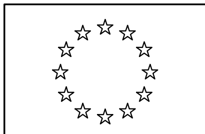

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COMMISSION STAFF WORKING DOCUMENT

Assessment of the 2012 national reform programme and stability programme for ITALY

Accompanying the document

Recommendation for a

COUNCIL RECOMMENDATION

on Italy's 2012 national reform programme and delivering a Council Opinion on Italy's updated stability programme for 2012-2015

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EXECUTIVE SUMMARY

In 2012, Italy's economic activity is expected to contract by 1.4%, and gradually recover in 2013. The unemployment rate is foreseen to increase further to 9.5% this year and 9.7% in 2013.

In the past few months, the policy response to ensure sound public finances and tackle Italy's long-standing structural weaknesses has been determined and wide-ranging. It has touched upon a whole range of areas including taxation, pensions, competition in product and services markets, the business environment, efficiency of the public administration and recently, the labour market.

Italy continues to face important and serious challenges in a number of areas. The dualism in terms of economic development between the North and the South remains an overarching concern. The full implementation of the bold fiscal consolidation strategy is a pressing need. The weak external competitive position requires better alignment of wage and productivity developments. A heavy tax burden on labour adversely affects labour supply and demand. Reducing tax evasion and improving compliance require further determined action. Labour market participation and employment rates are still low, in particular for young people, women and older workers. The overall quality of the education and training system is unsatisfactory, with high levels of early school leaving and low participation in lifelong learning. Significant infrastructure gaps and a lack of competition in the network industries, in particular energy and transport, are hindering economic activity. The business environment is not growth-friendly due to administrative inefficiencies, burdensome regulations and significant weaknesses in the civil justice system.

1. INTRODUCTION

Procedural aspects

In June 2011, the Commission proposed six country specific recommendations1 (CSRs) for economic and structural reform policies for Italy. In July 2011, the Council of the European Union adopted these recommendations2 which concerned the public finances, the labour market, competition, business environment, research, innovation and cohesion funds.

In November 2011, the Commission published its Annual Growth Survey for 20123 (AGS 2012) in which it set out its proposals for building a common understanding about the priorities for action at national and EU level in 2012. It focused on five priorities — growth-friendly fiscal consolidation, restoring normal lending to the economy, promoting growth and competitiveness, tackling unemployment and social consequences of the crisis, and modernising public administration — and encouraged Member States to implement them in the 2012 European Semester.

Against this background, in April 2012 Italy presented its 2012 national reform programme and stability programme, which were then endorsed by the Italian Parliament. These programmes provide details on progress made since July 2011 and plans going forward. The national reform programme was prepared in consultation with the local authorities and the social partners.

This Staff Working Document assesses the state of implementation of the 2011 country-specific recommendations as well as the Annual Growth Survey for 2012 in Italy, identifies current policy challenges and, in this light, examines the country's latest policy plans.

Overall assessment

The policy response to ensure sound public finances and tackle Italy's long-standing structural weaknesses has been determined and wide-ranging. Italy is implementing a bold fiscal consolidation strategy which is expected to correct the excessive deficit by 2012 and enable the country to achieve the medium-term objective of a broadly balanced budgetary position in structural terms by 2013, i.e. one year earlier than recommended in the country-specific recommendations issued in 2011. A further major improvement in fiscal governance, namely the introduction of a balanced budget rule in the Constitution, is another sign of Italy's commitment to sound public finances. Italy has put in place a wide range of growth- and competitiveness-enhancing measures in the areas of taxation, pensions, competition in product and services markets, the business environment, efficiency of the public administration and, more recently, the labour market. These measures address most of the country-specific recommendations issued in 2011. Notwithstanding these important achievements, full implementation of the adopted measures remains challenging, especially when it requires the cooperation of many actors, and there remains scope to progress further in the reform agenda.

Italy's most pressing challenges remain in the areas of the public finances, the labour market, education and market regulation, while there is scope to make the tax system more growth-enhancing and to increase the efficiency of civil justice. In particular, there is a need to fully implement the ambitious fiscal consolidation strategy. Addressing the

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[1] SEC(2011) 810 final of 7 June 2011

[2] OJ C 215 of 21 July 2011

[3] COM(2011) 815 final of 23 November 2011

vulnerable situation of young people on the labour market is another key challenge for Italy, especially in the light of the sharp increase in youth unemployment in the aftermath of the deep economic crisis. There is also scope to further enhance competition in the network industries.

Overall, the reform agenda set out in the national reform programme is relevant and ambitious to address Italy's challenges. If properly implemented, it would make a significant contribution to increasing the sustainability of the public finances and enhancing Italy's growth potential.

2. ECONOMIC DEVELOPMENTS AND CHALLENGES

2.1. Recent economic developments and outlook

Recent economic developments

The Italian economy entered recession again in the second half of 2011. The acute tensions recorded in the sovereign debt markets in the final months of 2011 and the resulting loss in economic agents' confidence led to a sharp fall in demand. Consequently, real GDP growth over 2011 as a whole was only 0.4 %, after 1.8 % in 2010.

The rise in employment that began in the last quarter of 2010 came to a halt in the closing months of 2011. The unemployment rate is estimated to have risen to 9.8 % in March 2012, the highest rate since July 2000, with more than one in three active young people being jobless. Inflationary pressures were relatively strong in the first half of 2011, then abated in the following months thanks to cost moderation and slack demand. In the last months of 2011, however, the increase in indirect tax rates contributed to driving up consumer prices.

Given the very high public debt ratio, Italy refrained from undertaking a large fiscal stimulus during the crisis, allowing the government deficit-to-GDP ratio to remain below the euro-area average in 2009-11. Still, the debt ratio climbed to 120 % of GDP by the end of 2011, mainly reflecting the severe fall in GDP. The sharp increase in the cost of borrowing in the last months of 2011 as a result of the aggravating sovereign debt crisis signalled the risk of a liquidity crisis due to the large debt rollover scheduled for the first months of 2012.

Outlook

According to the Commission services' spring 2012 forecast, real GDP is expected to contract by 1.4 % in 2012 and then gradually recover in 2013. Real GDP is set to continue falling in the first half of 2012, as spending and investment plans of consumers and firms are held back by poor labour market prospects and persistently high uncertainty in financial markets. Economic activity is expected to stabilise in the second half of the year, assuming no further worsening in financial market conditions and yields on 10-year Italian sovereign slightly below 6 %.

The current account deficit is expected to narrow in 2012-13 from the 3.2 % of GDP deficit recorded in 2011, on the back of depressed domestic demand and declining imports. By contrast, exports are set to continue increasing in line with sustained demand from extra-EU trade partners. No major improvement is expected in cost competitiveness as nominal unit labour costs are projected to rise broadly in line with the rest of the euro area: wage increases in the private sector are expected to be moderate, and public sector wages have been frozen for the entire 2011-14 period, while overall productivity is set to stagnate. Harmonised Index of Consumer Prices inflation is set to rise to 3.2 % in 2012,

driven by higher oil prices and further indirect tax increases and then fall back below 2 % at the end of the forecast period.

Employment is projected to decline. At the same time, labour force participation is set to continue recovering, driven by gradually rising participation by the older age groups — due to the recently adopted pension reforms — and a return to the labour market of inactive workers that are now pushed back to job seeking by the fall in households' disposable income. As a consequence, the unemployment rate is projected to rise further in 2012-13.

Consistency across the stability programme and the national reform programme, notably in terms of macroeconomic scenario and inter-linkages between fiscal and other macroeconomic areas, is ensured by the integration of the two documents within the Document on the Economy and Finance (Documento di Economia e Finanza) which also includes, in a third section, the analysis of trends in public finances. The stability programme and the national reform programme are consistent respectively with the Code of conduct and the guidance provided by the Commission.

2.2. Challenges

Italy is faced with the twin challenges of a very high public debt and persistently low growth. These challenges long pre-date the global financial crisis and largely explain investors' mounting concerns with the sustainability of Italy's public debt in an environment characterised by high risk aversion. There is a feedback loop between low growth and concerns about sustainability that works both ways: low growth makes it more difficult to achieve and maintain the large primary surplus that is needed to drive down the debt ratio, while concerns about debt sustainability increase pressure on interest rates and dampen economic agents' confidence, with negative impact on domestic demand and overall economic activity. Therefore, although the large fiscal consolidation effort may depress domestic demand and growth in the short term, it is a pre-requisite for restoring confidence and successfully putting in place a strategy to boost growth. There is also scope to improve the quality of the public finances in a growth-enhancing way by increasing the effectiveness and efficiency of public spending, further shifting the tax burden away from the factors of production and improving tax compliance and tax governance. The Italian tax system is still characterised by significant tax evasion and the administrative costs of revenue collection are in the upper range of the EU spectrum.

Over 1999-2007, Italy's real annual GDP growth averaged only 1.5 %, around ¾ percentage point (pp) below the performance of the euro area as a whole. This mainly reflects low productivity growth, in particular as total factor productivity growth dramatically declined. Following the deep recession recorded in 2008-09 and the temporary mild recovery of 2010-11, the level of real GDP is projected to be around 6 pps lower in 2012 than in 2007. Low productivity growth largely explains the significant loss in external competitiveness that Italy has recorded for over a decade. An unfavourable product specialisation and geographical orientation of its exports also contribute to this development (see Box 1).

Finally, Italy still suffers from significant dualism in terms of economic development between the North and the South, with the South's dismal performance largely due to its

inability to unlock its labour potential.[4] This remains an overarching concern for Italy that intensifies the challenges across most policy areas.

Despite considerable progress over the past decade, participation and employment rates are still very low, particularly among women, young people and older workers, and long-term unemployment is high among young workers, especially in the South. The heavy tax burden on labour has a negative impact on labour supply and demand, and the provision of adequate and affordable childcare and elderly care facilities remains insufficient. The creation of new permanent jobs is chronically weak. Piecemeal labour market reforms in the past eased labour market entry conditions by increasing the number of non-standard employment contracts, but they did not alter the traditional configuration of the Italian labour market, based on the protection of insiders by means of tight conditions for individual dismissals and preferential access to a system of unemployment benefits that hampers occupational and sectoral mobility. As a result, employment has increased, but at the cost of increased segmentation. Many outsiders – notably young and female workers – suffer from both job precariousness and inadequate income support when out of work. During the 2008-09 crisis the coverage of unemployment benefits was extended to categories of workers previously ineligible because of sector, firm size or type of employment contract but the system is still fragmented and benefits are often provided on a discretionary basis. Finally, income inequality is high by international standards and low-skilled workers, children and large households are particularly exposed to the risk of poverty and social exclusion.[5]

Wage increases do not adequately reflect local labour market conditions and productivity. This is particularly relevant in the context of the weak productivity growth, which has gradually eroded the cost competitiveness of the Italian economy as a whole, while contributing to the persistence of regional disparities in labour market performance.

Italy lags behind other EU countries in terms of human capital formation. Italian pupils have a mixed score on the OECD Programme for International Student Assessment, with performance in the northern regions in line with or above the EU average but significantly worse in the South. Despite various educational reforms, early school leaving remains a major challenge. Tertiary education attainment and adult participation in lifelong learning are also low, hampering the upskilling of the labour force. A production specialisation model still focused on traditional labour-intensive sectors with limited intensity of research, development and innovation, together with the small size of Italian firms, tend to limit the demand for high-skilled workers and the development of research and development capabilities.

Capital accumulation is also hampered by a series of factors, including relatively high corporate taxation and a complex tax system, as well as a corporate governance culture and institutional features that contribute to maintaining a highly fragmented economic structure with a prevalence of small-sized firms that highly rely on banks to raise funds. Infrastructure gaps also hinder economic activity and limit the attractiveness of the country for foreign investment. To start with, Italy suffers from a severe energy infrastructure gap and the use of existing structures is sub-optimal. Facilities to import

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[4] Regional imbalances in Italy are quite large. Unemployment and low female participation are concentrated in the southern regions. The employment rate varies greatly, with more than 21 pps of difference between north-eastern (67.6 %) and southern regions (46.5 %).

