show an increase in banks' capital ratios in December 2008 compared with six months earlier.

3.8 THE FINANCIAL MARKET

The Italian stock exchange continued to fall

In the first quarter of 2009 the general Italian stock exchange index lost 15 per cent, in line with the performance of the main euro-area stock markets (-14 per cent; Figure 32). Interrupting a sharp downswing that had begun in January and brought prices to a 13-year low, shares began to rebound after the first ten days of March. The recovery was led by financial shares, whose strong performance reflected the announcement of a return to profit for some major American and British banks and of the operating details of the US bank rescue plan. At the end of the quarter the Italian and euro-area indices were down by 63 and 57 per cent respectively from the highs recorded in the spring of 2007. The fall in share prices in the first quarter was due to the sharp drop in listed companies' current and expected earnings and to a further increase in the risk premium demanded by investors. The hardest-hit sectors were insurance, banking and services, which fell by 31, 19 and 15 per cent respectively. Oil and consumer goods companies showed smaller losses (11 and 14 per cent). The commodities sector bucked the trend, gaining 5 per cent.

The current earnings/price ratio rose further to historically high levels (Figure 33). The expected volatility of share prices implied by option prices also remains high.

The protraction of the financial crisis and low share prices continue to discourage new listings on the stock exchange. In the first quarter of 2009 only one company went public, listing on the MAC alternative capital market. At the end of February, 294 Italian companies were listed on Borsa Italiana with a total market value of €312 billion (19.6 per cent of GDP).

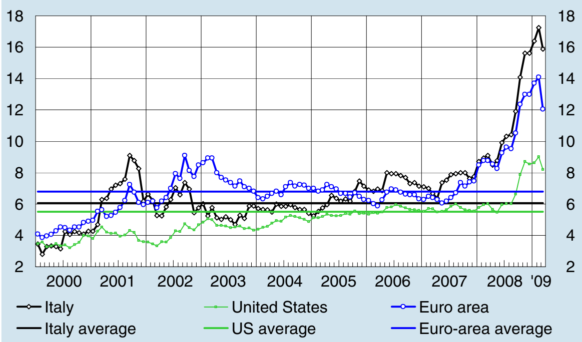
Figure 32

Share prices (1)
(end-of-week data; indices, 31 December 2004=100)

Source: Thomson Reuters Datastream.
(1) MIB for Italy, Dow Jones EURO STOXX for the euro area, Standard & Poor's 500 for the United States. The last available figure is for 3 April.

Figure 33

Current earnings/price ratios for the main stock exchanges (1)
(monthly data; percentages)



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

Net bond issues grew, led by securitizations

Net bond issues by Italian companies jumped to €80 billion in the fourth quarter of 2008, from €28 billion in the third (Table 8). Net issues by non-bank financial companies rose sharply thanks almost entirely to securitizations, notably those carried out by the Unicredit and Intesa banking groups in the last two months of the year for a total of €42 billion. As in the euro area, there were net issues again by non-financial companies, attributable mostly to a large placement by Eni; issues by smaller firms remained modest. According to preliminary data, the volume of net issues rose further in the first quarter of this year, in line with developments in the euro area.

The credit risk premium for private-sector companies remained high ...

In the first quarter of 2009 the yield spread between bonds issued by non-financial companies with a high credit rating and government securities diminished by more than 60 basis points, remaining at historically high levels; the decline in spreads was slightly larger than that recorded on comparable euro-area corporate bonds. The high level of spreads reflects the greater credit risk premium demanded by investors to hold private-sector bonds since the failure of Lehman Brothers last September and with the shift of portfolios towards public-sector bonds, deemed relatively less risky. Premiums on credit default swaps for Italian banks rose on average by 0.3 percentage points, less than the increase for banks of the other euro-area countries.

... while that for government securities rose further

The yield spread between ten-year Italian government securities and German Bunds remained at high levels, averaging about 140 basis points in the first quarter, an increase of more than 40 basis points compared with the previous quarter, but in the last weeks it fell to around 120 (Figure 34). The increase in spreads also involved the government securities of the other euro-area countries to a lesser extent and it grew more pronounced in January, when the rating agencies cut the ratings of some countries and put others under credit watch. It reflected both rising risk aversion among investors and a worsening in the

Table 8

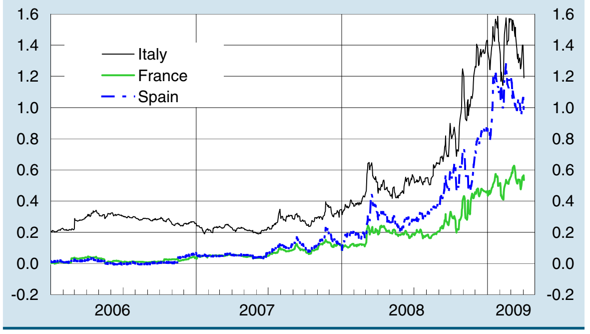
Net bond issues (1)
(millions of euros)

	Banks	Other financial corporations	Non-financial corporations	Total
		Italy		
2007	63,928	14,993	10,489	**89,410**
2008	123,932	78,755	1,177	**203,864**
2007 – Q1	21,619	2,391	-1,198	**22,812**
Q2	15,371	7,518	7,630	**30,519**
Q3	1,793	-3,236	-706	**-2,149**
Q4	25,145	8,320	4,763	**38,228**
2008 – Q1	39,930	-3,760	-133	**36,037**
Q2	45,023	15,948	-1,416	**59,555**
Q3	15,213	12,378	844	**28,435**
Q4	23,766	54,189	1,882	**79,837**
		Euro Area		
2007	285,445	325,771	28,697	**639,912**
2008	190,664	406,931	29,334	**626,929**
2007 – Q1	141,099	95,940	838	**237,877**
Q2	101,805	59,791	25,107	**186,702**
Q3	14,167	33,581	-4,378	**43,370**
Q4	28,374	136,459	7,131	**171,964**
2008 – Q1	35,270	8,569	-2,513	**41,326**
Q2	127,113	102,095	11,837	**241,045**
Q3	22,385	49,430	7,199	**79,014**
Q4	5,897	246,837	12,810	**265,545**

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.

Figure 34

Interest rate differentials between ten-year government securities and corresponding German securities
(daily data; percentage points)



Source: Based on Bloomberg data.

public finance indicators for 2008 and projections for the two years 2009-2010. Premiums on credit default swaps for the debt of the Italian Republic and the other euro-area countries also increased.

The outflow of savings from investment funds gains pace

Net redemptions of investment fund units accelerated in Italy to reach €40.6 billion in the fourth quarter of 2008, from €27.9 billion in the third. More than 40 per cent of the total involved Italian harmonized funds. The net outflow from hedge funds also intensified (€3.7 billion, compared with €1.4 billion in the third quarter). In the year as a whole, net redemptions nearly tripled (€137 billion, against €49 billion in 2007). In the fourth quarter Italian harmonized investment funds as a whole had returns of -2.3 per cent, compared with -1.4 per cent in the third quarter; the collapse of the international stock markets hit equity funds, which lost an average of 14.8 per cent, while bond funds showed a positive average return of 1.1 per cent. Harmonized investment funds assets totalled €432.8 billion at the end of 2008, down by 32.9 per cent from a year earlier. Individually managed portfolios also recorded net outflows in the fourth quarter (€16.8 billion); their estimated average return was negative by 2.4 per cent.

