

## *Executive summary*

### ***After a modest recovery, the economy is weakening***

- *In recent years, supportive global economic conditions, expansionary monetary policy, structural reforms and prudent fiscal policy supported Italy's gradual economic recovery.*
- *However, the recovery has slowed.*

### ***Italy continues to suffer from long-standing social and economic problems***

- *Real GDP per capita is roughly the same as in 2000 and well below its pre-crisis peak.*
- *Absolute poverty rates for young people rose sharply as a result of the crisis and remain high.*
- *The already large regional differences in GDP per capita and employment rates have widened over recent decades.*
- *Renewable energy capacity has expanded rapidly from 2000 to the mid-2010s but has since stalled.*

### ***A comprehensive reform package holds the key to stronger growth and social inclusion***

- *Italy faces the double challenge of reviving growth and making it more inclusive while putting the public debt on a steady downward path.*
- *Increasing productivity growth is key to raising living standards and to offsetting the large negative effect of demographics and a shrinking labour force.*
- *A credible medium-term plan to reduce the debt-to-GDP ratio will improve fiscal credibility and help contain the risk premium on government debt.*
- *Public spending needs to become more efficient and better targeted with a fairer tax system.*
- *The health of the banking system has improved but challenges remain.*

### ***In-work benefits and a moderate guaranteed income scheme would boost employment and reduce poverty***

- *A key part of making growth stronger and more inclusive involves increasing formal employment.*
- *The success of any guaranteed minimum income scheme will hinge on improving job-search and training programmes.*

### ***More effective regional development policies and strengthening capacity at the local level would help to narrow the regional divide***

- *Rationalising and improving coordination among the bodies involved in regional development policies by strengthening the role and expertise of central-government bodies would make regional policies more effective.*

### After a modest recovery, the economy is weakening

In recent years, supportive global economic conditions, expansionary monetary policy, structural reforms and prudent fiscal policy supported Italy's gradual economic recovery.

Exports, private consumption and more recently investment drove growth, buttressed by a shift of export industries towards higher value added products. The employment rate has increased by 3 percentage points since 2015 and the health of the banking system has improved.

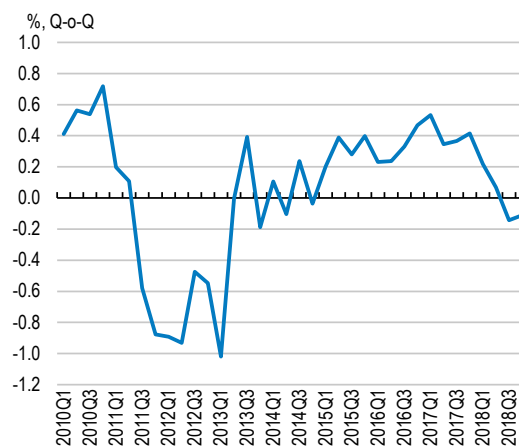
However, the recovery has slowed. GDP is projected to contract by 0.2% in 2019 and expand by 0.5% in 2020. Expansionary fiscal policy and low growth will push the general government budget deficit to 2.5% of GDP in 2019 from 2.1% in 2018. The 2019 budget rightly aims to help the poor but its growth benefits are likely to be modest, especially in the medium term. The new guaranteed minimum income (Citizen's Income), which replaces the Inclusive Income Scheme (REI), allocates significant additional funds to anti-poverty programmes, but its effectiveness will depend critically on marked improvements in job search and training programmes. The reduction in the retirement age – to 62 years with at least 38 years of contributions – will lower growth in the medium run by reducing work among older people and, if not actuarially fair, will worsen intergenerational inequality and raise the public debt.

### Italy continues to suffer from long-standing social and economic problems

Real GDP per capita is roughly the same as in 2000 and well below its pre-crisis peak.

Though the employment rate has risen, it is still one of the lowest among OECD countries, especially for women. Job quality is low and the mismatch between people's jobs and their skills is high by international comparison. Productivity growth has been sluggish or negative for the past 20 years.

Figure A. GDP growth has slowed



Source: OECD Economic Outlook 104 database, including more recent information.

StatLink <https://doi.org/10.1787/888933947692>

Table A. The economy is projected to recover gradually

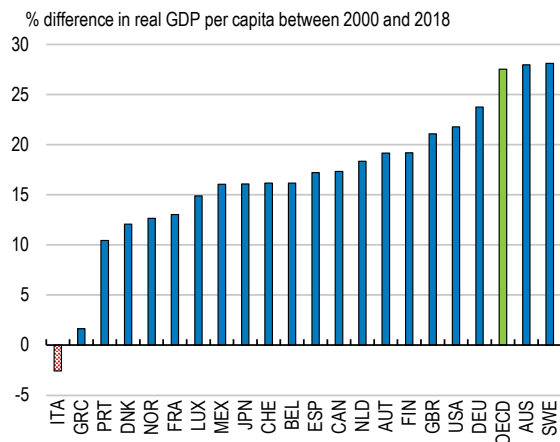
Annual % change, unless otherwise indicated