[5] According to Eurostat, in 2010 24.5 % of Italian population was at risk of poverty or social exclusion, compared with an EU average of 23.5 %.

and store gas struggle to cope with extreme events and are inadequate to meet the needs of a country that aims to be a 'gas hub' for the EU. The high share of imported gas in electricity generation means that the security of electricity supply ultimately relies on secure gas supply.[6] Despite recent progress, competition in the gas sector remains limited and the electricity sector is still highly concentrated in some areas of the country. Lack of adequate infrastructures determines an often suboptimal use of generation capacity which, combined with market shortcomings, results in high energy prices for consumers. Italy is heavily dependent on imported energy and the further development of renewables could play an important role in sheltering the country from external energy supply shocks. The transport sector also faces a number of challenges, mainly in the railway and maritime transport sectors. In spite of increased competition in high-speed services, the degree of market opening in the railway sector is still suboptimal. The Italian National Railways Company still controls both the Infrastructure Manager and the main incumbent operator for passenger and freight transport, which undermines the functioning of the sector. In the area of maritime transport, poor interconnections with inland transport and limited competition are other important challenges for Italy.

Infrastructure development in Italy would benefit from an improved use of EU cohesion funds, better focused on growth-enhancing projects. The absorption capacity of these funds remains particularly low in the southern regions.

Italy's regulatory environment is weighed down by public administration inefficiencies, burdensome business and labour regulations, a complex tax system and costly enforcement of contracts due to crucial weaknesses in the Italian civil justice system. Furthermore, the still incomplete implementation of the Services Directive at local level contributes to the difficult business environment.

Box 1. Summary of the results of the in-depth review under the macroeconomic imbalances procedure

On 14 February 2012, the European Commission presented its first Alert Mechanism Report, prepared in accordance with Regulation (EC) No 1176/2011 on the prevention and correction of macroeconomic imbalances. The report identifies Italy as one of the 12 Member States whose macroeconomic situation needs to be scrutinised more in-depth in order to identify actual or potential imbalances and the possible macroeconomic risks which they may entail.

The main imbalance affecting the Italian economy is the high government debt. Combined with the unsatisfactory growth prospects, it represents the main vulnerability of the Italian economy, with negative impact on the banking sector and the real economy and potential negative spillovers to the euro area as a whole. In addition, Italy has been losing external competitiveness since euro adoption, mainly due to stagnant productivity growth and an unfavourable export structure. While the current account deficit remains contained, its negative trend could entail significant macroeconomic risks for Italy and the euro area as a whole. The main observations of this review are:

• The high government debt represents a major imbalance of the Italian economy, with negative effects on the real economy and potential spillovers to the euro area as a whole. The high taxation - present and expected - needed to service it and put it on a sustainable path weighs on labour and capital costs. In addition, the higher risk premia associated with a high public debt affect the cost of capital also for the financial sector and the real economy. Other channels are the increased macroeconomic uncertainty and a reduced margin for countercyclical fiscal policies. Finally, the euro-area sovereign crisis has shown the potential negative spillovers from debt accumulation in a monetary union. Although during the crisis the increase in the debt ratio was more moderate than in the rest of the euro area, its high level has exposed the

[6] Italy is the biggest net importer of electricity in the EU, covering almost 15% of its electricity needs through imports.

country to investors' concerns about sustainability, especially against the background of a lacklustre growth performance and amid high risk aversion.

• Italy has been recording declining competitiveness since the end-1990s, due to both cost and non-cost factors. This is most evident in Italy's world market share losses, while it is only partly reflected in Italy's external position, given the relatively subdued growth of domestic demand. While the current account deficit does not breach the scoreboard threshold, its negative trend needs to be reversed to continue ensuring the sustainability of Italy's external position.

• Stagnation in productivity is the key factor behind Italy's loss of cost competitiveness since the euro adoption. Cost competitiveness, measured by the real effective exchange rate (REER) based on unit labour costs (ULC), worsened against the main euro area competitors in the first years of euro area membership. While Italy's productivity has lagged relative to the euro area average, wages have grown broadly in line, if not somewhat faster, resulting in more sustained ULC dynamics. The most recent estimates point to a relatively small overvaluation of Italy's REER and thus to a still manageable adjustment if wage developments are consistent with the need to regain cost competitiveness and if the implementation of bold structural reforms is successful in boosting productivity growth.

• An unfavourable product specialisation and geographical destination of exports also explain declining competitiveness. With an export product mix that is rather similar to that of emerging economies, Italy has been exposed more than other euro area countries to increasing global competition. As a partial response to these competitive pressures, restructuring had started in the tradable sector before the crisis: while maintaining its specialisation in labour-intensive sectors, Italy's exports moved up the quality ladder. Italy's exports are also held back by their still relatively low penetration into fast-growing emerging markets, especially in Eastern Asia. The small size of the Italian firms plays a key role in hindering the reorientation of exports towards distant markets.

3. ASSESSMENT OF POLICY AGENDA

3.1. Fiscal policy and taxation

Budgetary developments and debt dynamics

The stability programme update confirms the main goal of Italy's fiscal consolidation strategy, presented by the government in September and renewed in December 2011, to reach a balanced budgetary position in structural terms,7 i.e. Italy's medium-term objective, by 2013. The medium-term objective adequately reflects the requirements of the Stability and Growth Pact. The plan to reach it in 2013 is more ambitious than the one presented in the April 2011 programme update and on which the July 2011 Council recommendation was based, which aimed at narrowing the structural deficit to ½ pp of GDP by 2014. The plan incorporates the measures taken in the summer and December 2011 in response to the sovereign debt crisis and high risk aversion in financial markets.

In nominal terms, the programme plans to reduce the headline deficit to 1.7 % of GDP in 2012, i.e. the deadline for correcting the excessive deficit, and achieve a broadly balanced headline budget in 2014. The targets are backed by the measures adopted in 2010 and 2011 for the years 2012-14 (see Table in Box 2). The consolidation effort is frontloaded in 2012, when the programme projects a (recalculated) structural adjustment of 3.2 pps of GDP, followed by a further 1 pp of GDP in 2013 which would enable the country to achieve the medium-term objective in that year.

In 2011, Italy's budgetary position improved in line with the target: the general government deficit fell to 3.9 % of GDP (from 4.6 % in 2010 and 5.4 % in 2009) and the primary balance moved to a surplus of 1 % of GDP (after 0.0 % in 2010 and -0.9 % in 2009). Deficit-improving one-off measures contributed to the outcome, compensating for the lower-than-planned current revenues. Interest expenditure rose by 0.3 pp of GDP, while the deficit reduction was almost entirely due to primary expenditure that fell by 1 pp of GDP (to 45.1 %). Current primary expenditure grew moderately, mainly thanks to the freeze in public wages and recruitment, while capital spending fell significantly on the back of both further reductions in subsidies to investment and the one-off sale of broadband licences, recorded as negative expenditure. Total revenues rose by 0.1 pp of GDP (to 46.1 %), mainly owing to the one-off capital tax on the revaluation of corporate assets. Indirect taxes also rose, while income taxes remained flat.

In 2012 the programme projects the deficit to decline to 1.7 % of GDP and the primary surplus to further improve to 3.6 % of GDP, thanks to the sizeable budgetary consolidation measures adopted in 2010-11 and despite the underlying lower growth prospects compared to the 2011 programme update. The programme's macroeconomic outlook for 2012 is broadly in line with the spring forecast. It includes a more moderate fall in domestic demand, almost entirely offset by a less positive contribution of net exports. This implies a more tax-rich GDP composition in the programme than in the spring forecast, which explains most of the 0.3 pp of GDP difference in the deficit projection. On the back of the freeze of wages, career developments and recruitment, plus the partial de-indexation of pensions, in 2012 the programme projects current primary expenditure to rise marginally in nominal terms and remain flat as a share of GDP, broadly in line with the spring forecast. The latter expects a somewhat steeper growth in interest expenditure, counterbalanced by a slight fall in capital spending, which

[7] Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission services on the basis of the information provided in the programme, using the commonly agreed methodology.

is instead projected to stagnate in the programme. Thanks to the several revenue-raising measures adopted in 2011, current tax revenues are projected to grow by more than 10 % and increase sizeably as a share of GDP, i.e. considerably more than expected in the spring forecast, mainly due to the different composition of growth. In both projections, capital taxes are set to decline sharply in 2012. Taken at face value, the deficit target for 2012 is well below the 3 % reference value. In structural terms, the projected (recalculated) annual adjustment of 3.2 pps of GDP goes beyond the 0.5 pp minimum average annual adjustment required under the excessive deficit procedure. The structural primary balance is projected to rise by 3.5 pps to 4.8 % of GDP. Risks stem from both the implementation side, as some measures need strict enforcement to produce the budgeted expenditure savings, and the macroeconomic side, as growth could turn out lower and interest expenditure higher than projected should the sovereign market tensions escalate again.

The programme's growth outlook for 2013 is quite close to the spring forecast's, the main difference being the more favourable outlook for domestic demand in the programme, against the still negative contribution expected in the spring forecast. This has visible implications for the dynamics of revenues, which are projected to increase by almost ½ pp of GDP in the programme, whereas they remain flat as a share of GDP in the spring forecast. Total expenditure projections are very similar, with somewhat higher interest expenditure expected in the spring forecast, only partly compensated by lower capital spending.

Overall, the headline deficit projection of 0.5 % of GDP in the programme appears optimistic when compared to the 1.1 % of GDP in the spring forecast. The programme projects a higher primary surplus (4.9 % of GDP) than the spring forecast (4.5%). In the latter, the expected increase in the structural primary surplus in 2012-13 is around 4 pps of GDP, with structural revenues increasing by 2½ pps of GDP and structural primary expenditure falling by 1½ pps of GDP. Still, the spring forecast expects the budget to be balanced in structural terms in 2013.

According to the information provided in the programme and to the Commission services' forecast, the growth rate of government expenditure, net of discretionary revenue measures, over 2013 will not exceed a rate which is lower than the reference medium-term rate of potential GDP growth (-0.8 %) and which ensures an annual structural adjustment towards the medium-term objective by 0.5% of GDP.

Over 2014-15, the growth rate of government expenditure, net of discretionary revenue measures, planned in the programme does not exceed the reference medium-term rate of potential GDP growth (0.3 %). It should be noted that the programme's projections for 2014-15 do not include any further adjustment in structural terms: the achievement of a balanced headline budget in those years depends on the materialisation of the benign growth outlook forecast in the programme (real GDP growth of 1.0 % in 2014 and 1.2 % in 2015).

Box 2. Main measures

Main budgetary measures adopted in 2010-11

Revenue	Expenditure
2011	
Measures to improve tax compliance (0.1% of GDP) Increase in standard VAT rate (0.3% of GDP)	Lower transfers to sub-national governments (-0.4% of GDP) Freeze of public sector wages and restrictions on recruitment (-0.1% of GDP) Cuts to non-obligatory ministerial spending (-0.1% of GDP)
2012	
Re-introduction of owner-occupied dwelling taxation and rise in tax rates on other property (0.7% of GDP) Excise duties (0.5% of GDP) Stamp duties on financial assets (0.3% of GDP) VAT rates (0.2% of GDP) Harmonisation of personal withholding tax rate on interests and dividends (0.1% of GDP) Regional surtax on personal incomes (0.1% of GDP) Tax compliance improvement and recovery of unpaid taxes (0.5% of GDP) ACE and deductibility of labour costs (-0.15% of GDP)	Lower transfers to sub-national governments (-0.2% of GDP) Cuts to non-obligatory ministerial spending (-0.4% of GDP) Partial de-indexation of pensions (-0.1% of GDP) Other current expenditure (local authorities, military missions abroad) (0.2% of GDP)
2013	
• VAT rates (0.6% of GDP) • Stamp duties on financial assets (0.2% of GDP) • Solidarity tax on high public wages (0.1% of GDP) • Higher social contributions on self-employed (0.1% of GDP) Tax compliance improvement and recovery of unpaid taxes (0.1% of GDP) • Deductibility of labour costs (-0.2% of GDP) • ACE and deductibility of labour costs (-0.15% of GDP)	• Savings from higher retirement age, de-indexation of pensions and postponed end-career payments (-0.4% of GDP) • Smaller cuts to non-obligatory ministerial spending (0.2% of GDP)
2014	
• ACE and deductibility of labour costs (-0.1% of GDP)	• Savings from higher retirement age, de-indexation of pensions (-0.1% of GDP)

Notes: The budgetary impact in the table is the incremental annual impact reported in the programme, i.e. by the national authorities. A positive sign implies that revenue / expenditure increases as a consequence of this measure. Permanent measures are not repeated in successive years, unless the budgetary impact changes significantly. The no-policy-change baseline excludes any wage contract renewals until 2015.

