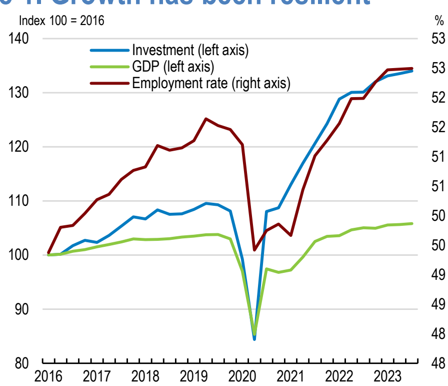
Executive summary

Growth has been resilient, but is slowing

The economy has weathered recent crises well, but growth is now slowing amid tightening financial conditions. Against the background of high public debt, the public finances need to be consolidated.

The energy crisis triggered a slowdown in activity. Large fiscal support and gains in competitiveness helped real GDP to rebound to its pre-pandemic level by mid-2021, with unemployment reaching historically low levels. However, high inflation in the wake of the energy crisis has eroded real household incomes and the tightening of euro area monetary policy has led to rapid increases in borrowing costs for households, businesses and the government.

Figure 1. Growth has been resilient



Source: OECD Economic Outlook database.

StatLink https://stat.link/jw3d2m

The tightening in financial conditions in the wake of euro area monetary policy tightening has been substantial. Lending rates to households and businesses have increased by around 3 percentage points since mid-2022. Credit growth has turned negative and the housing market has softened. The banking sector is well capitalised and better prepared to withstand shocks than in the past. But the banking and insurance sectors have substantial holdings of sovereign debt, requiring continued monitoring of balance sheet pressures that may arise from higher interest rates or the slowdown in growth.

Fiscal policy is now broadly neutral. Government support related to the energy crisis has partly been withdrawn and should end, but the National Recovery and Resilience Plan (NRRP) and targeted income tax cuts are supporting demand. If energy prices were to rise significantly again, only measures targeted to poor households should be re-introduced. With public debt high and on an upward trajectory under unchanged policy, the public finances will need to be consolidated.

OECD projections envisage subdued economic growth in 2024-25. Inflation is expected to decline gradually, as the energy price shock has led to wider price pressures that will take time to dissipate. Risks are tilted to the downside and tighter-than-expected financial conditions would further reduce domestic demand. On the upside, the faster spending of NRRP funds, including by re-focusing the Plan on large and centrally managed investment projects, as planned by the authorities and endorsed by the European Commission, could boost investment.

Table 1. Macroeconomic projections

Annual average growth, unless specified	2023	2024	2025
Gross domestic product (GDP)	0.7	0.7	1.2
Unemployment rate	7.6	7.8	7.6
Core inflation index	4.5	3.1	2.5
General government gross debt (% of GDP)	141.4	141.4	140.5

Source: OECD.

Putting public debt on a prudent path

Public debt is among the highest in the OECD as a share of GDP. With substantial fiscal pressures on the horizon, tax and spending reforms are needed to help put debt on a more prudent path.

The public debt to GDP ratio is on an upward trajectory under unchanged policies. Public expenditure on ageing-related costs and debt servicing costs are expected to increase by about 4½ percent of GDP between 2023 and 2040. Additional spending pressures are likely to arise from accelerating the climate transition and adapting to climate change. A sustained fiscal adjustment will be required over a number of years to put the debt ratio on a more prudent path, meet future costs and comply with proposed EU fiscal rules.

There is a need to make savings in government spending. Pensions account for a heavy share of overall spending. In the near term, this could be contained by phasing out early retirement schemes. The partial de-indexation of high pensions should be maintained in the near term but replaced in the medium term with a tax on high pensions that are unrelated to past pension contributions. This solidarity contribution of current pensioners could be maintained until the relative income of pensioners becomes more closely aligned with the OECD average. The forthcoming spending reviews – which currently target annual fiscal savings of around 0.2% of GDP – need to become more ambitious.

The ongoing tax reform should help address fiscal pressures. Efforts to tackle tax evasion should be continued, including by continuing to promote digital payments and reversing the increase in the ceiling on cash transactions. There is also room to reduce the erosion of the income tax base, including by reducing tax expenditures and limiting the proliferation of special flat tax regimes. Shifting taxes from labour to inheritance and property would make the tax mix more growth-friendly, while allowing revenues to increase. This should include updating the property tax base calculations, while taking into account distributional impacts.

Raising growth and inclusiveness

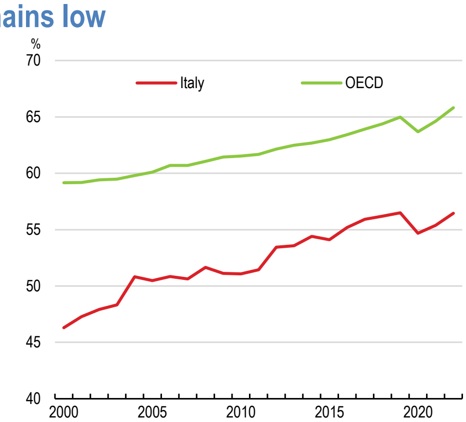
The economy faces challenges from low productivity growth, low labour market participation, especially of women, and relatively high poverty. Transitioning to innovation-led growth, while strengthening inclusiveness, will require a comprehensive package of reforms.

