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Assessment of the 2013 national reform programme and stability programme for ITALY

Accompanying the document

Recommendation for a Council Recommendation

on Italy's 2013 national reform programme and delivering a Council Opinion on Italy's stability programme for 2012-2017

{COM(2013) 362 final}

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Economic Outlook

Italy is undergoing a protracted recession. Italy's real GDP contracted by 2.4% in 2012, on the back of negative domestic demand driven by tight financing conditions and declining disposable incomes. Economic activity is expected to decline further in 2013, before starting to recover mildly in the second half of 2013. The unemployment rate is projected to continue increasing and to reach 12.2% in 2014, affecting young people in particular.

Key Issues

Italy's capacity to withstand the impact of the crisis is hampered by long-standing structural weaknesses. The high government debt and loss of external competitiveness, driven by sluggish productivity growth, were identified in the second in-depth review presented by the Commission on 10 April as the main macroeconomic imbalances of the Italian economy, which require monitoring and determined policy action.

Over the past year Italy has adopted a range of relevant and ambitious measures with a view to safeguarding fiscal sustainability and spurring growth. Italy has undertaken action to correct the excessive government deficit, strengthen the budgetary framework, enhance tax compliance, improve the functioning of the labour market and the wage setting framework, foster competition in key sectors of the economy and improve the business environment, including the efficiency of the public administration. These measures go towards meeting the country-specific recommendations issued in 2012 and can contribute to addressing many of the economy's challenges.

However, implementation of the measures taken remains challenging and the reform agenda needs to be taken forward. Delays in the adoption of enacting legislation or incomplete application of legislation are still holding back the potential benefits of several measures. There is also scope for further action in the following areas:

- **Public finances**: according to the Commission 2013 spring forecast, Italy corrected its excessive deficit in 2012 in a durable way, conditional upon the rigorous implementation of the consolidation effort enacted in 2011-12. Despite the budgetary consolidation, the high government debt-to-GDP ratio, expected to peak at 132.2% in 2014, remains a major burden on the Italian economy. While low growth makes it more difficult to put the public finances on a sustainable path, high public debt may hamper growth prospects, dampen domestic demand and crowd out productive public spending.

- **Taxation**: the high tax burden in Italy still weighs heavily on labour and capital. While in the short to medium term reducing the overall tax burden is not an option in the current budgetary conditions, there is scope for improving the efficiency of the tax system. Fighting against tax evasion, the shadow economy and undeclared work would help to lower the high statutory tax rates on compliant taxpayers.

- **Banking sector**: while the Italian banking sector showed resilience in the aftermath of the global financial crisis, the protracted recession affected asset quality and reduced the profitability of banks, resulting in constraints to the provision of credit to the economy, in particular to SMEs.

- **Labour market and social cohesion**: youth unemployment, which reached 35.3% in 2012, and the still low participation of women in the workforce represent a missed opportunity for the Italian economy, particularly in the southern regions. If effectively implemented, the June 2012 reform has the potential to help address the rigidities and segmentation in the labour market. Meanwhile, over the last decade, Italy's lacklustre productivity performance has not been adequately reflected in wage dynamics, leading to sustained unit labour cost growth and loss of cost competitiveness. Adjustments to the wage setting framework are thus required along the lines of the recent social partners' agreements. Finally, the protracted recession has exacerbated the risk of poverty and social exclusion. Therefore, it is crucial that the reform agenda be informed by the principles of social equity and the efficiency and the effectiveness of the social protection system be improved.

- **Education**: although some steps have been taken to upgrade the educational system, the still high early school leaving rate and low tertiary attainment rate point to a performance of the educational system that lags behind that in other EU countries. There is also evidence of a difficult transition from education to the labour market, including for high-skilled young people.

- **Market opening in services and network industries**: several measures aimed at opening to competition services and network industries have been adopted over the past years. Their proper implementation is key for the reforms to deploy their benefits. The persistence of sheltered market segments in services and network industries, compounded in the latter by the presence of infrastructure bottlenecks, translates into higher costs for firms and households, notably in the energy sector.

- **Public administration**: notwithstanding the reform action undertaken in this area, weaknesses in the public administration continue to contribute to an unfavourable business environment, discourage foreign direct investment and hamper the implementation of reforms. The main shortcomings include the long duration of proceedings in civil justice and a cumbersome and often opaque administrative and regulatory framework at various government levels. Furthermore, weaknesses in administrative capacity hamper the good use of structural funds, especially in the southern regions.