The degree of detail reflects the type of information made available in the stability programme and the multi-annual budget.

Italy also adopted several macro-structural measures that are meant to increase the growth potential, without directly impacting the budgetary balance. They are described and assessed in the subsequent sections.

As from 2008, the general government gross debt as a share of GDP started increasing again mainly due to negative real GDP developments. It reached 120.1% in 2011 (from 103.1% in 2007). The programme plans the debt ratio to peak in 2012 – also given the significant contribution to the euro-area firewalls sustained by Italy – and start declining as from 2013, thanks to large and increasing primary surpluses.

At end-2011, the average maturity of State securities was 7 years, while their financial duration was around 4.7 years, i.e. somewhat below the corresponding values at end-2010 (7.2 and 4.9 years respectively). Thanks to these relatively long durations, according to the sensitivity analysis presented in the programme, a permanent increase of 1 pp in the entire yield curve as from end-March 2012 would increase interest expenditure by only 0.19 % of GDP the first year, 0.36 % in the second year and 0.44 % in the third year. These increases are slightly lower than estimated in the previous programme, as now the planned cash borrowing requirement to be financed is much lower.

Over 2012-13, the debt projections in the programme are similar to those of the spring forecast. The debt-increasing impact of the difference between the real interest rates paid on debt and real GDP growth is slightly higher in the latter, while the debt-reducing primary surpluses are somewhat larger in the programme. Achieving the targeted large primary surpluses would put the debt-to-GDP ratio on a steadily declining path. This would help improve financial markets' perception of the debt sustainability and create a virtuous circle by reducing yields on Italy's sovereign securities.

In 2013-14 Italy will be in transition period and its budgetary plans would ensure sufficient progress towards compliance with the debt criterion. According to plans, the debt benchmark will be met at the end of the transition period (2015).

Long-term sustainability

Over the long term, the change in age-related expenditure is below the EU average, also thanks to recent measures which contribute to more than stabilising pension spending as a share of GDP. In addition, the initial budgetary position is already sufficient to put the debt on a steadily declining path as, assuming no further policy measures are taken, it would fall to 95.9 % of GDP by 2020. Achieving the budgetary targets in the programme would help reduce the debt even faster by 2020, though it would still be above the 60 % of GDP reference value. Ensuring sufficient primary surpluses over the medium term, as planned in the programme, would thus significantly improve the sustainability of public finances.

Fiscal frameworks

On 17 April 2012, the Italian Parliament adopted a law introducing a balanced budget rule in the Italian Constitution, with effect from 2014. The amended Constitution stipulates that all government subsectors must contribute to ensuring the budgetary equilibrium of the whole general government, consistently with the EU legislation. It thus entrusts regions with the responsibility to maintain a balanced budget at the regional level, while still allowing local governments to borrow to finance investment. The implementing legislation will need to specify key features of the new rules, including correction mechanisms to compensate for temporary deficits during cyclical downturns

or exceptional circumstances, coordination mechanisms between the different levels of government and guarantees for the independence of a monitoring body attached to Parliament.

Part of the consolidation effort enacted in legislation passed in 2011 relies on expenditure savings by central and local administrations. The process of expenditure rationalisation will be facilitated by the planned in-depth spending review. In the short-term, the government plans to achieve savings of 0.3 % of GDP in 2012, with the cooperation of all ministers. In the meantime, a broader review of expenditure is under preparation. The government is appropriately prudent in its expectations of the amount of immediate savings that the spending review will yield, and is placing more emphasis on ensuring permanent mechanisms that promote efficiency and effectiveness of public spending. In this review, however, growth-enhancing expenditure items (e.g. education, innovation) should have the priority.

Fiscal de-centralisation in Italy remains incomplete, with transfers from the central government continuing to fund a large share of regional and local expenditure. This has resulted in major vertical fiscal imbalances, with sub-central governments spending more than one third of total general government expenditure in 2009, despite having limited revenue autonomy. The completion of fiscal federalism can be an important complement to structural reforms and budget consolidation in Italy. By empowering sub-central governments and making them more accountable to citizens in their use of public money, it can improve the allocation of public resources and the relationship between taxpayers and the government. However, strong fiscal de-centralisation clearly requires an equally strong framework for budgetary coordination across government levels. In the short term, reinforcing control on sub-central expenditure through strict enforcement of the domestic stability and health pacts remains a priority. In the longer term, detailed rules governing implementation of fiscal federalism must be designed in a way that fosters fiscal discipline.

Tax system

The additional fiscal consolidation effort made since summer 2011 in response to the sovereign debt crisis mainly focuses on revenues, entailing a further increase in the already high overall tax burden. However, as announced under the Euro Plus Pact commitments, the new measures somewhat rebalance the tax burden from labour and capital to consumption and property, which is appropriate given Italy's strong reliance on direct taxes and the growth-enhancing potential of such a shift, while the design of the measures increases the overall fairness of the system. They include the increased deductibility of labour costs from firms' tax bases, particularly for women and young workers; increased taxation of real estate with a revaluation of the taxable base; higher taxes on financial assets and specific luxury goods. The government is also planning a wide-ranging reform of tax expenditures which should help simplify the tax system and could impact on other spheres of the economy. For instance, the subsidy associated to the tax treatment of the private use of company cars has negative effects on the environment.

Besides, a new enabling law on the tax reform adopted by the government on 16 April aims at (i) simplifying the tax system through the revision and streamlining of tax expenditures; (ii) making it more environmentally friendly; (iii) improving tax compliance and stepping up the fight against tax evasion, (iv) replacing personal income tax for micro businesses and the self-employed with a flat corporate tax and (v) improving fairness through a revision of cadastral values so as to bring them closer to market values.

Tax reforms recently undertaken and planned are an important step towards making the tax structure more growth-friendly. The increased tax deductibility of labour costs for women and young people is bound to support access of these two particularly disadvantaged groups to permanent employment, especially in the South. The increased emphasis on property taxation, including the planned revaluation of cadastral values, should increase the fairness as well as the growth-friendliness of the tax system. Recurrent taxes on property are indeed less distortive than other types of taxes, they offer a more predictable source of revenue and are consistent with the goal of decentralising fiscal powers in Italy. From a distributional point of view, the higher tax rate on non-principal dwellings and the basic allowance on principal ones will ensure some degree of progressivity. There remains scope for further shifting taxation away from labour and capital onto property and consumption, also with a view to favouring second earners' participation. Lastly, improving the recovery of unpaid taxes remains a key challenge for Italy.

3.2. Financial sector

Concerns about sovereign risk and increased investor aversion for peripheral euro area sovereign debt coupled with subdued macroeconomic prospects for the Italian economy put additional pressure on the funding costs and profitability of Italian banks in the second half of 2011. Banks struggled with severe stress in the euro-area interbank market and sharply increased retail and wholesale funding costs. This, coupled with the increase in loan-loss provisions as asset quality deteriorated, has contributed to a fall in banking sector profitability.

Concerns over sovereign debt markets and difficulties on the interbank market resulted in a call by the European Council on 27 October 2011 for a temporary increase in banks' Core Tier 1 capital ratio to 9 % by mid-2012 (above the threshold laid down as part of the Basel III package); this increase is coordinated by the European Banking Authority. In December 2011, the European Banking Authority established the need for four Italian institutions[8] to further increase capital by a total of EUR 15.37 billion. Unicredit was among the first banks to raise new capital (via a rights issue in December 2011) and by February 2012 all banks concerned submitted to the European Banking Authority compliance plans, on which the Authority expressed an overall favourable opinion. In addition, the funding pressure on Italian banks was alleviated by the two long-term refinancing operations by the European Central Bank, first in December 2011 and then again in February 2012. This initially led to a substantial improvement of the financing conditions for banks.

As regards small and medium enterprises' access to finance, which is covered by the 2011 recommendation on competition and business environment and the 2012 AGS, the situation has worsened over the last few months. The Bank of Italy and business organisations report substantial tightening in credit supply to non-financial corporations. Measures recently adopted by the government can improve firms' financial conditions and avert the risks of credit crunch. First, an allowance for new corporate equity was introduced, which allows companies to deduct part of the notional return on new injections of equity capital from taxable income. Second, the Guarantee Fund for small and medium enterprises was refinanced. Finally, EUR 5.7 billion were made available to accelerate the payment of old trade credits (above two years) to suppliers of goods and services to the central public administration.

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[8] Unicredit, Banca Monte dei Paschi di Siena, Banco Popolare, Unione di Banche Italiane.

These measures are clearly relevant. In particular, the allowance for new corporate equity is expected to encourage firms, including small and medium enterprises, to increase their capital base, while overcoming the debt bias of the tax system regarding investment financing decisions (i.e. v-à-v equity). This appropriately tends to favour more innovative firms. Overall, however, the development of further alternative, non-bank, financing options for companies is still insufficient.

3.3. Labour market, education and social policy

Labour force participation and employment rates are well below EU averages, particularly among young people, and Italy is still far from achieving the 67-69 % national target set for 2020 as regards the employment rate. This reflects a number of factors, including the high tax burden on labour, an education system that does not effectively respond to labour market needs and insufficient focus on adequate active labour market and work-life balance policies. A segmented labour market hampers labour market dynamism and generates inequality.

Measures adopted in 2011 and detailed in the national reform programme go towards meeting the 2011 recommendation on the labour market and the 2012 Annual Growth Survey priorities. In addition to the above-mentioned increased deductibility of labour costs from firms' tax bases, particularly for women and young workers, incentives were introduced to promote the hiring of unemployed women in disadvantaged areas. These measures help stimulate labour demand, in particular for two critical segments of Italy's labour market, and thus they are relevant. Yet, increasing female employment remains one of the most important priorities for the Italian labour market. The female participation rate in Italy is significantly lower than the EU27 average, and the female unemployment rate is rising. While the employment rate among childless women of prime working age is already considerably lower than for the euro area average — by almost 12 pps in 2010 — particularly among the low skilled, the gap opens up for women with at least two children. Increasing the availability and affordability of childcare services remains an important challenge for Italy.

On 4 April, following consultation with the social partners and other main stakeholders, the Italian government adopted a draft ordinary law with a view to reforming labour market functioning. The reform is sufficiently ambitious to comprehensively address the rigidities and asymmetries of employment protection legislation while better regulating flexibility at entry and moving towards a more integrated social safety net. As such, it addresses labour market segmentation, as recommended in the country-specific recommendations issued in 2011. The reform introduces disincentives against temporary contracts and measures to combat the abuse of non-dependent work by firms. Exit flexibility is improved by revising Article 18 of the Workers' Statute regulating wrongful individual dismissals in firms with more than 15 employees. For collective dismissals, the draft law aims to simplify procedural obligations and reduce costs to employers. Lastly, an integrated and more comprehensive insurance-based system of unemployment benefits will be introduced as from 2017. Wage supplementation and short-term working schemes will no longer apply to workers that lose their job as a result of a firm's or plant's closure but will be extended to sectors that are currently not covered.

Reform of the dismissal regulation potentially reduces the uncertainty and overall costs for employers linked to dismissals, by limiting the scope for reinstatement and capping back-wages due in case of unfair dismissal, and by accelerating the dispute settlement process. The effectiveness of the reform will also depend on the interpretation of the new rules by the labour judges. The constraints introduced to the use of fixed-term contracts and to combat the abuse of non-dependent work aim to promote permanent contracts as

the "common form of employment relationship", however the risk of a negative impact on overall labour demand cannot be neglected. The reform of the social safety net is a positive step, but the provision of effective activation policies will be critical to avoid any negative impact on labour supply incentives and public finances.

Undeclared work remains a major issue in Italy. The national statistical institute (ISTAT) estimates that the shadow economy accounts for between 16 % and 18 % of GDP, with peaks in six southern regions (Molise, Basilicata, Campania, Puglia, Calabria and Sicilia). It represents around 12 % of total full-time equivalent employment. The national reform programme reports on the intensification of control activities and the positive effects expected from the liberalisation of employment services.