Table 9

General government balances and debt (1)

(millions of euros and percentages of GDP)

	2005	2006	2007	2008
Net borrowing	61,432	49,312	23,225	42,979
% of GDP	*4.3*	*3.3*	*1.5*	*2.7*
Primary surplus	4,633	19,266	53,990	37,912
% of GDP	*0.3*	*1.3*	*3.5*	*2.4*
Interest payments	66,065	68,578	77,215	80,891
% of GDP	*4.6*	*4.6*	*5.0*	*5.1*
Debt	1,512,779	1,582,009	1,598,975	1,663,650
% of GDP	*105.8*	*106.5*	*103.5*	*105.8*

Source: Based on Istat data for items from the general government accounts (press release dated 2 April 2009).
(1) Rounding may cause discrepancies in totals.

Table 10

Public finance objectives and estimates for 2008

(billions of euros and percentages of GDP)

	General government			*Memorandum items:*	
	Net borrowing	Primary surplus	Debt	GDP growth rate	Net borrowing 2007
Objectives					
June 2007 (1)	35.9	42.5	....		38.3
% of GDP	*2.2*	*2.7*	*103.2*	*1.9*	*2.5*
September 2007 (2)	35.4	42.9	....		36.4
% of GDP	*2.2*	*2.7*	*103.5*	*1.5*	*2.4*
November 2007 (3)	....	....	....		....
% of GDP	*2.2*	*2.6*	*103.5*	*1.5*	*2.4*
Estimates					
March 2008 (4)	38.7	40.6	....		29.2
% of GDP	*2.4*	*2.6*	*103.0*	*0.6*	*1.9*
June 2008 (1)	39.1	40.7	....		29.2
% of GDP	*2.5*	*2.6*	*103.9*	*0.5*	*1.9*
September 2008 (5)	39.7	41.4	....		29.2
% of GDP	*2.5*	*2.6*	*103.7*	*0.1*	*1.9*
February 2009 (3)(6)	40.8	39.7	....		....
% of GDP	*2.6*	*2.5*	*105.9*	*-0.6*	*1.6*
Outturn (7)	**43.0**	**37.9**	**1,663.6**		**23.2**
% of GDP	*2.7*	*2.4*	*105.8*	*-1.0*	*1.5*

(1) Economic and Financial Planning Document. – (2) Forecasting and Planning Report. The primary surplus and net borrowing are 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. – (6) Information Note 2009-2011. – (7) Istat press releases dated 2 March and 2 April 2009 for net borrowing, primary surplus and GDP growth.

3.9 THE PUBLIC FINANCES

The deficit began to widen again in 2008

General government net borrowing increased from 1.5 to 2.7 per cent of GDP in 2008 (Table 9), basically in line with the estimate given in the Stability Programme update released in February 2009 (Table 10). The deterioration reflects the slowdown in revenue in connection with the initial effects of the recession and the tax relief enacted over the past two years. The primary surplus went back down, from 3.5 to 2.4 per cent of GDP.

The recession has braked revenue growth

The decline in economic activity and some tax relief measures reduced the growth of tax and social security revenue to 1 per cent in 2008 from 7.8 per cent in 2006 and 6.4 per cent in 2007. The ratio of tax and social security revenue to GDP fell by 0.3 percentage points to 42.8 per cent (Table 11). In detail, there were decreases in corporate tax payments and the main indirect taxes, which had contributed greatly to the earlier impressive revenue gains (Figure 35).

Table 11

General government expenditure and revenue

(millions of euros and percentage changes)

	2007	2008	% change on previous year 2007	% change on previous year 2008
EXPENDITURE				
Final consumption expenditure	304,367	318,112	1.7	4.5
of which:				
compensation of employees	*164,071*	*171,160*	*0.5*	*4.3*
intermediate consumption	*80,832*	*85,414*	*4.1*	*5.7*
soc. benefits in kind	*42,028*	*43,028*	*1.7*	*2.4*
Soc. sec. benefits in cash	264,483	278,008	4.9	5.1
Interest payments	77,215	80,891	12.6	4.8
Other current expenditure	38,840	38,885	8.7	0.1
Current expenditure	**684,905**	**715,896**	**4.4**	**4.5**
% of GDP	*44.3*	*45.5*		
Current expenditure, net of interest payments	**607,690**	**635,005**	**3.5**	**4.5**
% of GDP	*39.3*	*40.4*		
Investment (1)	35,969	34,973	3.7	-2.8
Investment net of property disposals	*37,357*	*36,239*	*2.6*	*-3.0*
Investment grants	25,045	23,077	10.8	-7.9
Other capital expenditure	1,876	977	-89.1	-47.9
Capital expenditure (1)	**62,890**	**59,027**	**-15.6**	**-6.1**
Total expenditure, net of interest payments (1)	**670,580**	**694,032**	**1.3**	**3.5**
% of GDP	*43.4*	*44.1*		
TOTAL EXPENDITURE (1)	**747,795**	**774,923**	**2.4**	**3.6**
% of GDP	*48.4*	*49.3*		

	2007	2008	% change on previous year 2007	% change on previous year 2008
REVENUE				
Direct taxes	233,229	241,427	9.1	3.5
Indirect taxes	227,156	215,519	3.1	-5.1
Social security contributions	205,299	214,718	8.2	4.6
Other current revenue	54,333	56,719	3.0	4.4
Current revenue	**720,017**	**728,383**	**6.4**	**1.2**
% of GDP	*46.6*	*46.3*		
Capital revenue	**4,553**	**3,561**	**3.9**	**-21.8**
of which:				
capital taxes	*301*	*478*	*33.8*	*58.8*
TOTAL REVENUE	**724,570**	**731,944**	**6.4**	**1.0**
% of GDP	*46.9*	*46.6*		
of which:				
taxes and social security contributions	*43.1*	*42.8*		
NET BORROWING	**23,225**	**42,979**		
% of GDP	*1.5*	*2.7*		
Primary surplus	**53,990**	**37,912**		
% of GDP	*3.5*	*2.4*		
Memorandum item:				
GDP	1,544,915	1,572,243		

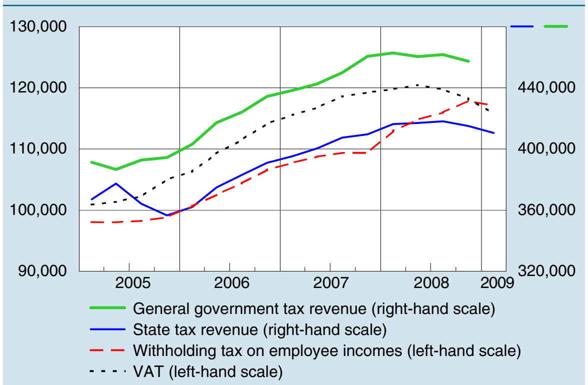
Source: Based on Istat data.
(1) Proceeds of property sales entered with a negative sign.