1. INTRODUCTION

In May 2012, the Commission proposed a set of country-specific recommendations (CSRs) for economic and structural reform policies for Italy.[1] On the basis of these recommendations, the Council of the European Union adopted six CSRs in the form of a Council Recommendation.[2] These CSRs concerned public finances, the budgetary framework and structural funds, education, the labour market, taxation, as well as competition and the business environment. This Staff Working Document (SWD) assesses the state of implementation of these recommendations in Italy.

The SWD assesses policy measures in light of the findings of the Commission's Annual Growth Survey for 2013 (AGS)[3] and the second annual Alert Mechanism Report (AMR),[4] which were published in November 2012. The AGS sets out the Commission's proposals for building the necessary common understanding about the priorities for action at national and EU level in 2013. It identifies five priorities to guide Member States to renewed growth: pursuing differentiated, growth-friendly fiscal consolidation; restoring normal lending to the economy; promoting growth and competitiveness for today and tomorrow; tackling unemployment and the social consequences of the crisis; and modernising public administration. The AMR serves as an initial screening device to determine whether macroeconomic imbalances exist or risk emerging in Member States. The AMR found signs that macroeconomic imbalances in Europe are being corrected. To ensure that complete and durable rebalancing is achieved, Italy and 13 other Member States were selected for a review of developments in the accumulation and unwinding of imbalances.[5]

Against the background of the 2012 Council Recommendation, the AGS and the AMR, Italy presented updates of its national reform programme (NRP) and its stability programme on 23 April 2013. These programmes were submitted to the consultation of the social partners, regional and local authorities during the parliamentary process leading to their formal approval by the Italian Parliament on 7 May 2013. The programmes provide detailed information on progress made since July 2012 and indicate the reform path to follow in the future, without however designing a precise plan for action given the political uncertainty at the time of their publication. The information contained in these programmes, together with the reform agenda outlined by the new government, provides the basis for the assessment made in this SWD.

[1] COM(2012) 318 final of 30 May 2012.
[2] OJ C 219 of 24 July 2012.
[3] COM(2012) 750 final.
[4] COM(2012) 751 final.
[5] SWD(2013) 118 final. 13 in-depth reviews were published on 10 April 2013. While selected for an in-depth review in the AMR, Cyprus was ultimately not reviewed under the Macroeconomic Imbalance Procedure in view of the advanced preparations for a financial assistance programme.

Overall assessment

In the Commission's assessment, Italy has made some progress towards addressing the CSRs of the Council Recommendation. While a sizeable effort has been made to tackle the issues identified in the 2012 CSRs, gaps in implementation and the persistence or even exacerbation of several key challenges have hampered progress.

The ambitious and wide-ranging policy action taken so far appears relevant to addressing the challenges identified in the 2012 CSRs and meeting the priorities set out in the AGS. The ambitious fiscal consolidation strategy put in place, enriched with measures aimed at enhancing the efficiency of public expenditure, strengthening the fiscal framework and improving tax compliance, have been strong signals of Italy's commitment to bringing the public finances onto a sustainable path, which is an essential prerequisite for anchoring market confidence and macroeconomic stability. On the structural side, key measures have been adopted to remove Italy's deep-rooted bottlenecks to growth. They aim to: foster competition in some product and services markets, including the network industries; improve the performance of the education system; address segmentation in the labour market; promote the responsiveness of wages to economic and competitive conditions; foster innovation; enhance the quality of the business environment; and improve the absorption of structural funds.

The implementation, at all levels of government and by all relevant stakeholders, of the measures taken remains challenging and entails risks in terms of credibility of action, however relevant and ambitious the reform action on the fiscal and structural front might be. In the case of Italy, implementation remains a critical challenge in three respects. First, although a large part of the measures adopted are already operational, others – in particular in the labour market, network industries and administrative simplification – still require the adoption of enacting legislation or regulations.[6] This has become a matter of urgency for some important provisions where the deadline for their specification through secondary legislation has already expired. Second, it is essential to guarantee and monitor the proper application of the adopted measures on the ground. For this purpose, close coordination between central, regional and local governments and the active involvement of all relevant stakeholders play a key role. Lastly, in recent months, the implementation of some important provisions in the fields of competition and civil justice has been hampered by setbacks, while some relevant measures that have been proposed by the government in the areas of taxation and administrative simplification are still to be approved by the Italian Parliament.

