Italy: Domestic demand drive confirmed by 3Q17 GDP

The downward revision of the headline reading might have been disappointing, but the breakdown shows economic growth is becoming more balanced

Source: Shutterstock

0.4%

GDP growth in third quarter

QoQ%

Worse than expected

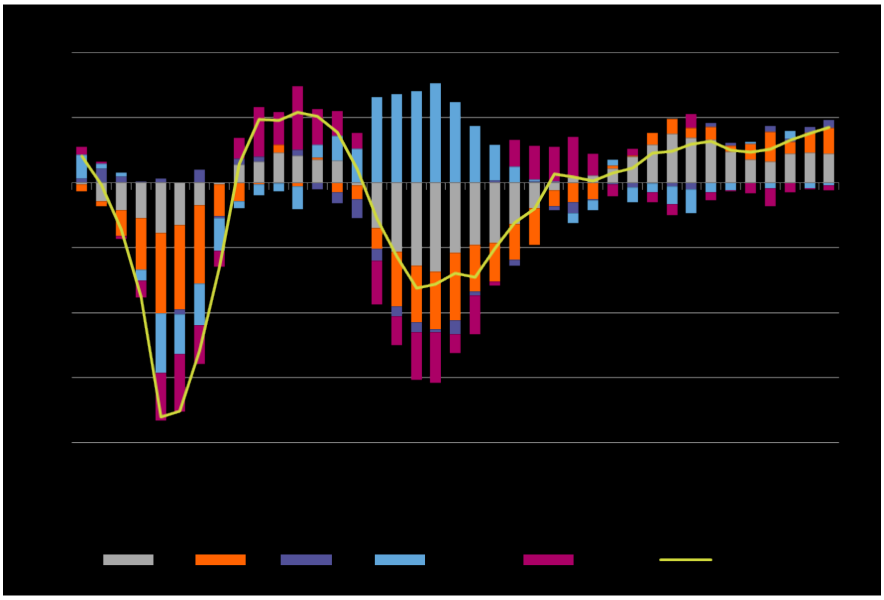
Downwards revision to 3Q17 GDP not a reason for concern

At first sight, the downward revision of the preliminary estimate of the Italian 3Q17 GDP to 0.4% QoQ (1.7% YoY) from the preliminary 0.5% (1.8% YoY) might look disappointing. However, the details of the demand breakdown show some interesting features which bode well for future growth developments. Data shows that domestic demand remains the main driver of the Italian economic recovery, with a rebalancing of components towards investment. As expected, gross fixed capital formation turned out the main contributor to quarterly growth (0.5% contrib.), followed by private consumption, which added another 0.2%.

More surprisingly, inventories contracted, subtracting 0.5% from quarterly growth, reversing the 0.4% positive contribution posted in 2Q17. Interestingly, the investment breakdown shows that equipment and other products have become the main driver (0.43% quarterly contribution) in the gross fixed capital formation domain, taking over transport equipment (0.27% contribution) and leaving construction (0.03% contribution) far away. The 6% QoQ (5.4% YoY) leap in equipment investment is likely reflecting the delayed impact of the introduction (in last year's budget) of existing generous tax incentives against a backdrop of a reduced capital stock. Chances are that, against a positive external/internal demand backdrop, the equipment investment recovery will continue in the 4Q17, if at a less spectacular pace.

Interestingly, notwithstanding strong domestic demand, net exports also provided a positive 0.14% contribution. Exports expanded a healthy 1.6% QoQ and imports 1.2% QoQ, possibly reflecting the surprising setback of inventories, which typically have a strong import component.

Domestic demand drive is getting more evenly balanced



Confidence data point to continued growth in 4Q17

Looking forward, available data evidence points to a continuation of GDP growth in 4Q17, with a clear industrial drive. The November manufacturing PMI, also released last Friday, has climbed to 58.3 (from 57.8 in October), the highest reading since 2011, pushed by the new orders component. The concurrent gain in the relevant employment component might suggest that the flat October employment Istat reading might be only a pause in the trend. To be sure, we will need more confirmations from the services sector, whose latest PMI readings have been slightly controversial. In a low inflation environment, the continuation of the employment recovery trend remains key to propel disposable income in the absence of any substantial acceleration in wages. We believe that this will materialise and that the current recovery will remain unambiguously demand-driven.

Based on available evidence, we are currently forecasting another expansion of the Italian GDP in 4Q17 at a 0.5% quarterly pace with the average yearly reading for 2017 at 1.6%.

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