The reduction depended not only on the contraction in profits and consumption but also on relief concerning the municipal real estate tax and the regional tax on productive activity (Irap). The latter, related to labour costs, was introduced with the Finance Law for 2007 and firms benefited mainly in 2008. Direct tax revenue increased by 3.5 per cent (after rising 12.7 per cent in 2006 and 9.1 per cent in 2007), thanks to the good performance of payroll withholding tax, which benefited from the continuing growth in employment and from the impact of labour contract renewals. The strongly progressive structure of the personal income tax also played a role. The information available on taxes within the powers of local administrations indicates a rise in the proceeds from regional and municipal

Figure 35

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.

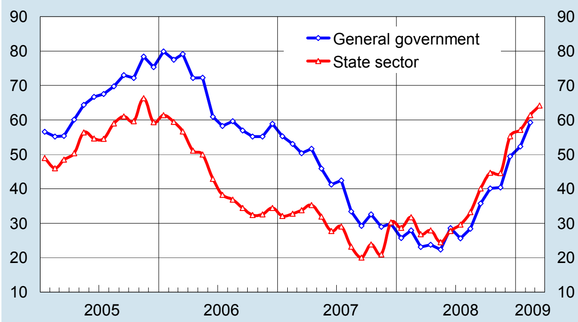
income surtax due to rate increases enacted in 2007, after the four-year suspension of that power at both levels of government. The significant reduction in indirect tax proceeds (by 5.1 per cent) stemmed from declines in revenue not only from Irap but also from VAT and some excise taxes. Social security contributions increased by 4.6 per cent, about 1 percentage point more than total wages.

Primary current spending topped 40 per cent of GDP

Primary current expenditure increased by 4.5 per cent, faster than in the previous two years, when growth had averaged 3.4 per cent. After falling in proportion to GDP for two years, it went up by 1.1 percentage points to a new all-time high (Table 11). The rate of growth in final consumption expenditure rose to 4.5 per cent from 1.7 per cent in 2007. Public employee compensation contributed, rising by 4.3 per cent as a result of the concentration in 2008 of payments stemming from the contract renewals of 2006 and 2007. There was also a further acceleration in intermediate consumption, which expanded by 5.7 per cent after growing by 4.1 per cent in 2007. Social benefits continued to grow rapidly. Capital expenditure declined by 6.1 per cent, or by 0.3 percentage points of GDP, especially local investment and grants to business. Net of real estate disposals, after increasing in 2007, investment spending fell by 3 per cent. As a ratio to GDP it returned to the level recorded in 1998, 2.3 per cent. Interest expenditure rose significantly (4.8 per cent, 0.1 percentage points of GDP), as a lagged effect of the rise in yields, which turned downwards again only towards the end of the year.

Figure 36

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



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

... and the borrowing requirement has started to expand again

After contracting for two years, the general government borrowing requirement net of privatization receipts increased by 1.2 percentage points to 3.1 per cent of GDP (Figure 36 and Table 12). For the most part, the increase was due to developments in the last four months of the year, which reflected the slowdown in revenue and some measures enacted with the November anti-crisis decree (see the box "The anti-crisis decree", *Economic Bulletin* no. 51, January 2009). Among other things, these measures resulted in refunds of tax credits over ten years old amounting to about €3 billion. While the central government borrowing requirement increased by €26.7 billion, that of local governments diminished by €2.9 billion, thanks in part to central government loans of some €8 billion to regions to settle health system liabilities. The gap between borrowing requirement and net borrowing remained unchanged at 0.4 per cent of GDP.

Table 12

General government borrowing requirement and debt
(millions of euros and percentages of GDP)

	2005	2006	2007	2008
Borrowing requirement	70,666	58,824	26,359	49,333
% of GDP	*4.9*	*4.0*	*1.7*	*3.1*
Net borrowing requirement (1)	75,284	58,862	29,859	49,352
% of GDP	*5.3*	*4.0*	*1.9*	*3.1*
Debt	1,512,779	1,582,009	1,598,975	1,663,650
% of GDP	*105.8*	*106.5*	*103.5*	*105.8*
Memorandum items				
Privatization receipts	4,618	38	3,500	19
% of GDP	*0.3*	*0.0*	*0.2*	*0.0*
Settlements of past debts	1,864	243	3,129	1,653
% of GDP	*0.1*	*0,0*	*0,2*	*0,1*

(1) Net of privatization receipts.

The debt/GDP ratio is back up to the 2005 level

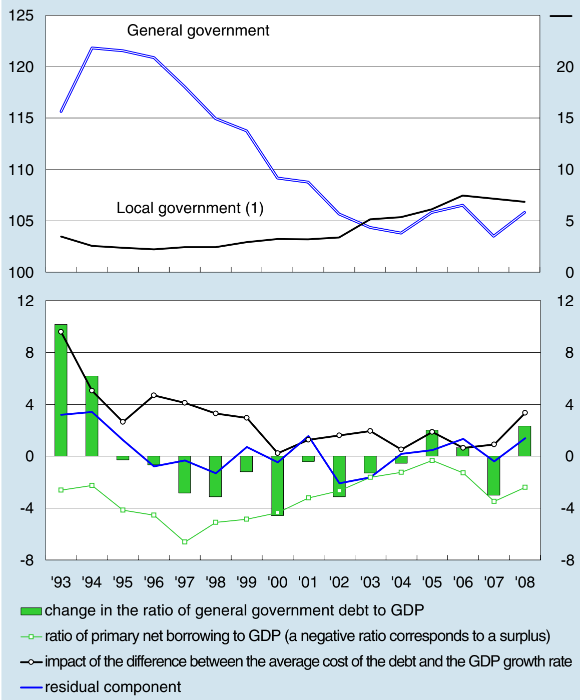
The ratio of general government debt to GDP increased by 2.3 percentage points, regaining the 2005 level of 105.8 per cent (Figure 37; see "The Public Finances, borrowing requirement and debt", *Supplements to the Statistical Bulletin*, vol. XIX, No. 13, 13 March 2009). The rise reflects both the slowdown in GDP and significant growth in the debt, which increased by €64.7 billion, compared with €17 billion in 2007, to €1,663.6 billion (Table 13). The acceleration was almost entirely due to the larger overall borrowing requirement (€49.3 billion as against €26.4 billion) and the increase in the Treasury's assets with the Bank of Italy (by €10.6 billion after a decrease of €13.1 billion in 2007). Central government debt rose from 96.3 to 99 per cent of GDP. Local government debt diminished for the second successive year, from 7.2 to 6.8 per cent, owing to the settlement of health sector debts.

The 2009 budget reduces the trend deficit by nearly €10 billion

The budget for 2009, passed last summer with the budget plans for 2009-2011, projects a reduction in net borrowing of 0.6 percentage points of GDP (about €10 billion) with respect to the deficit on a current legislation basis (Table 14; see the box "The budget for the years 2009-2011", *Economic Bulletin* no. 50, October 2008). The Finance Law for 2009 passed in December mandates only a few small changes to revenue and expenditure that have no net effect on the budget balance. These measures are flanked by two decree-laws to sustain the economy, one passed in November (see the box "The anti-crisis decree", *Economic Bulletin* no. 51, January 2009) and one in February (see the box "February's anti-crisis decree"). Overall, according to official estimates, the two decrees raise resources worth €7.5 billion and allocate them to measures in favour of households (about €3.5 billion), firms (about €1.5 billion) and to stimulate consumption and investment (about €1 billion each), leaving the budget balance unchanged.