The reform agenda needs to be taken forward in order to address the remaining severe challenges for the Italian economy. The high government debt remains a major burden on the Italian economy, especially against the background of slow growth. There is therefore a pressing need to pursue the fiscal adjustment effort in order to put the debt-to-GDP ratio on a steadily declining path, with positive feedback loops on confidence and growth. To ensure growth-friendly and equitable fiscal consolidation as recommended in the AGS, there remains scope for increasing the efficiency of expenditure and of the taxation system while pursuing

[6] According to a report published in February 2013 by the Italian government, a large part of the adopted measures do not need implementing legislation and are thus immediately applicable. Moreover, among the main implementing measures required, around 56% remain to be adopted.

with determination the fight against tax evasion, undeclared work and the shadow economy. Other key challenges are: making the labour market more inclusive, with particular attention to young people and women; improving the performance and quality of the education system, also with a view to facilitating the transition to work; further fostering competition in services and network industries; enhancing the business environment, including by improving the efficiency of the public administration; and achieving efficient management of structural funds. In addition, it is important to support the capacity of the banking sector to finance the economy and facilitate the needed adjustment, while the scope for alternative forms of financing for firms needs to be exploited. If combined, action in the areas of education, market functioning and enterprise financing could contribute to addressing Italy's weak performance in research and innovation. Lastly, as the protracted recession in Italy affects households' disposable income and employment opportunities, leading to an increased risk of poverty and social exclusion, the reform agenda needs to be informed by the principles of social equity and the efficiency and the effectiveness of the social protection system needs to be improved. The national reform programme submitted by Italy outlines the areas where the reform momentum needs to be maintained, within the constraints of the fiscal consolidation strategy laid out in the stability programme to bring the very high government debt-to-GDP ratio onto a declining path. While the ambition of the policy plans presented in the programmes has been restrained by the uncertain political context at the time of their submission, the new government has indicated the intention to strengthen the structural reform agenda, while confirming the budgetary targets put forward in the stability programme. A first step in this direction was made with the adoption on 17 May of a decree-law containing new provisions on real estate taxation and the extension of the wage supplementation scheme for under-employed workers, which is taken into account in this assessment.

2. ECONOMIC DEVELOPMENTS AND CHALLENGES

2.1. Recent economic developments and outlook

Recent economic developments

Italy is undergoing a protracted recession. Italy's real GDP contracted sharply during the 2008-09 economic and financial crisis. The recovery that followed was modest and short-lived: economic activity started contracting again in the second half of 2011, when the euro-area sovereign debt crisis spread to Italy. In 2012, it dropped by 2.4%, due to the strong fall in domestic demand driven by high uncertainty, tight financing conditions and declining disposable incomes. Employment also declined, more in terms of hours worked than of headcount employment, which fell by 0.3%. Combined with the increased participation of young and older people, this translated into an increase in the unemployment rate to 10.7% on average in 2012. Young people were particularly affected, with youth unemployment reaching 35.3% in 2012.

Economic outlook

According to the Commission 2013 spring forecast, high uncertainty continues to weigh on recovery prospects. Real GDP is projected to contract by a further 1.3% in 2013, on the back of persistent uncertainty and continued difficult access to credit. Subdued consumer and business confidence points to still contracting economic activity in the first half of the year. However, settlement of the government's commercial debt is expected to support a mild recovery as from the third quarter of 2013 and, in the absence of renewed tensions in financial markets and with improving confidence, private consumption and investment are set to stabilise in the second half of the year. In 2014, the gradual improvement in financing conditions supports domestic demand, especially investment in equipment. On the external side, the projected acceleration in global trade supports exports, especially towards non-EU trade partners. Overall, real GDP is anticipated to expand by 0.7% in 2014.

Employment is set to contract further in 2013. In 2013, on the back of further contraction in economic activity, employment is projected to continue declining, while a stabilisation is projected in 2014. The unemployment rate is set to rise further, to over 12% by 2014. Adjustment in employment entails some recovery in labour productivity. As wage growth remains subdued, the growth in nominal unit labour costs is projected to decelerate to around 1% over 2013-14.

