Rome, 4th October 2018

Today the Italian Government will be sending to the Parliament an Update of the 2018 Stability and National Reform programs. The Update (*Nota di Aggiornamento del Documento di Economia e Finanza*) will be accompanied by a Report to Parliament *(Relazione al Parlamento)* in accordance with Article 6 of Law 243/2012. The latter requires the government to notify the European Commission whenever it seeks parliamentary authorisation to alter its fiscal targets in the ensuing Budget.

The reason for this letter is that the government has decided to modify its fiscal targets for 2019-2021 in order to pursue a program of socio-economic reforms and public investment at a time when growth in the European and Italian economies is decelerating and unemployment in our country remains unacceptably high – both in absolute terms and relative to the EU average.

The 2019 Budget will introduce an income-support scheme (Citizenship Income) to reduce poverty. This reform will broaden the footprint and resources of existing inclusion schemes, and in addition it will restructure and develop Job-placement centres in order to help inactive, unemployed and under-employed individuals find jobs. A flat tax for small businesses and self-employed professionals will also be introduced, along with tax breaks for firms that raise capital expenditure and employment. In addition, early-retirement rules will be temporarily relaxed with a mechanism that will promote youth employment.

Public investment, which will probably decline to a low of 1.9 percent of GDP this year, will be boosted with additional funds and an overhaul of laws and regulations, planning and execution. Following the collapse of a motorway bridge in Genoa, an extraordinary maintenance programme for existing infrastructure will also be launched. The Budget will target a public investment ratio of 2.3 percent of GDP by 2021, but we intend to use any fiscal windfalls to raise that target towards 3 percent of GDP.

According to the latest estimates, the general government deficit will decline to 1.8 percent of GDP this year, from 2.4 percent in 2017 (2.0 percent net of banking sector support). We are now seeking Parliament's authorisation for an increase in the deficit to 2.4 percent of GDP in 2019. However, the new plan envisages a subsequent decline in the deficit to 2.1 percent in 2020 and 1.8 in 2021.

In structural terms, the deficit will widen by 0.8 percentage points in 2019 and then stabilise in 2020 and 2021. We believe that this fiscal policy strategy is more credible, and more likely to succeed, than the approach followed in 2016, when Italy was granted a temporary deviation from the preventive arm of the Stability and Growth Pact, but was then required to sharply tighten fiscal policy in the following year.

I emphasise that our deficit targets are well below the 3 percent limit and our communication to the Italian parliament states that the policy of gradually improving the structural balance will be reinstated once real GDP and the unemployment rate return to pre-crisis levels.

We expect the performance of the Italian economy to improve over the coming years thanks to a growth-friendly fiscal policy and socio-economic reforms. On the basis of a prudential assessment, real GDP growth is projected to accelerate from 1.2 percent this year to 1.5 percent in 2019 and 1.6 in 2020, before easing to 1.4 percent in 2021. Nominal GDP growth will exceed 3 percent annually throughout the 2019-2021 period. As a result of that and of declining deficits, the debt-to-GDP ratio will fall from an estimated 130.9 this year to 126.7 percent in 2021.

I look forward to continuing the dialogue with the Commission concerning our fiscal policy plans. Meanwhile, I would be grateful for your acknowledgement of this letter.

Yours sincerely,

Giovanni Tria

Mr. Valdis Dombrovskis
Vice President

Mr. Pierre Moscovici
Commissioner, Economic and Financial Affairs

European Commission
Brussels