Figure 37

General government debt: trend and determinants of its changes
(as a percentage of GDP)



(1) Right-hand scale. The increase in 2003 was mainly of an accounting nature in connection with the reclassification of Cassa Depositi e Prestiti S.p.A. outside general government.

Table 13

Changes in general government debt and its components
(millions of euros)

	2005	2006	2007	2008
Change in the debt = (a)+(b)+(c)+(d)	**68,175**	**69,230**	**16,967**	**64,675**
(a) Total borrowing requirement	70,666	58,824	26,359	49,333
(b) Change in the Treasury deposits with the Bank of Italy	-1,197	8,230	-13,142	10,611
(c) Issue discounts and premiums	-2,444	2,978	4,083	4,471
(d) Change in foreign currency liabilities	1,150	-801	-333	260

The Government forecasts a further increase in the deficit for 2009

In the "Information Note 2009-2011", a memorandum released together with the Stability Programme Update in February, the Government forecasts net borrowing to be 3.7 per cent of GDP in 2009 (Table 15), compared with an estimate of 2.1 per cent in the Forecasting and Planning Report in September.

The estimated primary surplus is lowered from 3 to 1.3 per cent of GDP, and the debt/GDP ratio is now expected to rise by nearly 5 points to 110.5 per cent, whereas the earlier forecasts were for a slight reduction. The worsened estimate reflects the downward revision of the economic forecast from a growth of 0.5 per cent to a contraction of 2 per cent.

The Information Note forecasts a rise of 0.4 points in the ratio of revenue to GDP – owing to an increase in social security contributions more than offsetting the further fall in tax revenue – and an increase of 1.4 points in the primary current spending ratio, above all due to employee compensation and social benefits. The latter's relatively strong growth reflects the automatic adjustment of pensions to 2008 inflation plus measures in favour of households (the consumption card and special bonus for low-income households) and reinforced unemployment benefits.

A further revision of the forecasts is expected with the forthcoming *Combined report on the economy and public finances*.

Table 14

Effects on net borrowing of the budget and the anti-crisis decrees
(*millions of euros*)

	2009	2010	2011
Three-year budget (1)	**9,893**	**17,137**	**30,925**
net change in revenue	4,662	4,961	5,523
net change in expenditure	-5,231	-12,176	-25,402
Finance Law for 2009 (1)	**0**	**0**	**0**
net change in revenue	-634	-321	-197
net change in expenditure	-634	-321	-197
Decree Law 185/2008 (1)	**32**	**192**	**185**
net change in revenue	2,988	884	406
net change in expenditure	2,956	691	222
Decree Law 5/2009 (1)	**3**	**4**	**13**
net change in revenue	702	-131	-206
net change in expenditure	699	-134	-219
Total effect (1)	**9,928**	**17,333**	**31,123**

Source: Based on official estimates contained in Ministry for the Economy and Finance, Department of the Accountant General, *La manovra di bilancio per il triennio 2009-2011*, February 2009.
(1) A positive sign indicates a reduction in net borrowing with respect to its value on a current legislation basis.

In the first quarter the accounts worsened more sharply

The deterioration of the public accounts that began towards the end of 2008 was accentuated in the first quarter of the new year. The state sector borrowing requirement came to €29.7 billion, €9 billion more than in the first quarter of 2008, mainly because of decreased revenue and increased expenditure on tax refunds. The general government borrowing requirement also worsened, amounting to €16.4 billion compared with €6.5 billion in the year-earlier quarter.

Table 15

Public finance objectives for 2009
(billions of euros and percentages of GDP)

	General government			*Memorandum items:*	
	Net borrowing	Primary surplus	Debt	GDP growth rate	Debt 2008
Objectives					
June 2008 (1)	32.7	50.1	....		
% of GDP	*2.0*	*3.1*	*102.7*	*0.9*	*103.9*
September 2008 (2)	34.1	49.7	....		
% of GDP	*2.1*	*3.0*	*102.9*	*0.5*	*103.7*
Estimates					
February 2009 (3)	57.7	20.2	....		
% of GDP	*3.7*	*1.3*	*110.5*	*-2.0*	*105.9*

(1) *Economic and Financial Planning Document*. – (2) *Forecasting and Planning Report*. – (3) *Stability Programme and Information Note 2009-2011*.

Revenue from the main taxes fell

In the first three months of 2009 total state tax revenues on a cash basis fell by 5.4 per cent compared with the first quarter of 2008. The decrease is greater than would be expected from the estimated performance of the relevant tax bases. Direct taxes decreased by 3.9 per cent (€1.8 billion), reflecting the sharp drop in the proceeds of the substitute tax on interest income and a contraction of 2.3 per cent in payroll withholdings, which had been especially large a year earlier owing to contract renewals. Indirect tax revenues fell by €2.8 billion or 7.2 per cent, owing to a decline in VAT on domestic consumption and imports from EU countries (7.4 per cent overall) and a very pronounced fall in VAT on imports from outside the EU (27.8 per cent). The data available also indicate a contraction in social security contributions in the first quarter.

FEBRUARY'S ANTI-CRISIS DECREE [1]

Decree Law 5 of 10 February 2009 reinforced the measures taken to support the economy in Decree Law 185 of 29 November 2008 (converted into Law 2/2009). According to official estimates, the new decree law will not affect the budget balance: through spending cuts and increases in revenue, it raises resources of €1.1 billion in 2009, €0.3 billion in 2010 and €0.4 billion in 2011, and uses them to stimulate aggregate demand, above all consumption of durable goods, and for tax relief for firms.

In 2009, the resources are being used to fund incentives to scrap highly polluting vehicles. Other provisions, which will begin to have an impact from 2010, introduce a 20 per cent tax credit on purchases of furniture, high-tech domestic appliances, television sets and computers for those who can already claim a 36 per cent personal income tax credit on the cost of building renovation work (€0.2 billion in both 2010 and 2011) and some concessions for firms (€0.05 billion and €0.2 billion respectively in 2010 and 2011). In particular, the decree establishes that companies in the same industrial district can opt for a collective tax regime. In this case, for at least a three-year period, taxes will be calculated based on a set income agreed with the tax authorities and then divided among the participating companies. The decree establishes tax reliefs for firms that form groups in 2009 and a reduction of the withholding tax rates on revalued properties introduced by decree at the end of November 2008.

The measure will be funded by increased revenue from VAT and taxes connected with motor vehicles (€0.7 billion in 2009), by revenue from controls on the legitimate use of privileges relating to stamp duty, mortgage tax and land registry tax and on inheritance and gift taxes (€0.1 billion in 2010; €0.2 billion in 2011) and by the effects of measures cancelling incentives for investments in disadvantaged areas (€0.3 billion in 2009 and €0.2 billion in 2010 and 2011).