The Italian government's macroeconomic outlook appears plausible for 2013 and optimistic for 2014. Italy's stability programme covers the period 2013-17. The macroeconomic projections are broadly in line with the Commission 2013 spring forecast for the current year, while they anticipate stronger economic recovery in 2014, driven by domestic demand. Real GDP is projected to continue growing at a dynamic pace in the outer years of the programme, also supported by the estimated impact of the adopted structural reforms. In line with the underlying macroeconomic scenario, the programme projects employment to recover as from next year and the unemployment rate to peak at 11.8% in 2014 and then to fall steadily. The outlook also implies a broadly balanced current account over the programme's horizon.

If properly and promptly implemented, the structural measures could have a sizeable impact on economic growth. The national reform programme estimates the impact of the measures adopted in the areas of labour market, product market and the business environment at 1.6 percentage points by 2015, 3.9 percentage points by 2020 and 6.9 percentage points in the long term. Simulations by the International Monetary Fund suggest an even bigger impact on economic growth.[7]

[7] According to the International Monetary Fund, the full implementation of Italy's product and labour market reforms should raise GDP by 5.7% over a five-year horizon and by 10.5% in the long term.

2.2. Challenges

High public debt and sluggish productivity performance, reflected in declining external competitiveness, weigh heavily on Italy's long-term economic outlook. The Italian economy is still affected by the high level of public debt that is coupled with persistently slow growth, driven by its weak productivity performance. The latter has in turn resulted in declining external competitiveness and the loss of export market shares.

Structural weaknesses are at the root of the sluggish productivity performance and loss of external competitiveness. As analysed in detail in the in-depth review (see Box 1), stagnating total factor productivity, which underlies Italy's poor productivity performance, is strongly related to the failure of many Italian firms to grow and become international players. Limited innovation capacity, institutional and regulatory barriers to firms' growth, obsolete corporate governance practices and the high cost of doing business are at the origin of the problem. Italy's exposure to competition from emerging countries, given the predominantly low- and medium-low technology composition of its exports, has also played a role.

The high government debt remains a major source of vulnerability for the Italian economy, especially against the background of persistently slow growth. Italy has the second highest debt-to-GDP ratio in the euro area, at 127% of GDP in 2012. While low growth makes it more difficult to put the public finances on a sustainable path, high public debt may in turn hamper growth prospects. In particular, the high level of taxation needed to service the debt dampens domestic demand and may raise the distortionary costs of taxation, while high interest expenditure crowds out productive public expenditure and reduces the room for social policies. The inefficiency of public spending in many areas adds to the challenge. Over the past two years, the adverse feedback loop between high debt and low growth has increased financial markets' concerns about debt sustainability. The sharp increase in the sovereign risk premium in 2011-12 translated into a higher cost of capital for the private sector, hampering productive investment. Despite some easing in financial market tensions since the second half of 2012, Italy remains vulnerable to sudden changes in market sentiment.

The challenges highlighted in the 2012 SWD[8] for Italy remain critical, while the crisis is putting pressure on the banking sector and social cohesion. The 2012 SWD identified challenges in the areas of taxation, the labour market, education, competition and the efficiency of the public administration. These challenges remain valid and some of them are amplified in the south. Addressing them, taking regional disparities into account, will also help to reduce the persistent north-south economic divide. Additional challenges derive from deteriorating bank asset quality, as well as an increasing risk of poverty and social exclusion due to the protracted recession.

The structure of the tax system is skewed towards distortionary taxes weighing on the factors of production and is unevenly distributed because of significant tax evasion. While in the short to medium term reducing the overall tax burden is not an option in the current budgetary conditions, there is scope for improving the efficiency of the tax system and reducing distortions. The high tax burden in Italy weighs heavily on labour and capital. By

[8] SWD(2012) 318 final.

contrast, the implicit tax rate on consumption remains low relative to the euro-area average, largely due to the erosion of the tax base through the extensive use of exemptions and reduced rates as well as tax evasion. As regards recurrent taxation of immovable property, which is considered to be among the least detrimental to growth, policy action in 2012 brought it in line with EU average, while better alignment of the property tax base with market values is needed to improve its fairness. Significant tax evasion and a large shadow economy contribute to the high statutory tax rates on compliant citizens and firms. Compliance costs and the administrative costs of revenue collection are in the upper range of the EU spectrum.