	2018	2019	2020
Gross domestic product	0.8	-0.2	0.5
Private consumption	0.6	0.5	0.5
Gross fixed capital formation	3.2	-0.2	1.1
Exports	1.4	2.7	2.3
Imports	1.8	2.1	2.7
Unemployment rate (%)	10.6	12.0	12.1
Consumer price index	1.2	0.9	0.8
Fiscal balance (% GDP)	-2.1	-2.5	-3.0
Public debt (gross, % of GDP)	132	134	135
Current account (% of GDP)	2.6	2.7	2.4

Source: OECD Economic Outlook 104 database, including more recent information.

Absolute poverty rates for young people rose sharply as a result of the crisis and remain high. Poverty rates vary widely between regions and in southern regions are among the highest in the EU. Only a small share of social benefits (excluding pensions) for the working age population go to the people most in need. The dearth of job opportunities pushes many young people to emigrate, exacerbating Italy's already fast population ageing.

**Figure B. Italy's GDP per capita is at the same level as 20 years ago**



Source: OECD *Economic Outlook 104* database, including more recent information.  
StatLink <https://doi.org/10.1787/888933947787>

**The already large regional differences in GDP per capita and employment rates have widened over recent decades.** Regional disparities in employment rates explain much of the difference in living standards among regions.

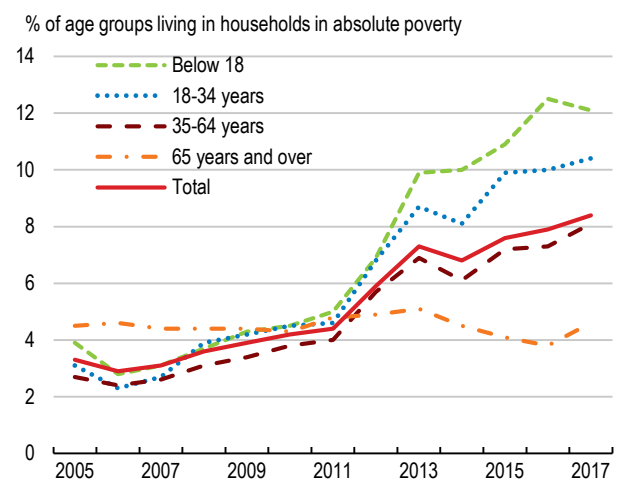
**Renewable energy sources have expanded rapidly from 2000 to the mid-2010s but have stalled since then.** Air pollution is high in some area, resulting in high mortality and harming well-being. Other environmental challenges result from weaknesses in public administration, reflected in patchy waste collection and management and deficient hydrological risk management. The administrative fragmentation and limited power of metropolitan bodies is an obstacle to the integration of land use and transport policies, hampering the design of low-emission growth policies.

**A comprehensive reform package holds the key to stronger growth and social inclusion**

**Italy faces the double challenge of reviving growth and making it more inclusive while putting the public debt on steady downward path.** Tackling Italy's structural challenges requires a multi-year reform package to achieve stronger and more inclusive growth, and revive confidence in the reform capacity of the country.

The ambitious reform package proposed in this Survey would support stronger employment, improve well-being and raise productivity growth. By 2030, annual trend GDP growth would increase from 0.6% under current policies to above 1.5%. If accompanied by a rise of the primary surplus to above 2%, the proposed reform package would help to put the debt-to-GDP ratio on a downward path.

**Figure C. Absolute poverty rates rose during the crisis and remain high, especially for the young**



Source: ISTAT *Poverty* database.  
StatLink <https://doi.org/10.1787/888933947711>

**Increasing productivity growth is key to raising living standards and to offsetting the large negative effect of demographics and a shrinking labour force.** This will require: enhancing competition in markets that are still protected, such as professional services and local public services; raising innovation and business dynamics, including through targeted incentives connected to the Industry 4.0 plan; removing obstacles hampering the growth of SMEs; and enhancing the efficiency of public administration by raising accountability and transparency and pursuing the digitalisation of the public sector.

**A credible medium-term plan to reduce the debt-to-GDP ratio will improve fiscal credibility and help contain the risk premium on government debt.** Without sustainable fiscal

policy, the room to enhance infrastructure, help the poor and deliver the public services people expect will inevitably narrow. Designing budgets within the EU Growth and Stability Pact, which should be implemented in a pragmatic way, would help to strengthen fiscal credibility by providing an anchor to fiscal policy. If fiscal credibility can be improved rapidly, a falling risk premium on government debt would accelerate the reduction of the debt ratio.

