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## Italy

1. After a period of protracted slow growth, the situation of the Italian economy improved in 2006. Real GDP grew by 1.9%, the highest rate since 2000, but still below the euro area average. Prospects for 2007 appear still favourable, even though the growth momentum is losing vigour. Employment continues to rise and the unemployment rate decreased to 5.7% in June 2007. Nevertheless, the employment rate, at 58.9% in the first half of 2007, remains well below the EU average and is much lower in the South. In fact, over the last three years, the regional divide has widened.
2. Medium-term prospects for the Italian economy remain challenging under the strain of structural weaknesses feeding into low productivity growth and high public indebtedness. Reversing this requires an economic policy strategy founded on micro-economic reforms to increase the efficiency and competitiveness of domestic production and on measures aimed at raising labour market participation and employment, including by enhancing human capital. Tackling regional disparities requires particular attention. Consolidation of public finances is a necessary precondition for this strategy, as it helps to create more favourable conditions for investment and to make room for enhanced expenditure on knowledge, human capital and infrastructure.

### **PART I: GENERAL ASSESSMENT**

3. Overall, the Implementation Report shows good progress on implementing the revised National Reform Programme (NRP) over the 2005-2007 period. Italy has responded to the country-specific recommendations adopted by the Council. Some progress has been made with regard to the other areas on which the Council concluded Italy should focus (R&D performance, the sustainability of healthcare, the sustainable use of resources, infrastructure, and impact assessments).
4. Last year's Commission Annual Progress Report concluded that progress on meeting the specific commitments agreed at the 2006 Spring European Council in the priority action areas was mixed. This assessment remains valid this year. Progress is most visible in the area of unlocking the business potential. Italy specifies the efforts it is taking to meet the euro area recommendations. Although the response in the area of public finances is substantial, Italy could have done more given the favourable cyclical and budgetary developments. Some initial steps have been taken to develop an integrated flexicurity approach, and to encourage more decentralised wage bargaining.
5. Consultation and efforts to develop ownership of the NRP at the level of central and local governments and the social partners is substantial, although there is still room for improvement in co-ordinating with regions. Italy's 2007 Implementation Report confirms the main priorities within the NRP, and provides a clear overview of progress in implementing the strategy. It also correctly highlights the importance of improving the efficiency of the judicial system throughout the country, as having an across-the-board impact in terms of the competitiveness and economic context of the country. Links between governance and monitoring of the NRP and the structural

funds are strong. The earmarking of structural funding for Growth and Jobs objectives is being applied satisfactorily, with significant support to foster employability and human capital, to boost research and innovation, and fight climate change.

## **PART II: ASSESSMENT BY POLICY AREA**

### **Macro-economic policies**

6. Given the high level of public debt and the considerable pressure from an ageing population, ensuring the long-term sustainability of public finances remains a key challenge for Italy, as was highlighted in the 2005 NRP. In line with this, the Council recommended that Italy rigorously pursues fiscal consolidation in order to place the debt-to-GDP ratio on a declining path, and fully implements pension reforms with a view to improving the long-term sustainability of public finances.
7. The result of Italy's fiscal consolidation strategy over the 2006-2007 period is substantial. The general government deficit has been reduced below 3% of GDP, with the larger part of the structural correction occurring in 2006. Notwithstanding this positive result, Italy has not fully utilised the favourable cyclical and budgetary developments, missing the opportunity to further accelerate the reduction of the public debt ratio. The adjustment has been achieved through an increase in the tax burden, and thanks to measures to increase tax compliance. In the Commission's opinion, the draft 2008 Budget Law, due to be approved by Parliament by the end of 2007, implies that fiscal consolidation efforts will stall in 2008.
8. Italy is continuing its efforts to pension reform and to limit increases in age-related public expenditure in the long term. A protocol agreement with the trade unions, adopted by the government in July 2007 and confirmed by a draft law, is a further step in this direction. However, it relaxes the eligibility conditions for seniority pensions for a specific group of workers and leaves some crucial issues open (for instance the definition of the actuarial coefficients in line with increases in life expectancy). More importantly, implementation remains crucial in order to ensure long term financial sustainability.
9. The Council also referred to the need to improve the sustainability of healthcare provision, while preserving quality and accessibility. Stringent expenditure control mechanisms are to be implemented consistently as the Commission considers them a good response. However there remains a need to improve the efficiency and cost effectiveness of expenditure.
10. Italy has partially succeeded in implementing a strategy aimed at ensuring long-term fiscal sustainability, including in the area of healthcare. Given that more progress is still required, the Commission considers that the Council recommendation remains valid and stresses the importance of the euro area recommendation to make use of the favourable cyclical conditions to pursue a more ambitious budgetary consolidation. More attention should also be paid towards improving the quality of public finances by containing growth in expenditure and improving efficiency and cost-effectiveness.