Employment and labour market participation among young people, women and older workers remain well below the EU average. In the context of a still segmented labour market, the vulnerable situation of young people continues to be a concern – the youth unemployment rate reached 35.3% in 2012 and in 2011 more than one in five 15-29-year-olds were neither in education nor employed – while low participation and employment among women, also due to the insufficient offer of care services, represent a missed opportunity for the economy and a risk for households' and children's well-being. These issues are particularly acute in the southern regions, where the poor performance of the labour market reflects the difficult general economic conditions. Following the latest pension reform adopted in 2011, which further raised the statutory retirement age, ensuring that older workers remain employable and have suitable job opportunities remains a challenge. Lastly, undeclared work remains an issue of concern in Italy.

The loss of external competitiveness of the Italian economy also requires adjustments on the wage setting side. Over the last years, Italy's lacklustre productivity performance has not been adequately reflected in wage dynamics, leading to sustained unit labour cost growth and loss of cost competitiveness. The dominant level of collective bargaining in Italy remains the national level, even though important changes to the bargaining framework since the beginning of the 1990s have promoted a gradual shift towards the company level. This hampers a better alignment of wages to firms' or local economic and competitiveness conditions, while wages negotiated at the national sectoral level in line with expected inflation may not be consistent with Italy's need to regain cost competitiveness relative to trade partners.

Italy's weak human capital endowment hinders innovation and young graduates face a difficult labour market. Public expenditure on education as a share of GDP in Italy is among the lowest in the EU, notably at tertiary level. With a rate of 17.6% in 2012, Italy performs significantly worse than the EU average in terms of early school leaving, especially in the southern regions, which translates into a lack of basic skills. In addition, Italy registers the lowest tertiary education attainment rate in the EU for the 30-34-year-old age group and adult participation in lifelong learning is below the EU average. This low skill level certainly contributes to the economy's limited ability to innovate, as reflected in the weak research and innovation intensity of Italian businesses. There is also evidence of a difficult transition from education to the labour market, including for high-skilled young people, which is compounded by the effects of the economic crisis: in 2012, almost one in five young tertiary education graduates were unemployed.

Social cohesion is being undermined as a consequence of the economic crisis and the risk of poverty and social exclusion is markedly on the rise. As highlighted in the AGS, tackling the social consequences of the crisis represents a key challenge. Due to the protracted recession, the risk of poverty and social exclusion has been increasing and concerned more than one in four people in 2011. In addition, the risk of entering poverty is high, while the transition out of poverty is low. Economic developments in 2012 point to further deterioration in households' disposable income, while the social protection system, which is strongly biased towards entitlement-based pension expenditure, is not well equipped to face this situation.

Notwithstanding the action undertaken so far, the Italian economy continues to be characterised by barriers to competition, as well as infrastructure gaps. The persistence of sheltered market segments in some services and network industries results in higher input costs for the tradable sectors. High electricity and gas prices for both households and industrial customers not only reflect limited competition in the gas sector, but also infrastructure bottlenecks. Inadequate infrastructure is also an issue for transport, especially as regards intermodal systems, but also ports and railways, where Italy ranks among the bottom five performers in the EU concerning the quality and density of its infrastructure. In telecommunications, Italy ranks low in terms of penetration and coverage of broadband, especially high-speed broadband. This may result from a combination of obstacles to platform competition and insufficient information and communication technology literacy among the population.

Weaknesses in the public administration continue to contribute to an unfavourable business environment and hamper the full implementation of the measures adopted. In spite of efforts to modernise it, in line with the AGS, the Italian public administration shows a number of shortcomings, namely the long duration of proceedings in civil justice, unaddressed issues in the fight against corruption, considerable delays in the payment of goods and services purchased from private firms, cumbersome public procurement procedures and a persistently heavy and complex administrative and regulatory framework at various government levels. These weaknesses are mirrored in gaps in the implementation of the reforms adopted, which in turn limit their effectiveness. They also affect the quality of the business environment and discourage inward foreign direct investment, thus preventing Italy from reaping the associated benefits in terms of competitiveness and innovation. They also result in an inefficient functioning of the public employment services across the country. Furthermore, important weaknesses in administrative capacity continue to hamper the good use of structural funds, especially in the southern regions.

The resilience of Italian banks has weakened since mid-2011. While the Italian banking sector showed resilience in the aftermath of the global financial crisis, the protracted economic recession affected the quality of its assets. As analysed in the 2013 in-depth review for Italy (see Box 1), this makes it difficult to provide credit to the economy, in particular to SMEs. Restoring normal lending to the economy is identified as a priority in the AGS.

