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Italy: Some support from surprisingly good 2019 fiscal data

This should in principle give the government some breathing space to implement some fiscal push to contrast the negative economic impact of Covid-19, but will unlikely prevent Italy from entering technical recession in 1Q20

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When all eyes were focused on Covid-19 epidemic developments, the first estimate of the budget deficit, general government debt and GDP growth for the whole of 2019, released earlier today, provided positive surprises.

Slightly better GDP growth in 2019...

According to Istat, in 2019 real GDP growth was 0.3%, slightly higher than the 0.2% suggested by the aggregation of published preliminary quarterly data. The publication of the first complete release of quarterly accounts (including the detailed demand breakdown), due on Wednesday, will tell us better where the mismatch comes from.

…and a big surprise from the budget deficit data

However, the biggest surprise in today's Istat release came from the public finance bit of the report, and particularly from the budget deficit part. The headline deficit, at 1.6% of GDP, turned out much lower than the 2.2% that the government had been anticipating, setting a new low since 2007. This came courtesy of a surprising increase of the primary surplus to 1.7% of GDP (from 1.5% in 2018), versus expectations of a decline. In turn, this mainly built on a 3.4% increase in direct tax revenues, particularly striking when considering that this came together with softening GDP growth. While a surprisingly effective contrast of tax evasion might have been at play here, we remain puzzled by the scope of the surprise.

Fiscal push unlikely to stop Italy from entering technical recession in 1Q20

Ex post, we can now note that in 2019 Italy ran a restrictive fiscal policy. The side effect of this is that in 2020 the Italian government will likely have more fiscal space to use to contrast the negative economic impact of the Covid-19 epidemics. Over the weekend the Italian government approved a law decree putting together a first set of measures meant to tackle the Covid-10 emergency. Part of these are targeted on citizens/businesses located in the segregated area (affecting some 50K people), others have a nationwide scope. The broad aim is to soften administrative duties and, in the most affected areas (the so-called "red zone"), to allow the deferral of tax and mortgage payments and re-introduce redundancy schemes for SMEs. More will likely follow to soften the blow, possibly focusing on a fast-forward restart of public investment plans, but will unlikely come soon enough to prevent Italy from entering technical recession in 1Q20.

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