The ongoing civil justice and public administration reforms will be crucial to raise investment and productivity. The long duration of trials and excessive bureaucracy have held back private and public investment. The recent reforms to streamline legal and administrative procedures, raise capacity, and strengthen judges' and civil servants' performance incentives should be thoroughly implemented. Strengthening the mobility of public servants would reduce entrenchment in positions with excessive discretion over administrative procedures and thus the risk of corruption.

Remaining regulatory barriers to competition must be lifted, especially in professional services. "Fair compensation" rules for professional services risk being perceived as minimum tariffs, thereby reducing market entry and price competition. Their scope should be reduced. The competition reform legislated in 2022 should be fully implemented, including by submitting concessions to public tenders at expiry.

Labour market participation of young people and women is among the lowest in the OECD. Labour market prospects of young people could be improved by expanding technical tertiary schools (ITS Academy), and female labour market participation could be enhanced by significantly expanding early childhood education and further strengthening incentives for paternity leave.

Figure 2. Female labour market participation remains low



Source: OECD.

StatLink https://stat.link/8x50a4

The government has discontinued the Citizen's Income and introduced a new social assistance scheme (Adi) and an employment support scheme (Sfl). Work incentives of benefit recipients in the new scheme could be improved through a more gradual withdrawal of benefits in case of taking up employment. Expanding access to the social assistance benefit (Adi) to people with very weak labour market prospects at a reduced rate would ensure that limited funds for training are targeted to employable people, while ensuring that the most vulnerable remain covered by the social safety net.

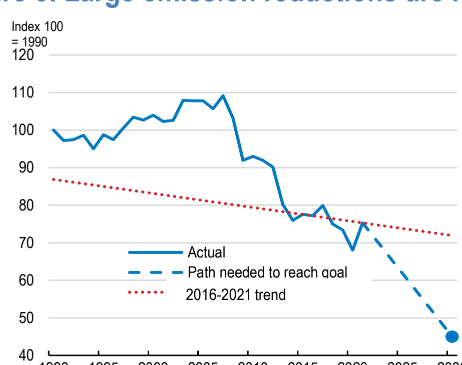
Strengthening the training system would help bring vulnerable people into the labour market. Lack of skills is a key barrier to employment. The NRRP provides funding for a new lifelong-learning programme that should be complemented with rigorous quality control for training providers. This includes introducing a national-level certification scheme for training providers and the expansion of existing programmes that make payment to training providers conditional on recipients durably finding employment.

Accelerating emissions reductions

The authorities aim for net zero greenhouse gas emissions by 2050. The economy's low energy intensity and abundant solar resources make Italy well placed to achieve the climate transition. But a further strengthening of existing measures and additional policies are needed to accelerate the reduction of emissions and adapt to climate change.

Significant progress in emissions reduction was made in the wake of the global economic crisis of 2008-09. The pace of emissions reduction has slowed over the past decade as growth has recovered and new policy action has slowed. Reaching the intermediate target of a 55% emissions reduction by 2030 (relative to 1990) will require a significant increase in the pace of emissions reduction. Enshrining the 2050 net-zero target in law and setting up an independent climate council for policy evaluation and advice could help strengthen government accountability.

Figure 3. Large emission reductions are needed



Source: OECD Greenhouse Gas Emissions dataset.

StatLink https://stat.link/8yaiem

The expansion of renewable electricity continues to be hampered by complex permitting processes despite recent streamlining. Fully unlocking the potential of renewables will require defining the criteria for the identification of suitable areas for renewable power plants, raising the capacity ceiling for simplified permitting procedures, and swiftly implementing key investments to enhance the transmission grid.

Improving public transport and reducing the number of highly polluting cars would reduce emissions from the transport sector. Transport could be further decarbonised by investing in the railway network, reducing the favourable tax treatment of diesel over gasoline and introducing financial incentives for the scrapping of old cars, irrespective of new car purchases. Electric vehicle (EV) use could be promoted by ramping up the deployment of publicly available electric charging stations, phasing out purchase subsidies for internal combustion engine cars and refocusing support on entry-level EVs, as well as aligning taxes on car sales, registration and ownership to emissions.

Retrofitting Italy's old building stock is crucial to decarbonise. Cost inefficient and regressive schemes that promote investment in energy efficiency renovations have been reformed but may be insufficient to induce retrofitting by low-income households with low tax bills. The current schemes should be complemented with a mix of subsidised long-term loans and grants, while subsidies for the installation of gas-powered boilers should be phased out. Regulatory measures or higher taxes for the rental of energy-inefficient properties would encourage energy efficiency renovations.