Regarding the 2011 recommendation on wage bargaining (also reflected in the 2012 Annual Growth Survey priorities on wage setting/productivity), on 28 June 2011 the social partners reached an agreement to reform the bargaining framework with a view to increasing the use of firm-level contracts. A provision in the September 2011 package allowed firm-level bargaining to derogate also from labour law on various aspects of the employment relationship, including dismissal procedures and type of contracts to be used in firms. Tax incentives on performance-related pay, which are negotiated at firm level, were extended to 2012. These initiatives support decentralised bargaining by decreasing its degree of subordination from the first tier of bargaining and removing the constraints to locally negotiated trade-offs between job security/work conditions and wage developments, thereby better taking into account the needs of specific production sectors. Therefore, important steps have been taken to address the country-specific recommendation issued in 2011 on wage bargaining but they still need proper implementation, which largely depends on the extent to which the social partners will effectively apply them. Thus, it will be important to closely monitor the implementation process. As argued in the in-depth review under the macroeconomic imbalances procedure, there is also scope to further improve the wage setting framework with a view to quickly regaining external competitiveness.

Longer working lives are among the 2012 Annual Growth Survey priorities regarding the labour market. The latest pension reform adopted in December 2011 aims to accelerate the steps to make the pension system sustainable, while increasing its fairness and labour market participation. In particular, the retirement age is raised, especially for women.[9] The reform is relevant and ambitious as it addresses the main weaknesses of Italy's pension system. The main remaining challenge is now to put in place an effective active ageing strategy to provide suitable job opportunities for older workers, in particular women, and to strengthen occupational pension schemes, so as to enable people to build up entitlements to adequate pensions.

Public Employment Services are not always up to the challenge of high unemployment in certain regions, especially in the South, and are poorly integrated with active labour market policies. The recently adopted labour market reform contains enabling acts to put in place efficient mechanisms in these fields, mainly intended to achieve a better match between labour supply and demand and to facilitate the integration of young people and

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[9] The statutory retirement age of women in the private sector increased from 61 to 62 for employees and 63½ for the self-employed in 2012. Further increases in the retirement age are envisaged over the following years until full equalisation between men and women in the public sector as of 2018, eight years earlier than planned in the summer package. Meanwhile, the statutory retirement age for men and for women working in the public sector is immediately increased from 65 to 66.

the reintegration of unemployed workers in the labour market. The full specification of the planned measures and their subsequent implementation is crucial.

Finally, the economic crisis is having serious consequences for youth unemployment. Following the European Council of 30 January 2012, the Italian authorities and Commission examined measures for reducing youth unemployment. They include a reprogramming and better use of European structural funds towards supporting education, apprenticeship, mobility, as well as extending the tax credit to favour the employment of young people. Besides, as also announced under the Euro Plus Pact commitments, a reform of the apprenticeship system aimed at facilitating the entry of young people (aged up to 29 years) into the labour market entered into force in October 2011, with large support from the social partners. Fiscal incentives for the use of apprenticeship contracts were also introduced in November 2011 (with co-financing by the European Social Fund). Following up on these initiatives, the draft labour market reform has the ambition of making the apprenticeship contract a major port of entry towards stable jobs. On 19 April, the government concluded an agreement with the regional authorities to set up a system for the certification of skills and vocational and training standards. The implementation of this new framework, with a view of having the competences recognised across the country and not only at regional level, is crucial.

Italy still underperforms the EU average in terms of early school leaving, especially as regards young immigrants. The national targets to reduce early school leaving rates – to 15-16 % in 2020 – are realistic but not sufficiently ambitious to have an impact on youth unemployment and the share of youth Not in Education, Employment or Training.

The recently adopted measures aim to curb early school leaving in general, reduce disparities between the North and the South and improve the quality of education, e.g. through more flexible education paths, easier transitions, improved guidance and focus on basic skills and key competences. Italy also drew up a new National Pupils Registry to monitor compliance with compulsory education and keep track of early school leaving, absenteeism and irregular attendance, with a view to adopting ad hoc preventive measures. These measures are relevant, but there is no evidence of a comprehensive strategy to combat early school leaving involving prevention, intervention and compensation measures. Lasting results will depend on efficient implementation.

Improving the quality and performance of tertiary education is another priority, also to reach the national target of a 26-27 % tertiary attainment rate, from 19.8 % in 2010, which is well below the EU average. The university system was reformed in 2010 under three headings: governance, recruitment and funding. In particular, financial/administrative management is now clearly separated from the management of teaching and research work. Furthermore, recruitment and career mechanisms are to be made more transparent and merit-based. Lastly, an increasing share of public funding to universities is to be allocated on the basis of teaching and research performance. However, the share of public funding allocated according to these principles only rose from 7 % in 2009 to 13 % in 2012. Reducing the drop-out rate[10] and adapting the supply of skills to labour market needs remain significant challenges, given the high unemployment rate among tertiary graduates.

Finally, the vocational education and training system is rather fragmented, and participation of adults in lifelong learning remains low in comparison with the EU

[10] According to the most recent available data published in *OECD Education at a Glance 2008*, the drop-out rate in Italy was 55 % in 2005.

average. This is especially the case for the low-skilled (1.1 %), who would benefit the most from further education.

Italy committed to reducing the number of people at risk of poverty or social exclusion by 2 200 000 by 2020. According to Italy's 2012 national reform programme, the Italian government plans to concentrate poverty-reducing action on materially deprived persons and low work-intensity households. The experimentation with the 'new social card' remains the main measure. Other measures concern non-EU nationals and the fight against undeclared work. According to Italy's national reform programme, the Italian government is going to revise its poverty-reducing objectives and the applicable measures. Expenditure on social policy, in particular sub-central government expenditure, is likely to be affected by the cuts in public spending made by the various consolidation packages adopted in 2010-2011, with potentially negative effects on the provision of welfare services to people in need and families as from 2012. Moreover, low labour market integration is one of the main obstacles preventing poverty reduction in Italy. Consequently, the creation of a more inclusive labour market is a key objective to achieve in the next years. In particular, the policy set out by Italy prioritises employment of young people and women.

3.4. Growth and competitiveness structural measures

Structural measures are key to increasing the growth potential of the Italian economy. This section covers the following policy areas: (i) liberalisation and competition; (ii) research and innovation; (iii) internal market legislation; (iv) energy, transport, infrastructure and environment.

Liberalisation and competition

The 2011 recommendation on competition and business environment recommended opening up the services sector to further competition, including for professional services, and adopting the Annual Law on Competition. To address this recommendation, Italy has adopted some important measures in the services sector, especially under the January 2012 package of liberalisation measures, which essentially replaced the initially planned Annual Law on Competition. The national reform programme estimates the growth potential related to these measures (including in the areas of local public services, professions, transports and energy) at 1.2% of GDP by 2020. However, some key regulations still need to be adopted to fully implement the recommendation, especially regarding the professional services, and there is scope to go further towards opening some services to competition.

The most relevant measures taken since the summer 2011 concern local public services and professional services. It is now stipulated that as a general rule, the provision of local public services must be awarded by public procurement, except when local governments judge that a single provider is more adequate or for services worth up to EUR 200 000 annually. Also regional railway services, save a temporary regime for existing concessions, will now be subject to public tendering procedures, while previously the obligation to tender them was explicitly excluded and direct award was the norm. The Competition Authority was given stronger supervision powers over local public services and can issue binding preventive opinions over any exclusive right assigned by the local authorities to specific economic agents. Incentives are also provided to merge the most competitive companies in optimal geographical configurations so as to achieve economies of scale.

Competition in professional services has been fostered to some degree by deregulating prices, reducing entry barriers and revising the parameters that set the number of

providers, such as pharmacists and notaries. In particular, all references to minimum, maximum and recommended tariffs in all regulated professions have been abolished, while a Presidential decree should reform the orders by August 2012. Adoption and implementation of this reform will lead to a review of access and regulation of the professions, notably in terms of disciplinary policy and with a view to protecting consumers. Professionals have been allowed to constitute limited liability companies and the access of young people to the professions has been facilitated by reducing the length of compulsory practical training and allowing them to complete part of it during university education. A significant increase in the number of notaries is expected between 2012 and 2014. However, no steps have been taken until now to reduce the number of reserved activities for professions, which limit the supply of some services, although a focused intervention on this is foreseen in the national reform programme.

The January 2012 package also devotes particular attention to consumers, who should reap the benefits of liberalisation and competition-enhancing measures envisaged for a range of services including fuel distribution, banks, insurances, retail shops and pharmacies. Overall, despite the positive progress, there is still scope to open up these market segments to competition.

By contrast, despite the implementation of the EU Directive 97/67/EC to harmonise the postal regulatory framework with the relevant European principles, the Italian postal market is still dominated by the national operator. According to the Antitrust Authority, further measures are needed to fully liberalise the postal market.

Research and innovation

The 2011 recommendation on research and innovation policies has been implemented to a limited extent. Although some measures have been adopted in line with the content of the country-specific recommendation, progress is still insufficient. According to the 2011-2013 National Research Programme, procedures will be simplified and the approach will be more market-oriented. The new ‘network contract’ promises to be a positive move to support innovative clusters and stimulate cooperation. Public support measures and framework conditions for research and development are in place (e.g. grants for industrial research, simplification of the Intellectual Property Rights system), the National Agency for the Evaluation of Universities and Research Institutes (ANVUR) has become operational, and a new governmental structure has been created to coordinate national research and development work and links with stakeholders. On innovation policy, Italy is overall a moderate innovator with a below-average performance.[11] Some measures have been taken, notably refinancing of the tax credit for research (in May 2011) for companies financing research projects in universities or public research bodies. This kind of ‘automatic’ instrument is a useful complement to selective instruments based on calls for proposals.

Italy set a national target to increase the share of GDP invested in research and development to 1.53% in 2020. Yet, the level of ambition of the measures adopted so far is insufficient and deep challenges to Italy’s competitiveness still need to be addressed. The main one is the persistent weak level of private sector investment in research and development. As evidenced in the national reform programme, it only amounts to 0.56% of GDP in Italy, against 1.09% on average in the EU. Other longstanding weaknesses regard (i) the insufficient coordination between research and innovation policy and other

[11] See: http://ec.europa.eu/enterprise/policies/innovation/files/ius-2011_en.pdf.

policies such as education, industrial, employment and competition policies; (ii) the lack of efficient implementation of the measures, continuity of policy and revision based on a systemic evaluation; (iii) the fragmentation and dispersion of the national public incentive system, based on many small measures and (iv) the low level of investment in researchers and high-skilled staff.

Limited progress has been made on innovative procurement schemes, essentially in terms of innovative tools for the development of the Digital Agenda. Besides, the rationalisation of public procurement is one of the main objectives of the planned spending review. In July 2011, incentives were introduced for subscribers of specific venture capital funds supporting business start-up and growth. Although this measure could be a step in the right direction, its effectiveness is doubtful since the tax incentive only indirectly stimulates the launch of venture capital funds.

Internal market legislation

As regards the Services Directive, transposition is satisfactory at national level. However, many fields of the Directive are of shared competence between the State and the regions. Therefore, in spite of the new Antitrust Authority's powers to screen and contest any anti-competitive administrative act, there may be an ex-ante risk, supported by some evidence, that the application of the national implementing law by local authorities is hampered by conflicting regional or local rules. Thus, a number of restrictions still obstruct the effective application of the Directive, especially in the retail, tourism and food sectors. Besides, a number of authorisation, registration or licensing requirements that presumably apply also to cross-border service providers are found in the tourism and construction service sectors. The situation regarding the Point of Single Contact has improved. The Italian portal provides a good degree of information on required formalities, although it does not yet allow for the full completion of the administrative procedures required by the Services Directive. The Italian Point of Single Contact is also difficult to use for cross-border providers, both for linguistic and technical reasons.

Moreover, Italy displays some weaknesses in its institutional set-up for handling State aid procedures, as there is neither a formal coordination and control of aid notifications, nor a formal and independent advice on draft State aid measures. There is also scope for reducing the length of State aid procedures.

Energy, transport, infrastructure and environment

A set of measures adopted under the January 2012 package aim to increase competition and transparency in the gas and electricity markets. One plans to unbundle the gas incumbent operator from the gas transmission operator, to be completed by September 2013. Other measures aim to encourage competition in the gas market, better align Italian gas prices with other EU gas spot markets and better manage gas storage facilities. By contrast, in the renewable energy sector, Italy has yet to adopt several implementing acts to make the new support scheme fully operational.

In the transport sector, the January 2012 package created a new independent 'Transport Authority' which will be responsible for highways, airports, ports and railways, both at national and local levels. It will have a series of responsibilities, including (i) ensuring non-discriminatory access of all operators to the infrastructure; (ii) setting the criteria to be followed by the railway infrastructure manager when setting access charges; (iii) designing tendering schemes for concessions; (iv) ensuring non-discriminatory participation of all operators to regional railway service tenders and (v) liberalising the mechanism for setting road haulage tariffs and conditions.