Table

The effects of Decree Law 5/2009 on the general government consolidated accounts (1)
(millions of euros)

	2009	2010	2011
EXPENDITURE			
Measures that increase expenditure	**1,063**	**81**	**0**
Vehicle incentives	1,063	0	0
Guarantee fund for firms	0	81	0
Measures that reduce expenditure	**-364**	**-215**	**-219**
Cancellation of fiscal incentives	-311	-211	-215
Reduced contributions to industrial districts	-50	0	0
Other	-3	-4	-4
NET CHANGE IN EXPENDITURE	**699**	**-135**	**-219**
REVENUE			
Measures that increase revenue	**712**	**101**	**201**
Induced effects of vehicle incentives	654	0	0
Effects of furniture and domestic appliance incentives	43	0	0
Reduction of withholding tax rates on revalued properties	4	1	1
Controls on legitimacy of tax reliefs	10	100	200
Measures that reduce revenue	**-10**	**-232**	**-407**
Vehicle incentives	0	-11	-17
Furniture and domestic appliance incentives	0	-171	-200
Collective taxation for industrial districts and equalization of networks of firms	-10	-50	-50
Tax reliefs for aggregations of firms	0	0	-140
NET CHANGE IN REVENUE	**702**	**-130**	**-206**
CHANGE IN NET BORROWING (2)	**-3**	**-4**	**-13**

(1) Based on official estimates contained in the bill to convert the decree into law (Chamber of Deputies Act, Legislature XVI, no. 2187). – (2) A minus sign indicates a reduction in net borrowing.

[1] The amendments made to the decree upon its conversion into law on 8 April are not taken into account.

SELECTED STATISTICS

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

CONTENTS

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
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
2008	1.1	0.2	0.2	2.9	0.6	-5.0	-0.8	-0.3	-0.3	6.2	-3.5	1.4	-0.3
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
Q3	-0.5	-3.8	-2.8	5.8	1.1	-5.3	-0.8	-1.5	-1.6	3.0	-3.5	1.1	0.8
Q4	-6.3	-4.3	-3.0	1.3	0.3	-22.0	-3.4	-5.9	-6.1	-23.6	-17.5	-0.2	-0.1

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
2005	1.9	1.3	0.8	1.6	0.3	3.1	0.7	1.7	1.7	7.0	5.8	0.3	-0.1
2006	2.0	1.5	0.9	0.4	0.1	0.5	0.1	1.2	1.2	9.7	4.2	0.8	0.2
2007	2.4	0.7	0.4	2.0	0.4	1.1	0.2	1.3	1.3	8.4	1.5	1.1	0.3
2008	-0.6	0.5	0.3	0.9	0.2	-4.6	-1.1	-0.8	-0.8	1.7	1.1	0.1	-0.1
2006 – Q1	0.4	0.4	0.2	-1.0	-0.2	-3.1	-0.7	0.3	0.3	6.7	6.9	0.2	0.9
Q2	3.0	2.5	1.4	4.4	0.7	4.6	1.0	2.8	2.7	6.7	5.7	0.3	-0.4
Q3	2.1	-2.4	-1.3	6.5	1.1	-0.7	-0.2	0.7	0.7	8.3	-1.0	1.3	1.1
Q4	3.4	4.3	2.3	-4.8	-0.8	7.8	1.7	2.6	2.4	4.6	-1.1	0.8	-0.8
2007 – Q1	4.3	-1.4	-0.8	2.0	0.3	8.0	1.8	3.1	2.9	9.6	2.8	1.1	1.6
Q2	-1.1	1.7	0.9	6.3	1.1	-11.9	-2.9	-1.9	-1.8	8.8	4.6	0.8	-0.9
Q3	1.4	-0.4	-0.2	-1.9	-0.3	-1.7	-0.4	-0.4	-0.4	10.0	-1.2	1.6	0.5
Q4	4.0	1.5	0.8	7.4	1.2	-0.8	-0.2	2.1	2.0	12.4	1.4	1.7	0.1
2008 – Q1	1.4	2.9	1.6	-0.7	-0.1	-2.8	-0.6	0.1	0.1	12.6	6.2	1.3	-0.7
Q2	-4.5	-3.0	-1.7	-3.6	-0.6	-7.8	-1.8	-4.9	-4.7	-9.0	-11.7	-0.2	-0.6
Q3	-1.4	1.2	0.6	-0.6	-0.1	-6.4	-1.4	-0.9	-0.8	2.6	6.8	-0.3	0.1
Q4	-12.1	-1.7	-1.0	5.6	1.0	-11.0	-2.5	-0.6	-0.5	-44.9	12.4	-10.4	1.9

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' consumption expenditure (2)	General government consumption expenditure	Exports
				Construction	Machinery, equipment, sundry products & vehicles	Total			
				Chain-linked volumes					
2003	0.8	3.1	1.4	1.8	0.7	1.3	1.2	1.7	1.2
2004	2.1	7.0	3.4	1.2	3.5	2.3	1.6	1.6	7.4
2005	1.7	5.6	2.8	2.2	4.5	3.3	1.8	1.5	5.0
2006	2.9	8.2	4.4	4.4	7.0	5.6	2.0	1.8	8.3
2007	2.6	5.3	3.4	3.0	5.9	4.4	1.6	2.2	5.9
2008	0.8	1.2	0.9	....	....	..	0.4	2.0	1.3
2006 – Q4	0.9	2.4	1.3	1.2	2.1	1.6	0.8	0.7	3.6
2007 – Q1	0.7	1.0	0.8	1.3	0.7	1.0	-0.1	0.9	0.5
Q2	0.4	0.7	0.5	-1.2	1.7	0.2	0.6	0.3	1.1
Q3	0.6	2.0	1.0	0.7	1.1	0.9	0.4	0.5	1.7
Q4	0.4	-0.2	0.2	0.4	1.5	0.9	0.3	0.3	0.7
2008 – Q1	0.7	1.1	0.8	2.1	-0.2	1.0	..	0.4	1.5
Q2	-0.3	-0.5	-0.3	-2.2	-0.3	-1.3	-0.3	0.9	-0.2
Q3	-0.3	1.3	0.2	-1.1	-0.4	-0.7	0.1	0.6	-0.2
Q4	-1.6	-4.7	-2.6	-2.8	-5.3	-4.0	-0.3	0.4	-6.7
				Implicit prices					
2002	2.6	-2.1	....	....	....	1.4	1.9	3.1	-0.4
2003	2.2	-1.8	....	....	....	1.2	2.1	2.5	-1.3
2004	1.9	1.5	....	....	....	2.4	2.1	2.0	1.0
2005	2.0	3.3	....	....	....	2.5	2.1	2.4	2.4
2006	1.9	3.8	....	....	....	2.9	2.2	2.1	2.7
2007	2.3	1.3	....	....	....	2.7	2.2	1.7	1.5
2006 – Q4	0.5	-0.5	....	....	....	0.7	0.2	0.3	0.2
2007 – Q1	0.7	0.2	....	....	....	0.9	0.6	0.5	0.2
Q2	0.7	0.8	....	....	....	0.7	0.6	0.5	0.6
Q3	0.5	0.6	....	....	....	0.2	0.6	0.3	0.3
Q4	0.5	1.2	....	....	....	0.7	1.0	1.0	0.3
2008 – Q1	0.5	1.6	....	....	....	0.6	0.7	0.4	1.1
Q2	0.8	1.1	....	....	....	0.7	0.9	1.5	0.7
Q3	0.5	1.4	....	....	....	0.7	0.8	-0.5	0.9
Q4	0.5	-3.8	....	....	....	-0.1	-0.5	0.8	-1.6