Approving the National Climate Adaptation Plan would equip Italy with a coherent adaption framework. Necessary investments are underway and appropriate funding will be key to sustainably mitigate the risk of flooding and landslides.

MAIN FINDINGS	KEY RECOMMENDATIONS
Supporting growth while bringing debt on a more prudent path	
GDP growth will gradually pick up over 2024-25. Public debt is on an upward trajectory at 2024 policies, limiting fiscal policy space	Steadily consolidate the public finances starting in 2025 to put debt on a more prudent path.
Delays in the implementation of public investment projects under the National Recovery and Resilience Plan (NRRP) risk reducing growth. The authorities have taken action to speed up implementation.	Re-focus the NRRP on large and centrally managed investment projects that can be delivered as foreseen by the revised NRRP.
Fiscal consolidation will require measures to limit the growth of public spending and enhance its efficiency over the coming years.	Introduce a solidarity contribution for high pensions that are not due to high contributions. Make the fiscal savings targets of the forthcoming spending reviews more ambitious.
The share of labour taxes in total revenue is higher than in OECD peers, while VAT collected and inheritance taxes are lower. A significant share of revenues is lost to tax evasion. The income tax base is eroded by costly tax expenditures. A recent enabling law foresees a comprehensive tax reform.	Shift taxes from labour to property and inheritance, while ensuring that revenue is maintained or increases. Update the property tax base calculations, taking into account distributional impacts. Continue to tackle tax evasion, including by continuing to promote the use of digital payments and reversing the increase in the ceiling on cash transactions. Phase out costly tax expenditures that lack economic or distributional justification, including, for instance, by limiting the coverage of the dependent spouse deduction.
Lifting potential growth and making it more inclusive	
The efficiency of the judicial system is weak, contributing to low productivity growth by weakening private investment and firm growth.	Continue strengthening the links between judges' performance, career progression and pay, and ensure that performance evaluation is thoroughly implemented.
Productivity growth is particularly weak in services, partly reflecting regulations that stifle competition, especially in professional services.	Reduce the scope of "fair compensation" rules in professional services.
Low tertiary education enrolment and graduation rates hold back innovation and digitalisation.	Continue to expand technical tertiary schools (ITS Academy).
Employment rates are low, partly due to weak financial incentives for social benefit recipients, and poverty is above the OECD average.	Make the withdrawal of benefits under the Adi and Sfl programmes more gradual in case of taking up employment. Expand access to the new social assistance benefit (Adi), including for people with very weak labour market prospects.
Labour market participation of women is among the lowest in the OECD.	Significantly expand coverage of early childhood education. Incentivise paternity leave by introducing a "father quota" or increasing the number of "bonus months" for leave taken by fathers.
Perceived corruption has declined markedly since the creation of the independent anti-corruption agency in 2014 but remains an issue.	Mandate the mobility of public servants within their administration, including local administrations.
Decarbonising the economy	
Monitoring of progress in climate change mitigation policy action and outcomes is a priority.	Set up an independent climate council for policy evaluation and advice.
Effective carbon tax rates differ widely across sectors and types of fuels, leading to large differences in abatement costs across sectors.	Follow up on plans to gradually raise excise taxes on fossil fuels when they are low, including by removing exemptions and rebates.
The ongoing "suitable areas reform" for the construction of new renewable energy power plants could speed up permitting, which, despite some recent streamlining, is still slow and complex.	Increase the ceiling below which installations in suitable areas can be authorised through the 'simplified enabling procedure' and maintain the environmental impact assessment exemption for low-capacity installations in suitable areas beyond July 2024.
The per capita car ownership rate is the second highest in the EU and a large share of cars is old and highly polluting.	Offer financial incentives for the scrapping of old cars, irrespective of new car purchases. Continue strengthening public transport and regional train networks.
The penetration of electric vehicles (EVs) is low, and a large share of EV purchase subsidies is unused.	Refocus car purchase support towards entry-level EVs and phase out subsidies for cars with internal combustion engines.
The regressive and cost-inefficient tax incentive system for energy efficiency home improvements has been reformed but may be insufficient to induce retrofitting by households with low tax bills.	Complement tax incentives for building retrofitting with targeted subsidised long-term loans and grants.
Italy is highly exposed to the consequences of climate change, as highlighted by recent extreme weather events. Necessary investments are underway.	Ensure appropriate funding for measures to reduce the risk of flooding and landslides.

From:

OECD Economic Surveys: Italy 2024

Access the complete publication at:
https://doi.org/10.1787/78add673-en

Please cite this chapter as:

OECD (2024), "Executive summary", in *OECD Economic Surveys: Italy 2024*, OECD Publishing, Paris.

DOI: https://doi.org/10.1787/9652c6b1-en