The new Transport Authority is expected to improve the regulation of the railway sector, which remains problematic. The control of both the infrastructure manager and the main incumbent operator by the Italian National Railways Company as well as the persistence of potentially distortive subsidies and practices remain indeed important bottlenecks to an efficient functioning of the sector. The new Transport Authority must present a report to the government by June 2013 to evaluate the scope for ownership unbundling between the infrastructure manager and the incumbent operator in the railway sector. Italy does not use maritime transport to its full potential. Poor integration of ports with the inland transport network, the lack of competition in port services and excessive red tape undermine the efficiency of the Italian port system, with negative repercussions in terms of competitiveness.

Another relevant issue is the time needed to complete infrastructure projects in Italy, since current administrative procedures tend to be very time consuming. The two appeal levels (Regional Administrative court and State Council) often stop a project's tendering or development, ultimately resulting in higher costs, also for private investors. Therefore, several measures in the January 2012 package aim to simplify administrative procedures and attract more private capital. Companies will be allowed to issue project bonds earlier, during the construction phase of the project, and local authorities will also be able to issue specific project-related bonds to ensure an adequate level of financing for the construction work.

Progress on the climate targets under the Europe 2020 Strategy is mixed. While advances towards the reduction of greenhouse gas emissions in non-Emission Trading Scheme sectors by 13 % by 2020 is modest, the objective of an increase in the share of renewable energy sources in final energy consumption by 17 % by 2020 is well on track. As regards the reduction of energy consumption by 27.9 Mtoe by 2020, it will benefit from the new objective set in the Energy Efficiency Action Plan 2011 of 9.6 % of energy saving by 2016. In terms of total greenhouse gas emissions, Italy ranks 4th in the EU27. According to the latest projections submitted by Italy and based on existing measures, Italy will only reduce emissions by 1.5 % by 2020. In 2011, the government transposed Directive 2009/28/EC on renewable energy. The government also released its 2011 Action Plan for Energy Efficiency, whose target is to reduce energy use by 14 % by 2020. However, the 2011 Action Plan has the same target for 2016 as Italy's previous 2007 Action Plan. Although the Plan discusses action taken and opportunities for the transport sector (which accounts for over one quarter of Italy's energy consumption), it does not specify new concrete actions for the sector. A positive development is the creation of the Kyoto Revolving Fund, providing loans to support investment in renewable energy and other sectors. The government is also expected to present a National Energy Plan in 2012.

Land filled waste is not only detrimental to the environment but is also a major cost to the Italian economy. Extended Producer Responsibility schemes are missing for the main waste streams, thus limiting the appropriate and sustainable funding of separate collection, sorting and recycling. 'Pay-as-you-throw' schemes incentivising prevention and public participation to separate collection are in place, but not in the whole country.

3.5. Modernisation of public administration

Italy's business environment has deep-rooted weaknesses, mainly stemming from high administrative burdens on firms, an inefficient judiciary system and an often ineffective public administration, including public procurement practices.

Administrative simplification

The functioning of the public administration in Italy is characterised by a number of weaknesses that affect its quality and effectiveness. In particular, although it is well equipped in terms of availability and sophistication of online material, Italy ranks among the countries with the lowest levels of e-government use, both by small companies and citizens. By the end of June 2012, the government aims to set out the implementation steps for the Italian Digital Agenda, with a view to fostering e-government and spread the use of digital technology in public places and for public procurement. In this latter field, Italy plans to simplify procedures and create, as from 2013, a national database as the only source of information, e.g. for competitive tendering.

Italy also records the highest cost to start up a company – seven times the European average. In January 2012, a broad range of administrative authorisations and barriers to doing business were abolished. The government is also empowered to issue by the end of 2012 regulations aimed at replacing unnecessary authorisations by ex-post controls. Regions and Provinces must adapt their legislation accordingly by the end of 2012.

These are relevant steps in Italy, and they need to be implemented properly to improve the functioning of the business environment.

Cohesion funds

The 2011 recommendation on cohesion funds highlighted the need to speed up in an effective way the absorption of cohesion policy funds, with special emphasis on improving administrative capacity and political governance. While measures have been taken to accelerate the absorption of funds, the issues of administrative capacity and political governance have not been addressed yet. Internal reprogramming initiatives taken in 2011 allowed minimising the loss of cohesion policy resources to EUR 1.9 million at the end of the year. The major reprogramming exercise for an amount of EUR 3.7 billion launched by Italy in December 2011 with the Cohesion Action Plan can be expected to yield its first positive results in 2012. The Plan almost exclusively affects convergence regions in the South and concentrates resources on four priority areas (education, employment, digital agenda and railway infrastructure). Specific task forces have been established for the two most critical European Regional Development Fund programmes (Campania and Sicilia), to support the regional and local administrations in speeding up implementation of the programmes.

However, pending the impact of the Plan and the results of the task forces, absorption rates in the South of Italy, where almost 80 % of European Regional Development Fund funding is concentrated, continue to be among the lowest in the EU. The work of the task forces has confirmed the persistence of major deficiencies in the capacity of regional public administrations to implement cohesion policy, as well as the importance and the need for national authorities to provide more support and coordination.

Judicial system

The 2011 recommendation on competition and business environment identified the need to accelerate contract enforcement procedures. In response, a number of measures have been adopted to enhance the efficiency of civil justice, notably by reducing case-handling times and backlogs, but most of them are not underlined in the national reform programme, despite the centrality of this issue. They aim to reorganise judicial districts, promote the specialisation of courts and judges and increase the recourse to alternative means of dispute resolution. A September 2011 enabling law empowered the government to revise the geographical distribution of judicial offices within twelve months and the first enacting decree was adopted in December. The current 12 judicial courts for industrial/intellectual property rights will soon become 20 courts specialised in company

law, which should speed up the case-handling of some business-related judicial matters. Moreover, compulsory mediation has been introduced in a number of judicial fields as from March 2011 and extended to additional fields in March 2012. These measures are positive steps that, if properly implemented, should reduce the length of procedures, avoid excessive litigation and help increase the productivity and the specialisation of judges, thus improving the functioning of civil justice. However, there remains scope for action. Implementation measures for the revision of the judicial offices' territorial distribution are still needed and the efficiency of some adopted measures suffers from their narrow scope, since they only concern specific steps of the judicial procedure and could possibly be extended to other phases of the proceeding.

As indicated in the national reform programme, another important challenge for Italy is to step up the fight against corruption. Italy remains one of the few Member States that has not ratified the 1999 Strasbourg Penal Convention on Corruption which lays down measures to be adopted to incriminate and prosecute corruption practices, including some that do not currently configure penal offences in the country. The pervasiveness of corruption entails heavy costs for Italy's productive system – estimated at EUR 60 bn by the Court of Auditors — and obstructs an optimal functioning of the markets.

4. OVERVIEW TABLE

2011 commitments	Summary assessment
Country-specific recommendations (CSRs)	
CSR 1: Implement the planned fiscal consolidation in 2011 and 2012 to ensure correction of the excessive deficit in line with the Council recommendations under the EDP, thus bringing the high public debt ratio on a downward path. Building on recently approved legislation, fully exploit any better-than-expected economic or budgetary developments for faster deficit and debt reduction and stand ready to prevent slippages in budgetary implementation. Back up the targets for 2013-2014 and the planned achievement of the medium-term objective by 2014 with concrete measures by October 2011 as provided for in the new multi-annual budgetary framework. Further strengthen the framework by introducing enforceable ceilings on expenditure and improving monitoring across all government sub-sectors.	Italy has partially implemented the CSR. Three packages adopted in 2011 on fiscal consolidation: in July (underpinning the budgetary targets in the SP); in September (aiming at a balanced budget in 2013, one year earlier than planned) and in December (additional permanent net consolidation effort of around 1.3 % of GDP, already from 2012). The Italian Parliament has just approved a bill introducing a balanced budget rule in the Italian Constitution. Effective ordinary legislation will need to be designed, specifying the balance to be considered, application arrangements (e.g. cyclical conditions) and appropriate correction mechanisms, as required by the fiscal compact.
CSR 2: Reinforce measures to combat segmentation in the labour market, also by reviewing selected aspects of employment protection legislation including the dismissal rules and procedures and reviewing the currently fragmented unemployment benefit system taking into account the budgetary constraints. Step up efforts to fight undeclared work. In addition, take steps to promote greater participation of women in the labour market, by increasing the availability of care facilities throughout the country and providing financial incentives to second earners to take up work in a budgetary neutral way.	Italy has partially implemented the CSR. No key policies to fight undeclared work and limited support for female employment (e.g. fiscal incentives in the South). The labour market reform presented by the government on 4 April, following consultations with the social partners, aims to comprehensively address the rigidities and asymmetries of employment protection legislation while moving towards a more integrated unemployment benefit scheme. This should improve the balance between flexibility of entry into and exit from the labour market.
CSR 3: Take further steps, based on the 2009 agreement reforming the collective bargaining framework and in consultation with the social partners in accordance with national practices, to ensure that wage growth better reflects productivity developments as well as local and firm conditions, including clauses that could allow firm level bargaining to proceed in this direction.	Italy has partially implemented the CSR. A social partners' agreement was reached in June, allowing firm-level bargaining to derogate from labour law (including on dismissal procedures and type of contracts to be used in the firm). Implementation of the agreement on collective bargaining will crucially depend on the behaviour of the social partners.
CSR 4: Extend the process of opening up the services sector to further competition, including in the field of professional services. Adopt in 2011 the Annual Law on Competition, taking into account the recommendations presented by the Anti-trust Authority. Reduce the length of contract law enforcement procedures. Further strengthen actions to promote the access of SMEs to capital markets by removing regulatory obstacles and reducing costs.	Italy has partially implemented the CSR. Rules were adopted to liberalise local public services, lift rigidities in professional services (Stability law and January 2012 package on liberalisations), strengthen the Antitrust Authority's powers and abolish disproportionate bans, restrictions and authorisations on economic activity from 2012 (this requires further legislative measures to be taken by the end of 2012). Sectoral

	liberalisation was launched (retail shops, pharmacies, public transport except taxi services). Reforms of the judicial system were adopted in September and December 2011 (Severino package), to improve its efficiency by reducing case-handling duration and backlogs. The December package also addressed SME support.
CSR 5: Improve the framework for private sector investment in research and innovation by extending current fiscal incentives, improving conditions for venture capital and supporting innovative procurement schemes.	Italy has partially implemented the CSR. Some measures have been taken, notably the refinancing of the tax credit for research for companies. The level of ambition and effectiveness is, however, insufficient. There has been no significant improvement on promoting venture capital.
CSR 6: Take steps to accelerate in a cost-effective way growth-enhancing expenditure co-financed by cohesion policy funds in order to reduce the persistent disparities between regions, by improving administrative capacity and political governance. Respect the commitments made in the national Strategic Reference Framework in terms of the amount of resources and quality of expenditure.	Italy has partially implemented the CSR. Measures to speed up the absorption of structural funds started in March 2011 and culminated in the November Cohesion Action Plan. Major deficiencies in the capacity of the public administration continue to hamper programme implementation, notably in the convergence regions.
Euro Plus Pact (national commitments and progress)	
Public finances: amend the Constitution to reinforce budgetary discipline.	The public finance commitment has been fully implemented. The Italian Parliament has just approved a bill introducing a balanced budget rule in the Italian Constitution. Effective ordinary legislation will need to be designed, specifying the balance to be considered, application arrangements (e.g. cyclical conditions) and appropriate correction mechanisms, as required by the fiscal compact.
Labour market: • Expand apprenticeship schemes; • Reform the taxation system with a view to shifting the tax burden from labour to consumption.	The labour market commitments have been partially implemented. • The reform of apprenticeships that entered into force in October 2011 is promising, even if there are some doubts on its capacity to enhance the use of this type of contracts. With the recently adopted labour market reform, apprenticeship contracts become the main port of entry towards stable jobs. • The December package shifts the tax burden away from labour and capital to consumption and property. • The enabling law on the tax reform