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: Construction	Gross fixed capital formation: Machinery, equipment, sundry products & vehicles	Gross fixed capital formation: Total	Resident households' consumption expenditure	General government consumption expenditure (2)	Exports
Chain-linked volumes									
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	0.7	2.1	0.9	0.4	1.2	0.8	1.1	1.9	1.1
2006	2.0	5.9	2.8	1.0	5.0	2.9	1.2	0.5	6.2
2007	1.6	3.8	2.1	1.0	3.1	2.0	1.2	1.0	4.6
2008	-1.0	-4.5	-1.8	-1.8	-4.2	-3.0	-0.9	0.6	-3.7
2006 – Q4	1.1	3.0	1.5	2.4	1.9	2.2	0.2	0.5	4.5
2007 – Q1	0.2	0.8	0.4	0.2	-0.1	..	0.6	0.3	1.2
Q2	0.1	-0.8	-0.1	-1.8	1.1	-0.4	0.1	0.2	-1.5
Q3	0.2	0.8	0.3	0.8	-0.3	0.2	0.2	..	1.3
Q4	-0.3	-1.2	-0.5	..	0.7	0.4	-0.3	0.2	-0.1
2008 – Q1	0.3	-1.2	..	0.6	-1.1	-0.3	-0.1	..	-0.2
Q2	-0.6	-1.1	-0.8	-1.1	0.1	-0.5	-0.8	0.5	-1.0
Q3	-0.7	-0.7	-0.7	-0.4	-3.2	-1.8	0.2	0.1	-2.4
Q4	-1.9	-6.0	-2.8	-5.1	-8.9	-6.9	-0.8	..	-7.4
Implicit prices									
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	6.3	2.9	4.7	1.2	3.0	2.3	3.3	4.0
2006	1.8	7.7	3.1	3.3	2.1	2.7	2.7	2.4	4.6
2007	2.4	2.6	2.5	3.5	1.6	2.5	2.2	0.7	4.0
2008	2.8	6.9	3.7	3.6	2.9	3.2	3.2	3.8	5.0
2006 – Q4	0.2	-1.0	-0.1	0.8	-0.1	0.4	0.1	-1.1	0.4
2007 – Q1	1.0	0.2	0.8	1.2	0.8	1.0	0.5	..	1.2
Q2	0.8	1.8	1.0	0.7	0.3	0.5	0.6	1.0	1.5
Q3	0.7	1.4	0.9	0.4	0.5	0.4	0.8	..	0.7
Q4	0.5	0.7	0.6	0.9	0.1	0.5	0.8	3.4	0.8
2008 – Q1	0.3	2.7	0.9	0.8	1.7	1.2	0.8	-1.8	2.0
Q2	1.9	1.6	1.9	1.0	0.6	0.8	1.3	6.1	1.0
Q3	0.1	3.8	0.9	1.6	0.4	1.1	1.0	-3.9	2.0
Q4	0.4	-3.2	-0.4	0.7	0.3	0.5	-0.9	1.2	-0.5

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		
2005	1.8	2.9	1.8	-1.1	-1.1
2006	3.5	4.2	3.8	-0.3	-0.6
2007	2.8	3.4	3.6	0.2	-0.5
2008	....	....	-0.8	....	....
2006 – Q1	3.6	4.8	4.0	-0.8	-1.2
Q2	3.5	4.3	3.9	-0.4	-0.8
Q3	3.9	4.3	4.2	-0.2	-0.4
Q4	3.2	4.5	4.6	0.1	-1.2
2007 – Q1	2.4	3.5	3.9	0.4	-1.1
Q2	3.2	3.1	3.5	0.3	0.1
Q3	2.5	3.6	3.8	0.2	-1.1
Q4	3.2	3.1	3.3	0.2	0.1
2008 – Q1	3.5	2.3	2.7	0.3	1.1
Q2	2.7	1.1	1.2	0.1	1.6
Q3	3.2	-1.0	-1.2	-0.2	4.2
Q4	....	....	-7.1	....	....
			Services		
2005	2.1	0.5	1.9	1.4	1.6
2006	1.8	0.5	2.7	2.2	1.3
2007	2.4	0.6	2.7	2.2	1.9
2008	....	....	1.4	....	....
2006 – Q1	1.6	0.3	2.2	1.9	1.4
Q2	2.0	0.4	2.8	2.4	1.6
Q3	1.9	0.7	3.0	2.3	1.2
Q4	1.5	0.9	3.2	2.2	0.6
2007 – Q1	2.5	1.0	3.1	2.0	1.4
Q2	2.1	0.7	2.8	2.0	1.3
Q3	2.2	0.3	2.7	2.3	1.9
Q4	2.9	0.2	2.4	2.3	2.8
2008 – Q1	2.9	0.1	2.2	2.1	2.8
Q2	3.2	-0.2	1.6	1.8	3.4
Q3	3.4	0.0	1.2	1.3	3.4
Q4	....	....	0.4	....	....
			Total economy		
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	1.0	2.9	1.8	1.5
2008	3.5	0.1	0.9	0.8	3.4
2006 – Q1	2.1	1.1	2.5	1.3	0.9
Q2	2.4	1.2	3.0	1.7	1.1
Q3	2.4	1.4	3.1	1.7	1.0
Q4	2.0	1.6	3.4	1.8	0.4
2007 – Q1	2.4	1.5	3.4	1.9	0.9
Q2	2.3	1.0	2.8	1.8	1.2
Q3	2.3	0.9	2.8	1.9	1.4
Q4	3.0	0.7	2.5	1.7	2.2
2008 – Q1	3.1	0.8	2.3	1.5	2.3
Q2	3.2	0.4	1.6	1.1	2.7
Q3	3.4	0.1	0.7	0.5	3.3
Q4	3.0	-1.3	-1.3	0.0	4.3

