Ministero dell'Economia e delle Finanze

ITALY DELIVERS

- **On September 14, the Italian Parliament approved a supplementary budget that will allow Italy to reach a balanced budget already in 2013.**
- According to its **Stability Programme**, approved by the Government on the 13th of April 2011 and approved by Parliament at the beginning of May 2011, the Italian Government committed to reach **the Medium Term Objective of close-to-balanced budget in 2014**. This would have implied an additional fiscal adjustment corresponding to a **cumulated 2.3pp of GDP** in **2013-2014 or a steady 0.8pp adjustment per year in cyclically-adjusted terms**. Italy's GDP was projected to rise 1.1% in 2011, 1.3% in 2012, 1.5% in 2013 and 1.6% in 2014. These budget plans were approved by the EU Council on the 12th of July 2011 and commented positively by all major international organisations.
- Consequently, in July **the Italian Government introduced the planned fiscal adjustment** by Decree Law no. 98/2011 then converted into Law no. 111/2011. Budget measures amounted to a cumulative **€48 billion,** allowing the achievement of a close-to-balance budget by 2014, as agreed at European level.
- Then, in mid-August, with the resurfacing of tensions in financial markets and the widening of Italy's government bond yield spreads, the Government introduced a supplementary fiscal package by Decree Law no. 138/2011. The additional package **increased the cumulative fiscal adjustment to €55.4 billion**, frontloaded the adjustment to 2012 and 2013 and **balanced the budget already in 2013, one year in advance than previously expected.**
- **Last week, the Upper House further** strengthened the package**. The overall fiscal adjustment** now amounts to a cumulative **€59.8 billion, the equivalent of around 3.4% of GDP**. Taking into account forthcoming revisions of macroeconomic projections, this is consistent with the balance budget target for 2013.
- **On the expenditure side**, measures include **cuts in central government expenditure**, implementation of the public spending review, **reform of the tax system and welfare** by way of an Enabling Act. Consolidation targets of the Enabling Act are ensured by law through a safeguard clause which provides for automatic cuts in tax expenditures if forthcoming measures do not provide the expected savings (leading to €4.0 billion cumulative savings in 2012, €16.0 billion in 2013 and €20.0 in 2014). Measures include a **wage freeze in the public sector until 2014**. Moreover, reductions in social security spending are achieved by means of a payment delay in severance pay for seniority pensions.
- **Sustainability of Italy's pension system is improved by strengthening eligibility requirements**. As from 2014, the **statutory retirement age of women working in the private sector** will be gradually increased from 60 to 65 so as to align it with that of men by 2026. Furthermore, the introduction of an automatic mechanism for early and old age pensions as well as for old age allowances **linking the statutory retirement age to expected developments in life expectancy**, previously foreseen to start in 2015, is **brought forward to 2013**. Compared to previous legislation, this measure will structurally increase the age requirements by 4 months as of 2016. In addition, for pensioners retiring earlier with 40 years of contributions, regardless of the age

eligibility criterion, new measures foresee a **further postponement of the so-called 'exit window mechanism',** by increasing the contribution period by 1 month in 2012, 2 months in 2013 and 3 months in 2014. In addition, in 2012 and 2013, pension benefits five times above the minimum **will not receive any indexation to price inflation** for the part of the pension exceeding three times the minimum. Up to this threshold, the indexation to price inflation will be reduced to 70%.

- **On the revenue side, there is an increase in the ordinary VAT tax rate from 20 to 21%. Taxation on financial assets is set to 20%** (with the exception of public debt instruments which remain taxed at 12.5%). The increase in taxation on oil products, which has been introduced on a temporary basis, is now permanent. Further measures have been introduced to fight tax evasion, including limiting cash transactions to amounts below €2,500 and harsher penalties in case of payment of professional services without proper invoicing. In addition, higher revenues are expected from lottery and excise taxes. A special tax on the energy sector is introduced to lighten the burden of cuts to local governments in the first year and then contribute to the overall correction later on. A 3 percentage point tax surcharge is introduced for incomes above €300,000.
- **Significant reforms are introduced to enhance potential growth. The structure of central and local government and administration is considerably simplified and its costs reduced**. A constitutional amendment is foreseen for the elimination of one layer of government, i.e. Provinces. **Competition in local public services** is strengthened by limiting the direct ownership of public utilities by local authorities and incentivising **privatisation of publicly-owned companies**. Other measures relate to the reduction of red tape for firms and the allowance of **more flexible labour contracts, strengthening the company level bargaining**. A mandate is **given to the Government to reorganise the structure of judicial offices with the aim of cutting** expenditure as well as increasing efficiency.
- Finally, the Government has already started the **Constitutional** process of introducing a **balanced budget rule**.

Overall Fiscal Adjustment 2011-14

	2011	2012	2013	2014
Net Increase in Revenues (€ bn)	**2.6**	**16.7**	**19.4**	**18.8**
of which increase in VAT (€ bn)	*0.7*	*4.2*	*4.2*	*4.2*
taxation on financial assets (€ bn)	*0.0*	*1.4*	*1.5*	*1.9*
excise, lotteries, stamp duties etc. (€ bn)	*1.2*	*5.4*	*7.8*	*6.6*
local tax on energy sector (€ bn)	*0.0*	*1.8*	*0.9*	*0.9*
Net Decrease in Expenditure (€ bn)	**0.2**	**7.6**	**18.9**	**21.0**
of which cuts in ministries expenditure (€ bn)	*1.7*	*7.4*	*6.3*	*5.0*
transfer to local governments (€ bn)	*0.0*	*4.2*	*6.4*	*6.4*
pensions (€ bn)	*0.0*	*1.0*	*3.5*	*3.4*
Cuts in tax expenditure (safeguard) (€ bn)	**0.0**	**4.0**	**16.0**	**20.0**
Impact on Primary Balance (€ bn)	**2.8**	**28.3**	**54.3**	**59.8**
% of GDP	***0.2***	***1.7***	***3.3***	***3.5***