### **Micro-economic policies**

11. Italy made mixed progress over the 2005-2007 period with regard to the implementation of policies to address the micro-economic challenges identified in the 2005 NRP. Notably by extending competition, granting incentives for scientific research and technological innovation, and upgrading infrastructure and protecting the environment.
12. The Council recommended Italy to pursue the implementation of recently announced reforms aimed at increasing competition in product and service markets. Italy has taken important steps in this area and the implementation of the reforms adopted in June 2006 is progressing. A second package, introduced in January 2007 which includes a mix of competition and consumer protection measures in the areas of financial services, mobile telecommunication, retail and wholesale distributions. Significant decreases in prices have been recorded, including in the telecom and pharmaceutical sectors. Since July 2007, SMEs and households now have access to an open electricity market. A number of draft laws have been presented on energy, liberalisation of local public services, reform of competition authorities, measures for consumers and to facilitate commercial and productive activities, and on class action. These are still being discussed in parliament. These are welcome steps in the right direction, but more is needed given the scale of the competition challenge and the need to modernise Italy's industrial base. It is important that draft laws are both adopted and implemented in a timely manner, including those on energy and the liberalisation of local public services. Italy has recently significantly improved its transposition deficit of EU legislation. It is important to continue these efforts while also bringing down the number of infringement cases.
13. The Council highlighted the need to focus on: R&D, a sustainable use of resources, implementing plans to improve infrastructure, and strengthening and fully implementing the system of impact assessment for proposed regulation.
14. In the area of R&D, Italy has made some progress in implementing a number of measures. These include public-private partnerships measures at local level, a tax credit scheme to support innovation, and a streamlining of the existing support schemes. New measures are being introduced in the context of the "Industria 2015" initiative to accompany structural change of industry. An independent evaluation agency for university and research is being set up to improve the governance of the research and innovation system. However, overall research spending remains low and the Implementation Report does not indicate to what extent the measures foreseen will allow progress towards meeting the 2.5% of GDP target for R&D. Further efficiency-enhancing measures are required in the public sector, where productivity is comparably low internationally.
15. The Implementation Report sets out detailed information on priorities, budget appropriations and deadlines with regard to infrastructure projects. It is now important that Italy vigorously implements the plans. Further efforts are needed to expand broadband to rural areas.
16. In the area of the business environment, Italy has made important progress to strengthen one-stop shops and reduce the time and costs for starting an enterprise. A target has been set for cutting administrative costs by 25% by 2012. A streamlined procedure for impact assessment is being introduced, but its scope is limited and its application across all new regulation is only expected in the medium term.

17. Italy's CO<sub>2</sub> emissions are significantly above 1990 levels, and policies and measures implemented have so far produced only limited effects on curbing emissions. In the wider environmental field the Implementation Report details measures to improve the sustainable use of resources, notably aimed at protecting water and soil (including remediation of contaminated sites), and improving waste management.
18. Italy has partially succeeded in implementing measures to deliver on the micro-economic commitments expressed in its NRP. The recommendation on competition and the points to watch have been addressed to some extent, but the Commission considers them to remain valid.