Source: Based on Eurostat data.
(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	Productivity of which: Value added (3)	Productivity of which: Employees (2)	Unit labour costs
			Total industry excluding construction			
2006	2.8	3.6	2.2	3.1	1.0	0.6
2007	2.8	3.1	0.9	1.8	0.8	1.8
2008	3.3	3.1	-1.5	-3.2	-1.7	4.8
2006 – Q1	3.7	4.6	4.3	4.4	0.1	-0.5
Q2	2.5	3.2	1.1	2.6	1.4	1.4
Q3	2.6	3.3	1.2	2.5	1.2	1.3
Q4	2.4	3.3	3.3	4.4	1.1	-0.9
2007 – Q1	1.6	1.8	0.6	2.3	1.7	1.0
Q2	3.0	3.6	1.6	2.8	1.2	1.5
Q3	2.9	3.4	1.2	1.7	0.4	1.7
Q4	3.6	3.8	-1.4	-1.5	0.0	5.1
2008 – Q1	4.2	4.3	1.6	0.2	-1.4	2.5
Q2	3.0	2.7	0.5	-1.3	-1.8	2.5
Q3	3.5	3.1	-1.6	-3.2	-1.6	5.2
Q4	2.5	2.4	-6.4	-8.4	-2.1	9.6
			Services			
2006	2.7	3.1	0.0	1.8	1.8	2.7
2007	1.8	2.0	0.8	1.9	1.1	1.1
2008	3.3	3.3	-0.8	-0.2	0.6	4.1
2006 – Q1	3.3	3.6	0.0	1.1	1.1	3.3
Q2	5.6	6.0	-0.7	1.6	2.3	6.3
Q3	3.9	4.3	-0.1	2.0	2.1	4.0
Q4	-1.5	-1.0	0.8	2.4	1.6	-2.2
2007 – Q1	2.2	2.5	1.9	2.4	0.5	0.3
Q2	0.2	0.3	1.8	2.0	0.1	-1.6
Q3	1.0	1.1	0.0	1.9	1.9	1.0
Q4	4.0	4.0	-0.6	1.2	1.8	4.6
2008 – Q1	3.3	3.6	-1.1	0.8	1.8	4.4
Q2	4.7	4.8	-1.4	0.0	1.5	6.2
Q3	3.0	2.8	-0.3	-0.6	-0.3	3.3
Q4	2.1	2.2	-0.6	-1.2	-0.6	2.6
			Total economy			
2006	2.7	3.2	0.5	2.0	1.5	2.2
2007	2.2	2.3	0.7	1.7	1.0	1.4
2008	3.3	3.3	-0.8	-0.9	-0.1	4.0
2006 – Q1	3.2	3.7	1.0	1.9	0.9	2.2
Q2	4.5	5.0	-0.1	1.8	1.9	4.6
Q3	3.4	3.9	0.0	1.8	1.8	3.4
Q4	-0.3	0.3	1.1	2.7	1.6	-1.4
2007 – Q1	2.1	2.4	1.5	2.3	0.7	0.6
Q2	1.1	1.3	1.5	1.9	0.5	-0.3
Q3	1.5	1.7	0.2	1.7	1.5	1.3
Q4	3.8	3.9	-0.7	0.4	1.1	4.6
2008 – Q1	3.5	3.7	-0.2	0.5	0.8	3.8
Q2	4.2	4.2	-0.5	-0.2	0.3	4.7
Q3	3.2	3.0	-0.5	-1.1	-0.6	3.7
Q4	2.2	2.3	-1.9	-2.7	-0.9	4.2

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.

Table A7

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. energy and unprocessed food products	Total	Total excl. energy and unprocessed food products	Total	Total excl. energy and unprocessed food products	Total	Total excl. energy and unprocessed food products	Total	Total excl. energy and unprocessed food 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
2008	3.5	2.8	2.8	1.8	3.2	2.3	4.1	3.2	3.3	2.4
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
Sept.	3.9	3.0	3.0	1.7	3.3	2.3	4.6	3.4	3.6	2.5
Oct.	3.6	3.0	2.5	1.5	3.0	2.3	3.6	2.9	3.2	2.4
Nov.	2.7	2.8	1.4	1.4	1.9	2.1	2.4	2.7	2.1	2.2
Dec.	2.4	2.8	1.1	1.2	1.2	1.9	1.5	2.4	1.6	2.1
2009 – Jan.	1.4	2.0	0.9	1.2	0.8	1.6	0.8	2.0	1.1	1.8
Feb.	1.5	2.1	1.0	1.2	1.0	1.7	0.7	1.6	1.2	1.7

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
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	-37,344	3,205	-7,008	-19,675	-6,762	-7,103	2,849	-69	71	2,846
2008	(-52,962)	(153)	(-8,643)	(-28,684)	(-6,682)	(-9,105)	(2,374)	(-12)	(-19)	(2,405)
2007 – Q1	-12,572	-2,213	-3,363	-4,077	-1,278	-1,641	1,151	-1	29	1,123
Q2	-9,352	1,876	-1,082	-8,184	-1,742	-220	-56	-27	-15	-14
Q3	-4,911	2,411	-857	-2,724	-1,620	-2,121	578	25	-30	583
Q4	-10,508	1,130	-1,706	-4,689	-2,123	-3,120	1,176	-65	87	1,154
2008 – Q1	-16,343	-2,040	-3,318	-5,917	-2,027	-3,041	1,312	23	-22	1,311
Q2	-12,750	1,411	-620	-11,832	-1,526	-184	984	-26	14	996
Q3	-7,739	49	-335	-3,993	-1,855	-1,605	207	-2	6	203
Q4	(-16,129)	(732)	(-4,371)	(-6,942)	(-1,274)	(-4,274)	(-129)	(-7)	(-17)	(-105)
2007 – Jan.	-5,995	-2,731	-1,471	-1,443	-524	174	259	-3	10	252
Feb.	-2,998	-435	-806	-1,209	-174	-375	287	-6	8	285
Mar.	-3,579	953	-1,087	-1,426	-579	-1,441	605	7	11	587
Apr.	-4,369	-306	-868	-2,095	-516	-585	-4	-8	..	4
May	-4,183	510	-229	-3,470	-541	-453	17	-18	-4	40
June	-800	1,672	14	-2,619	-685	818	-69	..	-10	-59
July	2,379	3,116	305	-230	-525	-287	35	21	-21	35
Aug.	-3,265	-108	-1,006	-1,100	-459	-592	37	..	5	32
Sept.	-4,026	-597	-155	-1,394	-637	-1,243	506	3	-14	517
Oct.	-1,302	1,608	-126	-1,512	-797	-475	65	-47	1	111
Nov.	-4,042	603	-942	-2,502	-668	-534	153	-11	81	83
Dec.	-5,164	-1,081	-638	-675	-658	-2,112	957	-7	4	960
2008 – Jan.	-6,709	-3,300	-1,102	-1,383	-605	-318	366	9	23	334
Feb.	-3,316	899	-1,160	-2,241	-465	-350	306	17	-32	321
Mar.	-6,318	361	-1,056	-2,293	-957	-2,374	640	-4	-12	656
Apr.	-4,055	-35	-446	-2,184	-756	-633	21	-14	-7	42
May	-6,430	1,217	-588	-5,984	-558	-517	37	-4	1	40
June	-2,265	229	414	-3,663	-212	966	925	-7	19	913
July	1,187	3,312	569	-1,439	-740	-515	40	-10	-4	54
Aug.	-4,483	-1,627	-1,125	-577	-512	-642	50	-1	10	41
Sept.	-4,443	-1,636	222	-1,978	-603	-448	116	9	..	107
Oct.	-3,452	911	-1,511	-1,507	-513	-831	95	-1	-10	106
Nov.	-4,992	-408	-1,389	-2,175	-520	-499	83	-6	-6	95
Dec.	(-7,686)	(229)	(-1,471)	(-3,259)	(-241)	(-2,944)	(-306)	(..)	(-1)	(-305)
2009 Jan.	(-7,248)	(-3,129)	(-1,419)	(-2,246)	....	....	(341)	....	....	....