Box 1 – Summary of the 2013 in-depth review (IDR) under the Macroeconomic Imbalance Procedure (MIP)

- **The second in-depth review for Italy, presented by the Commission on 10 April, concludes that the Italian economy is experiencing macroeconomic imbalances, which require monitoring and decisive policy action**. Italy’s high government debt, the loss of external competitiveness and its underlying sluggish productivity performance are the main macroeconomic imbalances. In particular, persistently weak productivity, rooted in structural weaknesses and insufficiently reflected in wage dynamics, led to increasing unit labour costs, the effect of which has been further amplified by a substantial appreciation of Italy’s nominal effective exchange rate between 2003 and 2009.

- **An unfavourable product specialisation model and the limited ability of Italian firms to grow are among the main factors behind the country’s poor productivity performance**. Italy’s specialisation model is very similar to that of emerging markets with most of the value added in relatively low-technology traditional sectors, mainly due to Italian firms’ limited innovation capacity. The in-depth review focuses on the role of micro- and small enterprises in the Italian economy, arguing that their predominance highlights the difficulties faced by Italian firms in growing and becoming international players because of institutional and regulatory barriers, structural firm features and an unfriendly business environment. These factors also limit the inflow of foreign direct investment, preventing Italy from taking advantage of the direct and indirect benefits that inward foreign direct investment brings, such as the transfer of capital and knowledge, increased involvement in world trade and the impulse towards a more competitive business environment and modern corporate management.

- **The resilience of the Italian banking sector has weakened since mid-2011, undermining banks’ ability to support economic activity and adjustment**. Italian banks’ loss of access to international wholesale funding following the extension of the euro-area sovereign debt crisis to Italy has significantly increased the sector’s dependence on Eurosystem refinancing. The double-dip recession in Italy has increased credit risk in the private sector, burdening Italian banks with a large stock of non-performing loans. This has led to a protracted contraction in credit, while the average cost of new credit remains elevated despite an accommodative monetary policy at euro-area level.

- **The persistence of sizeable vulnerabilities in the Italian economy translates into policy challenges in a wide range of areas**. The remaining avenues for action, on the fiscal and structural front, to strengthen the adjustment capacity of the Italian economy, are analysed in this SWD.

3. ASSESSMENT OF POLICY AGENDA

3.1. Fiscal policy and taxation

Budgetary developments and debt dynamics

The stability programme foresees a continued decline in the headline deficit, from 3% of GDP in 2012, and reaffirms the target of a balanced budget in structural terms as from 2013. Italy's new government has confirmed the budgetary objectives of the stability programme, already endorsed by Parliament on 7 May. The deficit for 2012, at 3.0% of GDP, was significantly above the 1.7% planned in the 2012 update of the stability programme and also above the 2.6% revised target published in September. This was largely due to lower-than-projected growth, notably in domestic demand, which significantly dampened revenue dynamics. For 2013, the programme targets a deficit of 2.9% of GDP. This includes the impact of the settlement of commercial debt, which is planned to increase the deficit by 0.5 percentage points of GDP. The decree-law adopted on 17 May suspends the June instalment of the property tax on owner-occupied houses, while committing the government to an overall redesign of the legislation on real estate taxation.[9] It also extends the wage supplementation scheme to workers not already covered for the year 2013, by reallocating available budgetary resources. The programme projects the deficit to decline to 1.8% of GDP in 2014. Looking ahead, the deficit ratio is planned to decrease steadily, to 0.4% by 2017, partly due to unspecified measures worth 0.6 percentage points of GDP in cumulative terms over 2015-17. The programme confirms the medium-term objective (MTO) for Italy of a balanced budget in structural terms and plans to achieve and maintain it as from 2013, which is in line with the Stability and Growth Pact, and in particular the need to put the debt ratio on a steadily declining path.

According to the Commission 2013 spring forecast, **Italy corrected its excessive deficit in 2012 in a durable way, conditional upon full implementation of the consolidation measures adopted in 2011-12**. The Commission 2013 spring forecast projects the deficit to be 2.9% of GDP this year, in line with the government's target, and to decline to 2.5% of GDP in 2014 – i.e. 0.7 percentage points of GDP higher than the government's target, on the back of the slower economic recovery assumed in the Commission 2013 spring forecast. Both the government's target and the Commission 2013 spring forecast incorporate the full implementation of the consolidation measures adopted in 2011-12, notably the additional expenditure restraint enacted with the spending review, the 1 percentage point hike in the standard rate of VAT (to 22%) as from July 2013 and the entry into force of new or higher taxes on financial wealth and transactions, and on local public services. The decree-law adopted by the government on 17 May, i.e. after the Commission 2013 spring forecast, is assessed not to significantly affect the 2013 deficit projection, provided that it is properly implemented.