### **Employment policies**

19. Italy's labour market performance in terms of employment growth and reduction in unemployment continues to improve. Female participation in the labour market has increased but important gender gaps in terms of activity, employment and unemployment remain. The employment rate of older workers, and women, remain significantly lower than the EU average, affecting the adequacy of future pensions. Some progress has been registered on early school leaving and youth educational attainment levels. Regional disparities remain significant and additional efforts are required to address underlying structural weaknesses.
20. The Council recommended Italy to reduce regional disparities in employment by tackling undeclared work, increasing childcare provision and ensuring the efficient operation of the employment services throughout the country. Italy has adopted a number of measures in response. It has increased action against illegal and undeclared work, such as intensification of inspections and tighter administrative sanctions. To better reconcile work and family life, Italy has committed to improving the quality and availability of childcare services. Although employment services have been reformed, differences in the quality and efficiency of services between the south and the north persist, in particular in the way these services are tailored to individual needs. Taxes on labour have been cut for those on permanent contracts, but the impact is not yet known. The "protocol agreement on welfare" envisages some measures to promote decentralised wage bargaining, but a more comprehensive approach is needed to allow a better alignment between wage and productivity developments. The policy measures undertaken so far should help reduce regional disparities, but implementation is slow and more incisive action is needed.
21. The Council also recommended Italy to develop a comprehensive lifelong learning strategy and improve the quality and labour market relevance of education. The Implementation Report does not set out a comprehensive strategy, but progress is however being made towards the preparation of a national qualifications framework. The consolidation of reforms of the education and training system and the improvement of quality of education by filling the gap in school performance across regions remains crucial.
22. Italy has taken initial steps to address the flexicurity concept. The "Protocol agreement" on welfare reform increases the level and duration of unemployment benefits, limits the use of fixed term contracts, and strengthens employment services. These measures are yet to be implemented and in parallel Italy needs to implement measures to increase flexibility. A lifelong learning system needs to be put in place.

23. Italy has partially succeeded in implementing its NRP commitments in the employment domain. There has been some progress in addressing undeclared work, but further efforts are needed to tackle regional disparities, including the further reform of employment services, improving the quality and labour market relevance of education, and establishing a lifelong learning system. Therefore the Commission considers the recommendation dealing with these issues to remain valid. Italy should also pay particular attention to the development of an active ageing strategy.

### **PART III CONCLUSIONS**

24. In the light of the 2007 Italian Implementation Report and the Commission's assessment of progress made in implementing key structural reforms and based on the Integrated Guidelines for Growth and Jobs, the following conclusions are appropriate:
25. Italy has made good progress in implementing its National Reform Programme over the 2005-2007 period. There has been some response in fulfilling the commitments agreed by the 2006 Spring European Council in the four priority areas.
26. The Implementation Report shows some policy response to the recommendations adopted by the Council. Given the scale of the challenge, significant further reforms are needed. There has been some policy response on the additional areas identified in the Council conclusions as requiring attention. The Implementation Report also specifically addresses the recommendations issued to the euro area countries.
27. Amongst the strengths shown by the 2007 Italian Implementation Report are the initial steps to improve the business environment, measures to enhance competition in professional and financial services and retail distribution, recent improvements in its transposition deficit of EU legislation; and e-government actions to modernise the public sector.
28. The policy areas in the Italian National Reform Programme where challenges need to be tackled with the highest priority are: fiscal sustainability, where efforts need to be pursued and the pension reform process needs to be completed; enhanced competition in product and service markets and pursuing the full implementation of announced reforms; further fighting regional disparities in the employment; and improving education and lifelong learning. Against this background it is recommended that Italy:
- rigorously pursues fiscal consolidation, in particular by curbing growth in current primary expenditure, and completes the pension reform process with a view to improving the long-term sustainability of public finances;
  - continues the progress made to enhance competition in product and services markets and vigorously pursues the implementation of announced reforms;
  - improves the quality and labour market relevance of education, promotes lifelong learning, tackles undeclared work and ensures the efficient operation of employment services, within a flexicurity approach and with a view to reducing regional disparities.