**Public spending needs to become more efficient and better targeted with a fairer tax system.** Designing thorough spending reviews during the preparation of the yearly budget and effectively implementing them would promote priority-setting and spending re-allocation, contributing to free up resources for effective public programmes and public investment. Improving voluntary tax compliance and vigorously fighting tax evasion are key for tax revenues and allow for a reduction in tax rates, making the tax system fairer.

**The health of the banking system has improved but challenges remain.** The government strategy to deal with insolvent banks through a mix of resolutions, recapitalisations and acquisitions has yielded fruit. Banks' capital ratios are above minimum requirements. The stock of nonperforming loans in banks' balance sheets has fallen markedly over the last two years and profitability has returned, though it remains low. The banking sector is undergoing a rationalisation and consolidation process, but the reform to cooperative banks is still to be fully implemented. The health of the banking sector is closely linked with public finance and its effects on government bond yields. Lower government bond yields would help to safeguard the stability of the banking sector.

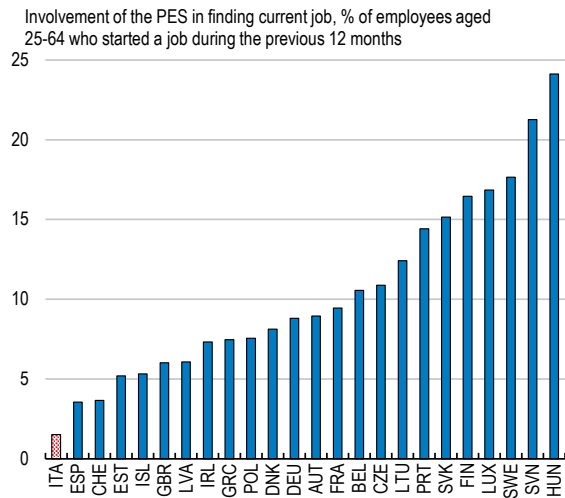
**In-work benefits and a moderate guaranteed income scheme would boost employment and reduce poverty**

**A key part of making growth strong and more inclusive involves increasing formal employment.** Italy's tax and benefit system and

social services can do more to support employment in low-wage regions and for second earners. The transfer and eligibility rules of the Citizen's Income will need to ensure work incentives are strengthened and not weakened because of higher transfers. The level of the transfer provided by the current plan for the Citizen's Income risks encouraging informal employment and creating poverty traps. Ensuring transfers are conditional on well designed and monitored employment and social inclusion "pacts" is key to supporting beneficiaries to move into employment. Introducing an in-work benefit system and lowering the Citizen's Income benefit to about 70% of the relative poverty line (50% of the median equivalised household income) would contribute to raising employment, especially in lagging regions, and protecting households from poverty.

**The success of any guaranteed minimum income scheme will hinge on improving job-search and training programmes.** This will depend on implementing a multi-year plan to revamp public employment services based on higher investments in IT systems, profiling tools and human resources, especially in lagging regions where social needs are greater and more urgent. Developing strong partnerships with private-sector job-search and training agencies and extending the existing training voucher to include both Citizen's Income beneficiaries and other job seekers would improve their job prospects. Stronger collaboration and coordination between public employment service and municipalities' social assistance programmes would help to achieve the Citizen's Income objectives. Integration of immigrants through language and professional training courses and certifying immigrants' skills would support social inclusion, and boost labour force participation.

**Figure D. Italy's public employment services help few jobseekers find work**



Source: Calculations based on EU-LFS 2014.

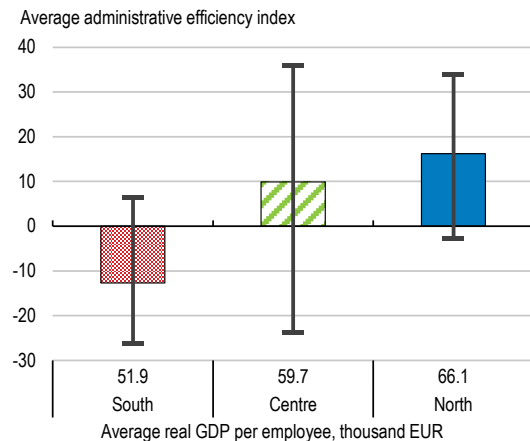
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**More effective regional development policies and strengthening capacity at the local level would help to narrow the regional divide**

**Rationalising and improving coordination among the bodies involved in regional development policies by strengthening the role and expertise of central-government bodies would make regional policies more effective.** Funds for regional development policies need to add to, and not to substitute for, ordinary spending. The ordinary public administration needs to offer a more similar level of essential services across the whole country. Setting and enforcing minimum performance standards for services provided by sub-national administrations, such as active labour market

policies or waste management, would go in the right direction. Local public administrations that repeatedly fail to achieve these minimum standards should undergo a restructuring programme in collaboration with better performers and the central government to strengthen capacity, reorganise processes and enhance accountability and transparency. Improving the governance of metropolitan areas would enhance agglomeration economies and strengthen the role of metropolitan cities as engines of green growth. Progress in this area will hinge on regions and municipalities sharing some of their functions and budget with metropolitan bodies.

