What’s next for Italy?
National Association for Business Economics
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What’s next for Italy?

◆ **Economy:** Will it continue to expand?

◆ **Banks:** Positive developments, but are they still vulnerable?

◆ **Public finances:** What are the sources of risk? Can Italy be heading for a strong fiscal expansion?

◆ **Politics:** Will the government survive? What are the policy priorities?

◆ **Financial markets:** What are the risks over the next few weeks/months?

◆ **Economic/political scenarios:** Italexit, Syriza-like, or radicals to become mainstream? Or Italexit?
Divergence in GDP per capita since the launch of EMU

Source: Thomson Reuters Datastream, European Commission AMECO, LC-MA calculations.
Youth and long-term unemployment: a big concern

Source: Thomson Reuters Datastream, ISTAT, Eurostat, LC-MA calculations; 4-term moving average of quarterly data. (Very) Long-term unemployment = ratio of job seekers for more than (24) 12 months to labour force.
Will the political climate dent confidence?

Source: Thomson Reuters Datastream, ISTAT, LC-MA calculations.
High percentage of government bonds over total assets

Source: Thomson Reuters Datastream, ECB, LC-MA calculations.
Banks have reduced NPLs forcefully, but the stock is still high.

Source: Thomson Reuters Datastream, Bank of Italy.
Credit growth still somewhat depressed (ex securitisation)

Source: Bank of Italy, TR Datastream; unadjusted for securitisation unless specified. Discontinuity in the series in 2010.
So-called “austerity” was already over in 2014
A primary surplus steadily above 3% of GDP is key
The long maturity of public debt helps

*Italy - Implicit cost of debt financing and interest payments as % of GDP*


Impact of a 1% parallel shift in the yield curve on interest rate expenditure as % GDP: **0.11 after 1y, 0.25 2y, 0.36 3y, 0.45 4y**

Source: Thomson Reuters Datastream, European Commission Forecasts, Italian MEF, LC-MA calculations.
Who is afraid of TARGET balances?

Source: ECB, Thomson Reuters Datastream, LC-MA calculations.
ITALY – FINANCIAL MARKETS

Bank CDSs moving in parallel

Source: Thomson-Reuters Datastream, LC-MA calculations.
The percentage of debt held by non resident is still high.
The ESCB is the only buyer of Italy’s government paper

Source: Bank of Italy, ECB, Thomson Reuters Datastream, LC-MA calculations.
What’s next for Italy? Scenarios over the next 1-2 years

◆ 50% probability: Radicals to become mainstream. The 5SM and the League start behaving more responsibly and pragmatically, finding ways to claim they have delivered on promises.

◆ 45% probability: A Syriza-like trajectory. Populists try to deliver on electoral promises. They will eventually back down, but not before a new crisis and financial market turbulence. Help from Europe? Restructuring of debt?

◆ 5% Italexit. Confrontational stance towards Europe and departure from fiscal discipline cause a major crisis. No help from Europe, no desire to compromise or back down by the government. Reaction function: Italexit, i.e. 10 years of economic depression.

◆ Is it the start of a new Euro crisis? Eurozone contagion?