	adopted on 16 April does not envisage a further shift of the tax burden from labour to consumption.
Structural policy: • Speed up public works; • Reduce red tape and increase the efficiency of public administration.	The structural policy commitments have been partially implemented. • Concerning public works, several measures in the January 2012 package aim to attract more private capital and simplify administrative procedures. One of the priority areas of the Cohesion Action Plan is the improvement of the railway infrastructure. • As regards modernisation of public administration, in January 2012, a broad range of administrative authorisations and barriers to doing business were abolished. Yet, there remains scope for improvement in these fields.
Europe 2020 (national targets and progress)	
Employment rate target: 67-69 %	Employment rate: 61.7 % in 2009, 61.1 % in 2010. No progress has been made towards achieving the target.
R&D target: 1.53 % of GDP	Gross domestic expenditure on R&D: 1.26 % of GDP in 2009, 1.26 % of GDP in 2010. No progress has been made towards achieving the target.
Greenhouse gas (GHG) emissions target: -13% (compared to 2005 emissions; ETS emissions are not covered by this national target	Change in non-ETS GHG emissions: -10% (non-ETS sectors currently account for 62% of total GHG emissions).
Renewable energy target: 17 %	Share of renewable energy in gross final energy consumption: 8.9 % in 2009.
Energy efficiency — reduction in primary energy consumption in Mtoe: -27.9	n.a. The energy efficiency objectives are set according to national circumstances and national formulations. As the methodology to express the 2020 energy consumption impact of these objectives in the same format was agreed only recently, the Commission is not yet able to present this overview.
Early school leaving target: 15-16 %	Early leavers from education and training (percentage of the population aged 18-24 with at most lower secondary education and not in further education or training): 19.2 % in 2009, 18.8 % in 2010. Some progress has been made towards achieving the target.
Tertiary education target: 26-27 %	Tertiary educational attainment: 19 % in 2009, 19.8 % in 2010. Some progress has been made towards achieving the target.
Target to reduce the share of the population at risk of poverty or social exclusion, in number of persons: -2 200 000	People at risk of poverty or social exclusion in 1 000 persons: 14 835 in 2009, 14 742 in 2010. Some progress has been made towards achieving the target.

5. ANNEX

Table I. Macro-economic indicators

	1995-1999	2000-2004	2005-2008	2009	2010	2011	2012	2013
Core indicators								
GDP growth rate	1.8	1.5	0.9	-5.5	1.8	0.4	-1.4	0.4
Output gap [1]	0.2	1.1	1.5	-4.3	-2.5	-2.0	-2.9	-2.3
HICP (annual % change)	3.0	2.5	2.5	0.8	1.6	2.9	3.2	2.3
Domestic demand (annual % change) [2]	2.2	1.6	0.8	-4.4	2.1	-0.9	-2.9	-0.1
Unemployment rate (% of labour force) [3]	11.2	8.8	6.8	7.8	8.4	8.4	9.5	9.7
Gross fixed capital formation (% of GDP)	19.3	20.6	21.2	19.4	19.6	19.5	19.2	19.4
Gross national saving (% of GDP)	21.9	20.7	20.0	16.9	16.7	16.5	16.4	17.5
General government (% of GDP)								
Net lending (+) or net borrowing (-)	**-4.4**	**-2.8**	**-3.1**	**-5.4**	**-4.6**	**-3.9**	**-2.0**	**-1.1**
Gross debt	**117.2**	**105.8**	**105.1**	**116.0**	**118.6**	**120.1**	**123.5**	**121.8**
Net financial assets	**-102.6**	**-94.1**	**-89.9**	**-100.2**	**-98.8**	**n.a**	**n.a**	**n.a**
Total revenue	45.8	44.4	45.1	46.5	46.0	46.1	48.4	48.4
Total expenditure	50.2	47.2	48.2	52.0	50.6	50.0	50.4	49.5
of which: Interest	9.3	5.6	4.9	4.7	4.6	4.9	5.4	5.6
Corporations (% of GDP)								
Net lending (+) or net borrowing (-)	**-0.3**	**-1.0**	**-1.9**	**0.3**	**-1.0**	**-1.0**	**-1.4**	**-1.6**
Net financial assets, non-financial corporations	**-84.5**	**-107.6**	**-125.7**	**-131.2**	**-126.7**	**n.a**	**n.a**	**n.a**
Net financial assets, financial corporations	**1.6**	**-9.5**	**-0.9**	**21.2**	**26.0**	**n.a**	**n.a**	**n.a**
Gross capital formation	10.4	11.4	11.5	9.4	11.1	10.7	10.2	10.6
Gross operating surplus	23.9	23.9	22.4	20.8	21.0	20.9	20.1	20.4
Households and NPISH (% of GDP)								
Net lending (+) or net borrowing (-)	**7.1**	**3.7**	**3.4**	**3.1**	**1.9**	**1.7**	**1.1**	**1.2**
Net financial assets	**182.2**	**201.3**	**195.4**	**183.6**	**175.3**	**n.a**	**n.a**	**n.a**
Gross wages and salaries	28.8	28.9	30.0	31.4	31.1	31.1	31.1	30.7
Net property income	18.9	15.7	14.9	12.5	12.2	12.0	12.6	12.8
Current transfers received	20.7	20.7	21.4	24.0	23.8	24.0	24.3	24.3
Gross saving	14.2	11.1	11.0	10.3	9.0	8.5	7.7	7.8
Rest of the world (% of GDP)								
Net lending (+) or net borrowing (-)	**2.4**	**-0.1**	**-1.6**	**-2.0**	**-3.6**	**-3.1**	**-2.2**	**-1.3**
Net financial assets	**5.3**	**11.8**	**23.9**	**31.0**	**30.0**	**n.a**	**n.a**	**n.a**
Net exports of goods and services	3.5	0.9	-0.5	-0.5	-1.9	-1.5	-0.4	0.6
Net primary income from the rest of the world	-1.0	-0.6	-0.2	-0.5	-0.5	-0.7	-0.8	-0.8
Net capital transactions	0.2	0.1	0.1	0.0	0.0	0.0	0.0	0.0
Tradable sector	47.5	45.2	42.8	41.0	41.0	40.8	n.a	n.a
Non tradable sector	42.3	44.7	46.9	49.1	48.6	48.7	n.a	n.a
of which: Building and construction sector	4.7	5.0	5.6	5.7	5.4	5.4	n.a	n.a
Real effective exchange rate (index, 2000=100)	107.3	107.2	119.5	125.0	121.2	121.7	120.0	119.6
Terms of trade in goods and services (index, 2000=100)	104.2	102.3	98.3	102.0	98.1	95.2	93.8	95.2
Market performance of exports (index, 2000=100)	115.4	95.7	85.5	78.3	79.5	80.5	80.2	80.1

Notes:

[1] The output gap constitutes the gap between actual and potential gross domestic product at 2000 market prices.

[2] The indicator for domestic demand includes stocks.

[3] Unemployed persons are all persons who were not employed, had actively sought work and were ready to begin working immediately or within two weeks. The labour force is the total number of people employed and unemployed. The unemployment rate covers the age group 15-74.

Source :

Commission services' spring 2012 forecast

Table II. Comparison of macroeconomic developments and forecasts

	2011		2012		2013		2014	2015
	COM	SP	COM	SP	COM	SP	SP	SP
Real GDP (% change)	0.4	0.4	-1.4	-1.2	0.4	0.5	1.0	1.2
Private consumption (% change)	0.3	0.2	-2.3	-1.7	-0.4	0.2	0.5	0.7
Gross fixed capital formation (% change)	-1.9	-1.9	-3.8	-3.5	1.3	1.7	2.5	2.8
Exports of goods and services (% change)	5.6	5.6	1.1	1.2	4.0	2.6	4.2	4.6
Imports of goods and services (% change)	0.4	0.4	-4.1	-2.3	2.3	2.2	3.6	3.9
Contributions to real GDP growth:								
- Final domestic demand	-0.4	-0.4	-2.3	-1.8	-0.1	0.2	0.7	1.0
- Change in inventories	-0.5	-0.5	-0.7	-0.3	0.0	0.1	0.0	0.0
- Net exports	1.4	1.4	1.5	1.0	0.5	0.1	0.2	0.3
Output gap[1]	-2.0	-2.1	-2.9	-2.8	-2.3	-2.2	-1.5	-0.8
Employment (% change)	0.3	0.3	-0.8	-0.4	0.0	0.3	0.6	0.7
Unemployment rate (%)	8.4	8.4	9.5	9.3	9.7	9.2	8.9	8.6
Labour productivity (% change)	0.3	0.1	-0.4	-0.8	0.5	0.2	0.3	0.5
HICP inflation (%)	2.9	2.9	3.2	3.0	2.3	2.2	2.0	1.8
GDP deflator (% change)	1.3	1.3	2.1	1.8	2.2	1.9	1.9	1.9
Comp. of employees (per head, % change)	1.4	1.4	1.5	1.1	1.4	1.1	1.4	1.3
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	-3.1	-3.1	-2.2	-2.3	-1.3	-2.0	-1.7	-1.3

Note:

[1]In percent of potential GDP, with potential GDP growth according to the programme as recalculated by the Commission services.

Source:

Commission services' spring 2012 forecasts (COM); Stability programme (SP).

Table III. Composition of the budgetary adjustment

(% of GDP)	2011	2012		2013		2014	2015	Change: 2011-2015
	COM	COM	SP	COM	SP	SP	SP	SP
Revenue	**46.1**	**48.4**	**48.7**	**48.4**	**49.1**	**49.0**	**48.7**	**2.6**
of which:								
- Taxes on production and imports	14.1	15.5	15.6	15.8	16.3	16.2	16.1	2.0
- Current taxes on income, wealth, etc.	14.3	15.5	15.5	15.3	15.3	15.3	15.1	0.8
- Social contributions	13.7	13.7	13.8	13.6	13.7	13.7	13.7	0.0
- Other (residual)	4.0	3.7	3.8	3.7	3.8	3.8	3.8	-0.2
Expenditure	**50.0**	**50.4**	**50.4**	**49.5**	**49.6**	**49.1**	**48.7**	**-1.3**
of which:								
- Primary expenditure	45.1	45.0	45.1	43.9	44.2	43.5	42.9	-2.2
of which:								
Compensation of employees	10.8	10.6	10.6	10.3	10.3	10.0	9.8	-1.0
Intermediate consumption	5.8	5.7	5.7	5.4	5.3	5.3	5.2	-0.6
Social payments	22.1	22.4	22.5	22.3	22.4	22.3	22.2	0.1
Subsidies	1.1	1.0	1.0	1.0	0.9	0.9	0.8	-0.3
Gross fixed capital formation	2.0	1.8	1.9	1.5	1.8	1.8	1.7	-0.3
Other (residual)	3.3	3.5	3.4	3.4	3.4	3.2	3.2	-0.1
- Interest expenditure	4.9	5.4	5.3	5.6	5.4	5.6	5.8	0.9
General government balance (GGB)	**-3.9**	**-2.0**	**-1.7**	**-1.1**	**-0.5**	**-0.1**	**0.0**	**3.9**
Primary balance	**1.0**	**3.4**	**3.6**	**4.5**	**4.9**	**5.5**	**5.7**	**4.7**
One-off and other temporary measures	0.7	0.2	0.2	0.1	0.1	0.2	0.1	-0.6
GGB excl. one-offs	**-4.6**	**-2.2**	**-1.9**	**-1.2**	**-0.6**	**-0.3**	**-0.1**	**4.5**
Output gap[2]	-2.0	-2.9	-2.8	-2.3	-2.2	-1.5	-0.8	1.2
Cyclically-adjusted balance[2]	-2.9	-0.6	-0.3	0.1	0.6	0.7	0.4	3.3
Structural balance[3]	**-3.6**	**-0.7**	**-0.5**	**-0.1**	**0.5**	**0.5**	**0.3**	**3.9**
Change in structural balance		*2.9*	*3.1*	*0.7*	*1.0*	*-0.1*	*-0.2*	
Structural primary balance[3]	1.3	4.7	4.8	5.5	5.9	6.1	6.1	4.8
Change in structural primary balance		*3.4*	*3.5*	*0.8*	*1.1*	*0.1*	*0.0*	
Expenditure benchmark								
Public expenditure growth[4] (real)		-7.41	-6.66	-2.30	-3.46	-1.19	0.13	-
Reference rate[5,6]		0.33	0.33	0.33	0.33	*0.33*	*0.33*	-
Lower reference rate[5,7]		-0.81	-0.81	-0.81	-0.81	*-0.81*	*-0.81*	-
Deviation in % of GDP from applicable reference rate		-3.01	-2.67	-0.67	-1.19	*-0.66*	*-0.09*	-
Two-year average deviation in % of GDP from applicable reference rate		n.a.	n.a.	-1.84	-1.93	*-0.93*	*-0.37*	-

Notes:

[1]On a no-policy-change basis.