**Figure E. Higher efficiency of municipalities is associated with higher productivity**



Note: The administrative efficiency index is the percentage difference between assessed spending needs given conditions and actual spending. A higher value indicates greater efficiency.

Source: OECD *Regional Statistics* database; and OpenCivitas.

StatLink <https://doi.org/10.1787/888933947749>

## MAIN POLICY FINDINGS

## KEY RECOMMENDATIONS

**Boosting sustained and inclusive growth**

After a modest economy recovery, real GDP per capita is still lower than in 2000 and the economy is now slowing. The health of the banking system has considerably improved but challenges persist. Poverty remains high especially among the young. The 2019 budget introduced a fiscal easing, mostly through higher current spending (especially social transfers). The relaxation of early retirement rules will raise already high pension spending. The debt to GDP ratio will gradually increase and public finances remain vulnerable to higher interest rates.

The tax system is complex and tax administration highly fragmented. Many tax expenditures are poorly targeted. Despite recent progress, tax evasion remains high and cash payments are used more than elsewhere.

Public investment has fallen as a share of GDP. The central and sub-national governments have failed to use all available funds for public investment due to poor project preparation and slow execution. The new public procurement code is well thought out but its slow implementation has hindered public investment.

Develop a multi-year programme of institutional, economic and social reforms and do not reverse important measures taken in recent years. Boost fiscal credibility by setting out a medium-term fiscal plan within the EU Growth and Stability Pact, aiming to steadily raise the primary surplus. Continue to pursue reforms to boost productivity including measures to improve the efficiency of the judicial system through improvements in administration processes and greater use of alternative dispute resolution. Fully implement the reforms of cooperative and of mutual banks, and complete the reform of the insolvency regime.

Reverse the changes in early retirement rules introduced in 2019 and preserve the link between retirement age and life expectancy.

Continue to improve voluntary tax compliance and avoid repeated tax amnesties. Lower the maximum threshold for cash payments. Abolish tax expenditures that are poorly targeted or have outdated objectives.

Continue to improve coordination across tax administration agencies.

Create, as planned, a technical support unit for public investment using existing administrative structures and ensure it is well staffed.

Simplify the most complex aspects of the public procurement code but protect the powers of the anticorruption authority.

Develop a comprehensive public investment and spatial plan linking infrastructure developments with land use management.

**Tax and benefits reforms to reduce poverty and encourage employment**

Poverty remains high, especially in lagging regions and among families with children while in-work poverty is rising. The new guaranteed income scheme (Citizen's Income) will greatly increase resources to fight poverty but its sustainability and effectiveness hinge on significantly improving public employment and social services. Adults out of work have little effective support from public employment services to prepare for and find stable formal sector jobs.

The employment rate, while at a record high, is low by international standards. Informal work is high, especially in lagging regions. Current tax and benefit rules are complex and lead to high effective tax rates, especially for low wage earners and second earners, weakening incentives to find jobs in the formal sector. The Citizen's Income risks weakening work incentives further.

Implement a multi-year plan to revamp public employment services based on enforcing essential service standards and higher investments in IT systems, profiling tools and human resources.

Ensure capacity to administer the Citizen's Income by building on and strengthening, where necessary, municipalities' social assistance services and establishing strong collaboration between them and public employment services.

Provide more quality infant care places at a low cost relative to average wages, prioritising regions with low female employment.

Reduce the labour income tax wedge on low-income workers and second earners through lowering employer social security contributions and tax and benefit reforms, while maintaining the tax system's progressivity.

Lower and taper off Citizen's Income benefits to encourage beneficiaries to seek employment in the formal sector and introduce an in-work benefit for low-income earners.

**More effective investments in regional development and strengthening capacity at the local level**

Institutional setting of regional development policies is complex and coordination between bodies, at central and local level, is weak, leading to poor disbursement of regional development and EU cohesion funds and contributing to regional disparities.

Metropolitan governance bodies have little power, limiting agglomeration economies.

The agency (ANPAL) to coordinate active labour market policies has little power to ensure regional agencies achieve essential service standards.

Much municipal waste is recycled but the rate of recycled waste varies greatly among regions, generating health hazards in some areas and harming green growth.

Rationalise and improve coordination among bodies involved in regional development policies by strengthening the role and expertise of central government bodies.

Empower metropolitan governance bodies with the transfer of some of the powers of regions and provinces.

Grant to ANPAL the power to restructure public employment services that repeatedly fail to meet commonly agreed performance targets.

Restructure operations relating to waste management of sub-national governments that repeatedly fail to reach targets for waste collection and recycling.



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