Table A9

Lending by banks in Italy 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 employees (2)	Producer (b) (3)	Consumer		Manufac-turing	Construc-tion	Services	
					Centre and North						
2007 – 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
Sept.	9.0	3.8	11.4	5.8	1.8	1.8	10.6	5.6	11.1	9.8	7.8
Dec.	6.0	-0.5	7.8	3.1	0.6	1.2	7.2	4.4	8.3	7.3	4.9
2009 – Feb.	7.3	-2.8	5.9	1.4	-1.1	-0.1	5.3	..	..	..	3.5
					South and Islands						
2007 – 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
Sept.	3.8	14.1	9.2	6.9	1.9	3.0	7.9	2.8	13.1	9.0	5.8
Dec.	4.2	11.2	6.2	4.8	-0.1	3.0	5.2	0.2	9.9	5.1	4.4
2009 – Feb.	5.2	3.4	4.7	3.2	-2.1	2.0	3.6	..	..	..	3.2
					ITALY						
2007 – 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
Sept.	8.5	4.1	11.1	6.0	1.8	2.0	10.2	5.2	11.4	9.8	7.5
Dec.	5.9	-0.3	7.6	3.3	0.4	1.6	7.0	3.9	8.6	7.0	4.8
2009 – Feb.	7.1	-2.7	5.8	1.7	-1.4	0.3	5.1	1.6	7.0	5.4	3.5

(1) Statistics for February 2009 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	*of which:* PO funds	Short-term securities	Medium and long-term securities	MFI loans (1)	Other operations (1)	*of which:* change in central bank current accounts	Borrowing requirement	*of which:* financed abroad
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	22,520	-2,525	14,779	13,142	26,359	-6,192
2008	4,224	-5,683	19,504	41,645	-1,526	-14,515	-10,611	49,333	-10,370
2006 – Q1	10,657	-891	18,406	13,007	2,474	-11,612	-16,246	32,932	-24
Q2	1,162	-1,615	7,154	28,742	-696	-25,553	-26,568	10,808	655
Q3	232	-1,210	-7,819	5,993	56,489	-39,102	12,948	15,792	1,289
Q4	-4,575	-1,240	-12,893	-14,637	9,806	21,590	21,637	-709	-8,934
2007 – Q1	-1,537	-3,474	20,684	7,523	-261	-5,506	-5,753	20,902	-527
Q2	-16,496	-13,509	345	28,729	-2,143	-8,731	-8,936	1,704	2,433
Q3	-2,330	-8,550	3,074	-2,809	-1,126	7,061	5,459	3,871	-6,288
Q4	6,387	-2,914	-18,541	-10,923	1,005	21,955	22,372	-117	-1,809
2008 – Q1	1,313	-1,111	25,905	23,405	266	-33,228	-31,203	17,661	466
Q2	934	-1,266	8,186	-11,264	3,804	5,508	5,968	7,168	-5,717
Q3	-2,295	-947	-1,120	4,054	-5,695	16,058	17,012	11,001	-2,287
Q4	4,272	-2,360	-13,467	25,450	100	-2,852	-2,388	13,503	-2,832
2008 – Jan	3,013	-36	14,516	7,222	-125	-26,608	-26,459	-1,982	2,124
Feb.	-3,532	-659	4,821	1,657	-655	6,201	6,883	8,492	243
Mar.	1,833	-415	6,568	14,525	1,047	-12,821	-11,627	11,151	-1,900
Apr.	-1,102	-195	4,215	10,695	615	-2,778	-2,661	11,645	1,973
May	-1,248	-333	5,125	-19,459	1,016	23,216	23,393	8,650	-5,159
June	3,283	-738	-1,153	-2,500	2,173	-14,931	-14,763	-13,128	-2,531
July	-3,084	342	-2,111	11,941	-4,893	-7,086	-6,948	-5,232	-2,743
Aug.	643	-321	796	12,460	-2,128	-8,814	-8,007	2,957	475
Sept.	146	-968	195	-20,347	1,326	31,958	31,967	13,276	-19
Oct.	1,541	-2,403	5,424	14,006	414	-8,225	-8,178	13,161	-568
Nov.	2,303	56	-4,078	16,079	1,493	-10,544	-10,493	5,252	-845
Dec.	428	-12	-14,812	-4,635	-1,807	15,917	16,283	-4,909	-1,419
2009 – Jan.	3,301	-344	12,227	19,189	357	-34,127	-34,126	947	7
Feb.	-2,698	-671	6,499	3,982	917	6,758	6,777	15,458	675

(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		Short-term securities	Medium and long-term securities	MFI loans (1)	Other liabilities (1)	General government debt			*Memorandum item:*
		of which: PO funds						*of which:* in foreign currencies	*of which:* medium and long-term	central bank current accounts
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	1,190,064	127,635	10,379	1,598,975	3,465	1,333,210	9,721
2008	147,252	31,492	147,373	1,236,435	126,113	6,476	1,663,650	3,609	1,370,711	20,333
2006 – Mar.	160,186	69,687	135,868	1,142,223	63,865	59,824	1,561,967	22,314	1,276,930	30,880
June	161,349	68,072	143,025	1,172,128	63,166	60,839	1,600,507	18,375	1,303,854	57,449
Sept.	161,581	66,862	135,204	1,178,358	120,357	8,789	1,604,289	15,116	1,314,434	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	129,900	8,989	1,609,883	5,020	1,318,815	28,616
June	138,972	48,639	143,349	1,203,468	127,756	9,194	1,622,739	4,908	1,347,193	37,552
Sept.	136,642	40,089	146,422	1,200,310	126,631	10,796	1,620,801	4,678	1,344,868	32,094
Dec.	143,029	37,175	127,869	1,190,064	127,635	10,379	1,598,975	3,465	1,333,210	9,721
2008 – Mar.	144,342	36,064	153,806	1,214,016	127,902	8,354	1,648,420	3,236	1,354,912	40,925
June	145,276	34,799	161,975	1,204,390	131,705	7,894	1,651,240	3,214	1,345,240	34,956
Sept.	142,981	33,852	160,869	1,211,082	126,011	6,939	1,647,881	3,537	1,346,537	17,944
Dec.	147,252	31,492	147,373	1,236,435	126,113	6,476	1,663,650	3,609	1,370,711	20,333
2008 – Jan	146,042	37,139	142,390	1,198,090	127,511	10,230	1,624,263	3,431	1,341,433	36,181
Feb.	142,510	36,479	147,224	1,199,954	126,855	9,548	1,626,091	3,391	1,342,073	29,297
Mar.	144,342	36,064	153,806	1,214,016	127,902	8,354	1,648,420	3,236	1,354,912	40,925
Apr.	143,241	35,869	158,037	1,225,265	128,516	8,238	1,663,296	3,284	1,366,777	43,586
May	141,993	35,537	163,148	1,206,048	129,532	8,061	1,648,782	3,290	1,347,699	20,193
June	145,276	34,799	161,975	1,204,390	131,705	7,894	1,651,240	3,214	1,345,240	34,956
July	142,192	35,141	159,861	1,217,550	126,811	7,756	1,654,172	3,237	1,355,547	41,905
Aug.	142,835	34,820	160,668	1,230,906	124,684	6,949	1,666,043	3,435	1,366,291	49,912
Sept.	142,981	33,852	160,869	1,211,082	126,011	6,939	1,647,881	3,537	1,346,537	17,944
Oct.	144,522	31,449	166,283	1,225,642	126,428	6,893	1,669,767	3,962	1,360,073	26,122
Nov.	146,824	31,505	162,200	1,242,757	127,921	6,841	1,686,543	3,979	1,377,893	36,615
Dec.	147,252	31,492	147,373	1,236,435	126,113	6,476	1,663,650	3,609	1,370,711	20,333
2009 – Jan.	150,553	31,148	159,600	1,256,070	126,472	6,475	1,699,171	3,910	1,390,818	54,459
Feb.	147,855	30,478	166,100	1,260,261	127,388	6,456	1,708,060	3,968	1,395,426	47,682

(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”.