[2]Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by the Commission on the basis of the information in the programme.

[3]Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.

[4]Modified expenditure aggregate used for the expenditure benchmark, growth rates net of non-discretionary changes in unemployment benefit and of discretionary measures.

[5]The reference rates applicable to 2014 onwards will be available from mid-2012. For illustrative purposes, the current reference rates have also been applied to the years 2014 onwards.

[6]The (standard) reference rate applies starting in the year following the one in which the country reaches its MTO.

[7]The lower reference rate applies as long as the country is adjusting towards its MTO, including the year in which it reaches the MTO.

Source:

Commission services' spring 2012 forecasts (COM); Stability programme (SP). Commission services' calculations.

Table IV. Debt dynamics

(% of GDP)	Average 2006-10	2011	2012		2013		2014	2015
			COM	SP	COM	SP	SP	SP
Gross debt ratio[1]	**109.9**	**120.1**	**123.5**	**123.4**	**121.8**	**121.5**	**118.2**	**114.4**
Change in the ratio	2.6	1.5	3.4	3.3	-1.7	-1.9	-3.3	-3.8
Contributions [2] *:*								
1. Primary balance	**-1.2**	**-1.0**	**-3.4**	**-3.6**	**-4.5**	**-4.9**	**-5.5**	**-5.7**
2. 'Snow-ball' effect	**3.2**	**2.9**	**4.6**	**4.6**	**2.4**	**2.5**	**2.3**	**2.1**
Of which:								
Interest expenditure	4.8	4.9	5.4	5.3	5.6	5.4	5.6	5.7
Growth effect	0.2	-0.5	1.7	1.5	-0.5	-0.6	-1.1	-1.4
Inflation effect	-1.9	-1.5	-2.5	-2.1	-2.6	-2.3	-2.2	-2.2
3. Stock-flow adjustment	**0.7**	**-0.4**	**2.2**	**2.2**	**0.4**	**0.5**	**-0.1**	**-0.2**
Of which:								
Cash/accruals diff.	0.1	0.0	-0.1	-0.3	-0.3	-0.7	-0.8	-1.0
Accum. financial assets	0.6	-0.5	2.2	0.1	0.7	0.4	0.3	0.3
Privatisation	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Val. & residual effects	0.0	0.0	0.0	2.4	0.0	0.7	0.5	0.4
% of GDP		2011	**2012**		**2013**		**2014**	**2015**
			COM/SP[3]	**SP**[4]	**COM/SP**[3]	**SP**[4]	**SP**[4]	**SP**[4]
Gap to the debt benchmark[5,6]	-	-	-	-	-	-	-	-
Structural adjustment[7]	-	-	-	-	1.0	1.0	-0.1	-0.2
To be compared to:								
Required adjustment[8]	-	-	-	-	0.0	0.0	0.0	0.0

Notes:

[1]End of period.

[2]The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, the accumulation of financial assets, and valuation and other residual effects.

[3] Assessment of the consolidation path set in the SP assuming growth follows the COM forecasts.

[4] Assessment of the consolidation path set in the SP assuming growth follows the SP projections.

[5] Not relevant during the excessive deficit procedures that were ongoing in November 2011 and in the three years following the correction of the excessive deficit.

[6]Shows the difference between the debt-to-GDP ratio and the debt benchmark. If positive, the projected gross debt-to-GDP ratio does not comply with the debt reduction benchmark.

[7]Applicable only during the transition period of three years from the correction of the excessive deficit for excessive deficit procedures that were ongoing in November 2011.

[8]Defines the remaining annual structural adjustment over the transition period which ensures that - if followed – Member State will comply with the debt reduction benchmark at the end of the transition period, assuming that COM (SP) budgetary projections are achieved.

Source :

Commission services' spring 2012 forecasts (COM); Stability programme (SP). Commission services' calculations.

Table V. Long-term sustainability

	IT		EU27	
	No policy change scenario	**Stability programme scenario**	**No policy change scenario**	**SCPs scenario**
S2	-2.8	-3.5	2.9	0.7
of which:				
Initial budgetary position (IBP)	-3.4	-4.3	0.7	-1.6
Long-term change in the primary balance (LTC)	0.5	0.8	2.3	2.4
of which:				
pensions	-0.3	-0.2	1.1	1.2
healthcare and long-term care	1.1	1.2	1.5	1.5
other	-0.3	-0.2	-0.3	-0.3
S1 (required adjustment)*	-0.9	-1.4	2.2	-0.1
Debt, % of GDP (2011)	120.1		82.8	
Age-related expenditure, % of GDP (2011)	27.8		25.8	

Notes:

Note: The 'no policy change' scenario depicts the sustainability gap under the assumption that the budgetary position evolves according to the spring 2012 forecast until 2013. The 'stability programme' scenario depicts the sustainability gap under the assumption that the budgetary plans in the programme are fully implemented.

* The required adjustment of the primary balance until 2020 to reach a public debt of 60% of GDP by 2030.

Source: Commission services, 2012 stability and convergence programmes

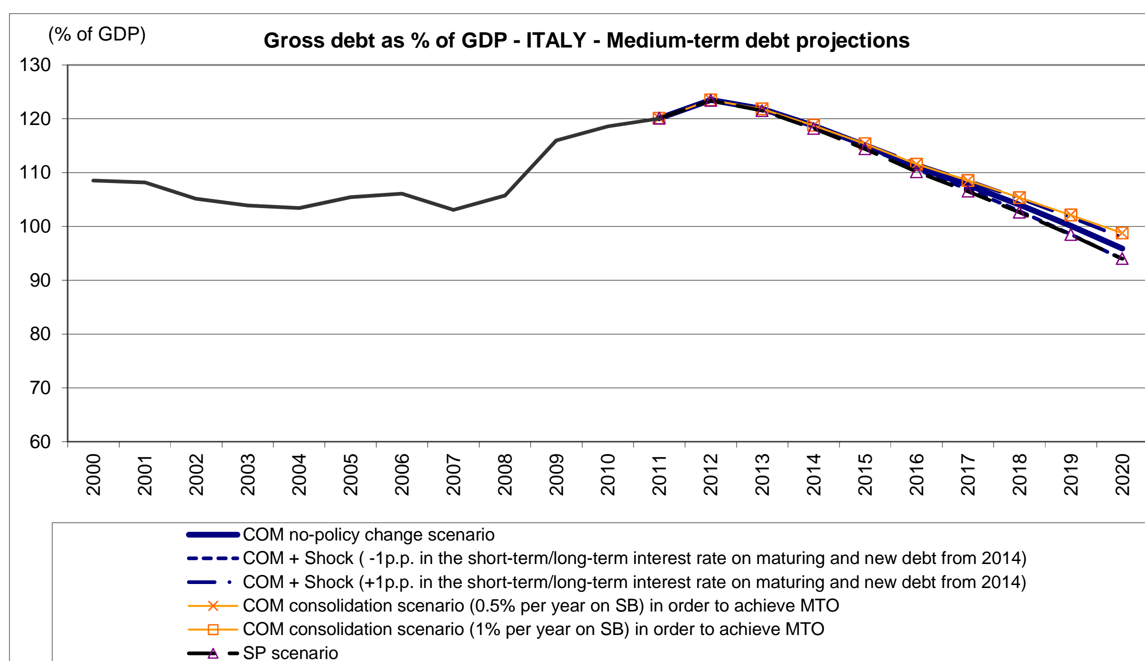

Table VI. Taxation indicators

	2001	2005	2007	2008	2009	2010
Total tax revenues (incl. actual compulsory social contributions, % of GDP)	41.1	40.1	42.7	42.7	42.8	42.3
Breakdown by economic function (% of GDP)[1]						
Consumption	10.3	9.9	10.2	9.8	9.7	10.2
of which:						
- VAT	6.2	5.9	6.2	5.9	5.7	6.2
- excise duties on tobacco and alcohol	0.7	0.7	0.7	0.8	0.8	0.8
- energy	2.4	2.2	2.0	1.9	2.1	2.0
- other (residual)	1.1	1.1	1.2	1.2	1.3	1.2
Labour employed	17.9	18.1	18.6	19.2	19.3	19.3
Labour non-employed	2.1	2.2	2.2	2.3	2.5	2.6
Capital and business income	8.3	7.3	9.1	8.9	8.3	7.7
Stocks of capital/wealth	2.5	2.6	2.7	2.5	2.8	2.5
p.m. Environmental taxes[2]	3.0	2.8	2.7	2.5	2.7	2.6
VAT efficiency[3]						
Actual VAT revenues as % of theoretical revenues at standard rate	43.4	40.6	42.7	40.6	37.3	41.3

Note:

1 Tax revenues are broken down by economic function, i.e. according to whether taxes are raised on consumption, labour or capital. See European Commission (2012), Taxation trends in the European Union, for a more detailed explanation.

2 This category comprises taxes on energy, transport and pollution and resources included in taxes on consumption and capital.

3 The VAT efficiency is measured via the VAT revenue ratio. The VAT revenue ratio is defined as the ratio between the actual VAT revenue collected and the revenue that would theoretically be raised if VAT was applied at the standard rate to all final consumption. A low ratio can indicate a reduction of the tax base due to large exemptions or the application of reduced rates to a wide range of goods and services ('policy gap') or a failure to collect all tax due to e.g. fraud ('collection gap'). See European Commission (2011), Tax reforms in EU Member States, European Economy 5/2011, for a more detailed explanation.

Source: Commission

Table VII. Selected macro-financial stability indicators

	2007	2008	2009	2010	2011
Total assets of the banking sector (% of GDP)	219.2	234.5	245.4	243.5	256.6
Share of assets of the five largest banks (% of total assets)	33.1	31.2	31.0	39.2	…
Foreign ownership of banking system (% of total assets)	18.1	13.4	12.3	…	…
Financial soundness indicators:					
- non-performing loans (% of total loans) [1), 2)]	4.6	4.9	7.0	10.0	11.0
- capital adequacy ratio (%) [1), 3)]	10.4	10.8	12.1	12.1	12.8
- return on equity (%) [1), 4)]	12.8	4.5	3.8	3.7	2.2
Bank loans to the private sector (year-on-year % change)	10.5	5.8	2.4	3.9	1.0
Lending for house purchase (year-on-year % change)	8.7	0.0	5.9	7.5	4.4
Loan to deposit ratio	141.5	136.6	131.2	120.5	125.5
CB liquidity as % of liabilities	0.9	1.7	0.9	1.6	0.0
Banks' exposure to countries receiving official financial assistance (% of GDP)[5)]	3.6	4.0	3.1	2.8	2.7
Private debt (% of GDP)	99.6	102.9	109.0	116.1	115.4
Gross external debt (% of GDP) [6)]					
- Public	42.1	47.5	50.5	51.3	45.0
- Private	23.2	24.2	24.1	25.2	23.9
Long term interest rates spread versus Bund (basis points)*	27.0	69.7	109.1	129.3	281.6
Credit default swap spreads for sovereign securities (5-year)*	…	88.4	108.2	164.4	299.4

Notes:

1) Latest available June 2011.

2) The capital adequacy ratio is defined as total capital divided by risk weighted assets.

3) The capital adequacy ratio is defined as total capital devided by risk weigthed assets.

4) Net income to equity ratio. After extraordinary items and taxes.

5) Covered countries are IE, EL, PT, RO, LV and HU.

6) Latest data 2011Q3.

* Measured in basis points.

Source :

Bank for International Settlements and Eurostat (exposure to macro-financially vulnerable countries), IMF (financial soundness indicators), Commission (long-term interest rates), World Bank (gross external debt) and ECB (all other indicators).