29. In addition, it will be important for Italy to focus over the period of the National Reform Programme on the following challenges: increasing R&D investment and efficiency, where despite welcome policy developments, further efforts are needed to reach the 2010 target and to enhance the efficiency of public spending; increasing efforts to meet the CO2 emission reduction targets; improving the quality of regulation by strengthening and fully implementing the system of impact assessment, notably for SMEs; implementing plans to improve infrastructure; increasing childcare provision with a view to reconciling work and family life and fostering labour market participation of women; and putting in place a consistent active ageing strategy to increase employment of older workers, and with a view to improving pension adequacy.

#### **PART IV: STATISTICAL GRAPHS AND DATA**

# ITALY

	IT						EU27			
	2000	2003	2004	2005	2006	2010 National target	2000	2005	2006	2010 EU target
GDP per capita in PPS	117.4	111.2	107.6	105.4	103.7		100.0	100.0	100.0	
Labour productivity per person employed	126.7	115.4	112.6	111.4	109.5		100.0	100.0	100.0	
Employment rate										70.0
Total	53.7	56.1	57.6b	57.6	58.4		62.2	63.4p	64.4p	
Women	39.6	42.7	45.2b	45.3	46.3		53.7	56.2p	57.2p	
Men	68.0	69.6	70.1b	69.9	70.5		70.8	70.8p	71.6p	
Employment rate of older workers										
Total	27.7	30.3	30.5b	31.4	32.5		36.9	42.3p	43.5p	
Women	15.3	18.5	19.6b	20.8	21.9		27.4	33.5p	34.8p	
Men	40.9	42.8	42.2b	42.7	43.7		47.1	51.5p	52.6p	
Gross domestic expenditure on R&D	1.05	1.11	1.10	1.10		2.5	1.86e	1.84e	1.84e	3.0
Youth education attainment level										
Total	69.4	71.0	73.4	73.6	75.5		76.6	77.4	77.8	
Women	74.2	75.1	78.6	78.1	79.4		79.3	80.1	80.7	
Men	64.5	66.8	68.2	69.2	71.7		73.8	74.7	74.8	
Comparative price levels	97.5	103.6	105.2	104.4	104.4		100.0	100.0	100.0	
Business investment	18.0	17.9	18.1	18.2	18.5		18.4	17.8	18.2	
At-risk-of-poverty rate after social transfers										
Total	18.0		19.0b	19.0				16.0e		
Women	19.0		20.0b	21.0				17.0e		
Men	18.0		18.0b	17.0				15.0e		
Dispersion of regional employment rates										
Total	17.5	17.0	15.6	16.0	16.0		13.0	11.9	11.4	
Women	30.5	29.7	25.7	26.6	26.1		20.0	16.8	16.2	
Men	9.8	9.1	8.7	8.9	9.3		9.6	9.7	9.3	
Long-term unemployment rate										
Total	6.3	4.9	4.0b	3.9	3.4		4.0	4.1p	3.7p	
Women	8.4	6.6	5.5b	5.2	4.5		4.6	4.5p	4.0p	
Men	4.8	3.8	2.9b	2.9	2.6		3.5	3.8p	3.5p	
Total greenhouse gas emissions	106.6	110.8	111.7	112.1			90.7	92.1		
Energy intensity of the economy	186.9	189.2	188.8	190.7			213.1	208.1		
Volume of freight transport relative to GDP	102.2	93.7	104.3	111.6	110.2e		99.1e	105.4e	106.7e	

## PERFORMANCE COMPARED TO EU-27