Table VIII. Labour market and social indicators

Labour market indicators	2006	2007	2008	2009	2010	2011
Employment rate (% of population aged 20-64)	62.5	62.8	63.0	61.7	61.1	61.2
Employment growth (% change from previous year)	1.9	1.0	0.8	-1.6	-0.7	0.4
Employment rate of women (% of female population aged 20-64)	49.6	49.9	50.6	49.7	49.5	49.9
Employment rate of men (% of male population aged 20-64)	75.5	75.8	75.4	73.8	72.8	72.6
Employment rate of older workers (% of population aged 55-64)	32.5	33.8	34.4	35.7	36.6	37.9
Part-time employment (% of total employment)	13.5	13.8	14.5	14.5	15.3	15.7
Part-time employment of women (% of women employment)	26.7	27.1	28.1	28.2	29.3	29.6
Part-time employment of men (% of men employment)	4.8	5.1	5.4	5.2	5.6	6.1
Fixed term employment (% of employees with a fixed term contract)	13.1	13.2	13.3	12.5	12.8	13.4
Unemployment rate[1] (% of labour force)	6.8	6.1	6.7	7.8	8.4	8.4
Long-term unemployment[2] (% of labour force)	3.4	2.9	3.1	3.5	4.1	4.4
Youth unemployment rate (% of youth labour force aged 15-24)	21.6	20.3	21.3	25.4	27.8	29.1
Youth NEET[3] rate (% of population aged 15-24)	16.8	16.2	16.6	17.7	19.1	:
Early leavers from education and training (% of pop. 18-24 with at most lower sec. educ. and not in further education or training)	20.6	19.7	19.7	19.2	18.8	:
Tertiary educational attainment (% of population 30-34 having successfully completed tertiary education)	17.3	18.9	19.9	20.2	20.7	:
Labour productivity per full-time-equivalent (annual % change)	0.6	0.7	-0.8	-2.7	2.5	0.2
Hours worked per person employed (annual % change)	-0.2	0.1	-0.7	-1.7	0.2	-0.1
Labour productivity per hour worked (annual % change; constant prices)	0.4	0.3	-0.7	-2.2	2.3	0.2
Compensation per employee (annual % change; constant prices)	1.0	-0.1	1.2	-0.4	1.7	0.1
Nominal unit labour cost growth (annual % change)	2.0	1.6	4.5	4.0	-0.5	1.0
Real unit labour cost growth (annual % change)	0.2	-0.7	2.0	1.9	-0.9	-0.3

Notes:

[1] According to ILO definition, age group 15-74

[2] Share of persons in the labour force who have been unemployed for at least 12 months.

[3] NEET are persons that are neither in employment nor in any education or training.

Sources:

Commission (EU Labour Force Survey and European National Accounts)

Table VIII (cont.). Labour market and social indicators

Expenditure on social protection benefits (% of GDP)	2005	2006	2007	2008	2009
Sickness/Health care	6.78	6.88	6.64	6.98	7.31
Invalidity	1.52	1.51	1.53	1.57	1.74
Old age and survivors	12.86	13.00	13.14	13.63	14.44
Family/Children	1.11	1.15	1.22	1.26	1.40
Unemployment	0.51	0.51	0.45	0.51	0.80
Housing and Social exclusion n.e.c.	0.02	0.02	0.02	0.02	0.02
Total	26.4	26.6	26.7	27.8	29.8
of which: Means tested benefits	1.17	1.59	1.67	1.74	1.95
Social inclusion indicators	**2006**	**2007**	**2008**	**2009**	**2010**
Risk-of-poverty or exclusion[1] (% of total population)	25.9	26.1	25.3	24.7	24.5
Risk-of-poverty or exclusion of children (% of people aged 0-17)	28.4	29.4	29.1	28.8	28.9
Risk-of-poverty or exclusion of elderly (% of people aged 65+)	24.6	25.3	24.4	22.8	20.3
At-risk-of-poverty rate[2] (% of total population)	19.6	19.9	18.7	18.4	18.2
Value of relative poverty threshold (single household per year) - in PPS	8323	8644	9157	9119	9119
Severe material deprivation[3] (% of total population)	6.3	6.8	7.5	7.0	6.9
Share of people living in low work intensity households[4] (% of people aged 0-59 not student)	10.8	10.0	9.8	8.8	10.2
In-work at-risk-of poverty rate (% of persons employed)	9.6	9.8	8.9	10.3	9.4

Notes:

[1] People at risk of poverty or social exclusion (AROPE): individuals who are at risk of poverty (AROP) and/or suffering from severe material deprivation (SMD) and/or living in households with zero or very low work intensity (LWI).

[2] At-risk-of poverty rate: share of people with an equivalised disposable income below 60% of the national equivalised median income.

[3] Share of people who experience at least 4 out of 9 deprivations: people cannot afford to i) pay their rent or utility bills, ii) keep their home adequately warm, iii) face unexpected expenses, iv) eat meat, fish, or a protein equivalent every second day, v) enjoy a week of holiday away from home once a year, vi) have a car, vii) have a washing machine, viii) have a colour TV, or ix) have a telephone.

[4] People living in households with very low work intensity: share of people aged 0-59 living in households where the adults work less than 20% of their total work-time potential during the previous 12 months.

Sources:

For expenditure on social protection benefits ESSPROS; for social inclusion EU-SILC.

Table IX. Product markets performance and policy indicators

Performance indicators	2002-2006	2007	2008	2009	2010	2011
Labour productivity[1] total economy (annual growth in %)	-0.3	0.2	-1.6	-3.6	2.1	1.8
Labour productivity[1] in manufacturing (annual growth in %)	-0.1	1.4	-4.0	-12.1	8.7	n.a.
Labour productivity[1] in electricity, gas, water (annual growth in %)	3.1	1.6	8.8	-9.5	n.a.	n.a.
Labour productivity[1] in the construction sector (annual growth in %)	-0.7	-2.6	-3.2	-6.6	-2.1	n.a.
Patent intensity in manufacturing[2] (patents of the EPO divided by gross value added of the sector)	1.9	1.8	1.6	n.a.	n.a.	n.a.
Policy indicators	**2002-2006**	**2007**	**2008**	**2009**	**2010**	**2011**
Enforcing contracts[3] (days)	n.a.	1210	1210	1210	1210	1210
Time to start a business[3] (days)	n.a.	13	10	10	6	6
R&D expenditure (% of GDP)	1.1	1.2	1.2	1.3	1.3	n.a.
Tertiary educational attainment (% of 30-34 years old population)	15.5	18.6	19.2	19.0	19.8	n.a.
Total public expenditure on education (% of GDP)	4.6	4.3	4.6	n.a.	n.a.	n.a.
	2005	**2006**	**2008**	**2009**	**2010**	**2011**
Product market regulation[4], Overall (Index; 0=not regulated; 6=most regulated)	n.a.	n.a.	1.4	n.a.	n.a.	n.a.
Product market regulation[4], Retail (Index; 0=not regulated; 6=most regulated)	n.a.	n.a.	2.6	n.a.	n.a.	n.a.
Product market regulation[4], Network Industries[5] (Index; 0=not regulated; 6=most regulated)	2.0	2.0	2.0*	n.a.	n.a.	n.a.

Notes:

[1]Labour productivity is defined as gross value added (in constant prices) divided by the number of persons employed.

[2] Patent data refer to applications to the European Patent Office (EPO). They are counted according to the year in which they were filed at the EPO. They are broken down according to the inventor's place of residence, using fractional counting if multiple inventors or IPC classes are provided to avoid double counting.

[3] The methodologies, including the assumptions, for this indicator are presented in detail on the website http://www.doingbusiness.org/methodology.

[4] The methodologies for the product market regulation indicators are presented in detail on the website http://www.oecd.org/document/1/0,3746,en_2649_34323_2367297_1_1_1_1,00.html. The latest available product market regulation indicators refer to 2003 and 2008, except for Network Industries.

[5] Aggregate ETCR.

*figure for 2007.

Source :

Commission, World Bank - *Doing Business* (for enforcing contracts and time to start a business) and OECD (for the product market regulation indicators).

Table X. Green growth performance

Italy		2001-2005	2006	2007	2008	2009	2010
Green Growth performance							
Macroeconomic							
Energy intensity	kgoe / €	0.15	0.15	0.14	0.14	0.14	0.14
Carbon intensity	kg / €	0.46	0.44	0.42	0.42	0.40	n.a.
Resource intensity (reciprocal of resource productivity)	kg / €	0.67	0.65	0.61	0.60	0.57	n.a.
Waste intensity	kg / €	n.a.	0.12	0.13	0.14	n.a.	n.a.
Energy balance of trade	% GDP	-1.5%	-2.1%	-1.9%	-2.3%	-2.7%	-3.4%
Energy weight in HICP	%	6	7	9	8	8	8
Difference between change energy price and inflation	%	0.2	7.4	-0.6	7.4	-5.8	-3.3
Environmental taxes over labour taxes	ratio	14.0%	13.2%	12.3%	11.2%	11.9%	n.a.
Environmental taxes over total taxes	ratio	6.9%	6.4%	6.0%	5.7%	6.1%	n.a.
Sectoral							
Industry energy intensity	kgoe / €	0.15	0.14	0.13	0.12	0.11	n.a.
Share of energy-intensive industries in the economy	% GDP	9.6	9.6	9.8	9.6	8.4	n.a.
Electricity prices for medium-sized industrial users	€/ kWh	0.08	0.09	0.10	n.a.	n.a.	n.a.
Public R&D for energy	% GDP	n.a.	0.02%	0.02%	0.04%	0.03%	n.a.
Public R&D for the environment	% GDP	n.a.	0.02%	0.02%	0.03%	0.02%	n.a.
Recycling rate of municipal waste	ratio	48.4%	58.9%	61.9%	60.6%	60.4%	n.a.
Share of GHG emissions covered by ETS	%	n.a.	40.3%	40.8%	40.7%	37.6%	n.a.
Transport energy intensity	kgoe / €	0.48	0.46	0.44	0.43	0.42	n.a.
Transport carbon intensity	kg / €	1.38	1.31	1.25	1.20	1.20	n.a.
Change in the ratio of passenger transport and GDP	%	-1.5%	4.7%	1.1%	-4.4%	n.a.	n.a.
Security of energy supply							
Energy import dependency	%	84.4%	86.8%	85.2%	85.2%	82.9%	n.a.
Diversification of oil import sources	HHI	n.a.	0.14	0.16	0.15	0.15	n.a.
Diversification of energy mix	HHI	0.37	0.35	0.35	0.34	0.34	n.a.
Share of renewable energy in energy mix	%	6.0%	6.7%	6.6%	7.5%	9.5%	n.a.

Country-specific notes:

The year 2011 is not included in the table due to lack of data.

General explanation of the table items:

Source: Eurostat unless indicated otherwise; ECFIN explanations given below

All macro intensity indicators are expressed as a ratio of a physical quantity to GDP (in 2000 prices)

Energy intensity: gross inland energy consumption (in kgoe) divided by GDP (in EUR)

Carbon intensity: Greenhouse gas emissions (in kg CO2 equivalents) divided by GDP (in EUR)

Resource intensity: Domestic Material Consumption (in kg) divided by GDP (in EUR)

Waste intensity: waste (in kg) divided by GDP (in EUR)

Energy balance of trade: the balance of energy exports and imports, expressed as % of GDP

Energy weight in HICP: the share of the "energy" items in the consumption basket used in the construction of the HICP

Difference between energy price change and inflation: energy component of HICP, and total HICP inflation (annual %-change)

Environmental taxes over labour or total taxes: from DG TAXUD's database "Taxation trends in the European Union"

Industry energy intensity: final energy consumption of industry (in kgoe) divided by gross value added of industry (in EUR)

Share of energy-intensive industries in the economy: share of gross value added of the energy-intensive industries in GDP

Recycling rate of municipal waste: ratio of municipal waste recycled over total municipal waste

Public R&D for energy or for the environment: government spending on R&D (GBAORD) for these categories as % of GDP

Share of GHG emissions covered by ETS: based on greenhouse gas emissions as reported by Member States to EEA (excl LULUCF)

Transport energy intensity: final energy consumption of transport (in kgoe) divided by gross value added of industry (in EUR)

Transport carbon intensity: greenhouse gas emissions in transport divided by gross value added of the transport sector

Passenger transport growth : measured in %-change in passenger kilometres

Energy import dependency: net energy imports divided by gross inland energy consumption incl. of international bunkers

Diversification of oil import sources: Herfindahl index (HHI), calculated as the sum of the squared market shares of countries of origin

Diversification of the energy mix: Herfindahl Index over natural gas, total petrol products, nuclear heat, renewable energies and solid fuels

Share of renewable energy in energy mix: percentage-share in gross inland energy consumption, expressed in tonne oil equivalents