Italy achieved a notable improvement in the structural balance over 2012. Italy's structural balance, i.e. the general government balance corrected for the cycle and net of the

[9] A safeguard clause ensures that the redesign has to be made in the full respect of the budgetary targets in primary terms; furthermore, if the budgetary-neutral reform fails to be approved by the end of August 2013, the suspended property tax instalment will have to be paid by 16 September.

impact of one-off measures, improved by a sizeable 2¼ percentage points of potential GDP in 2012. When recalculated by the Commission based on the information in the stability programme, following the commonly agreed methodology, the structural balance is planned to improve further, by 1.0 percentage point of GDP this year, i.e. broadly in line with the Commission 2013 spring forecast.[10] According to the stability programme, it is expected to improve by 0.4 percentage points in 2014, whereas the spring forecast projects a slight deterioration. In 2013, the planned budgetary position in structural terms is slightly negative, at -½% of potential GDP, due to the impact of the additional investment expenditure related to the settlement of the commercial debt. In the stability programme, Italy's MTO of a balanced budgetary position in (recalculated) structural terms is projected to be appropriately reached in 2014, and broadly maintained – albeit worsening slightly – in the outer years of the programme horizon. The primary balance in (recalculated) structural terms is projected to improve from around 4% of GDP in 2012 to nearly 6% in 2017.

Expenditure growth has been contained, contributing to progress towards the MTO. In 2012, thanks to the savings measures enacted in 2010-11, primary expenditure in nominal terms contracted for the third year in a row, decreasing by over 1.5% relative to the 2009 level. According to the information provided in the programme and to the Commission 2013 spring forecast, the growth rate of government expenditure in 2012, net of discretionary revenue measures, was well below the lower benchmark of -0.8% and thus contributed to an annual structural adjustment towards the MTO of 0.5% of GDP. In the two subsequent years, the growth rate of expenditure is also set to contribute to progress towards the MTO, as it will remain below the lower benchmarks of -0.81% and -1.07% in 2013 and 2014 respectively. Following an overall assessment of Italy's budgetary developments and plans, with the structural balance as a reference, including an analysis of expenditure net of discretionary revenue measures, the adjustment path towards the MTO was very significant in 2012, also given the tax-poor composition of growth. The structural adjustment expected in the Commission 2013 spring forecast for 2013 is also appropriate. However, the departure from the adjustment path towards the MTO shown in the forecast for 2014 does not appear to be appropriate.

[10] The structural balances as recalculated by the Commission differ slightly from those presented in the stability programme mainly because the former are based on output gaps computed through a methodology that limits backward revisions compared to the Commission 2013 spring forecast, while the methodology used in the stability programme allows for backward revisions.

Box 2. Main measures

Main budgetary measures

Revenue	Expenditure
2012	
• Taxation of real-estate property (+0.9%) • Excise duties (+0.5 %) • Stamp duties on financial assets (+0.3%) • Harmonisation of personal withholding tax rate on interests and dividends (+0.1%) • Regional surtax on personal incomes (+0.1%) • Fight against tax evasion (+0.5%) • Allowance for new corporate equity (ACE) [11] and deductibility of labour costs (-0.1%)	• Lower transfers to local governments (-0.2%) • Cuts to ministerial spending (-0.4%) • Partial de-indexation of pensions (-0.1%) • Other current expenditure (local authorities, military missions, earthquake) (+0.2%)
2013	
• VAT rate (+0.1 %) and excise duties (+0.1%) • Stamp duties on financial assets (+0.2%) • Financial transaction tax (+0.1%) • Social contributions from self-employed (+0.1%) • Fight against tax evasion (+0.1%) • Productivity-related tax incentives (-0.1%) • ACE and deductibility of labour costs (-0.3%)	• Higher retirement age and de-indexation of pensions (-0.4%) • Cuts to ministerial/local spending (-0.8%) • Other current expenditure (local authorities, military missions, earthquake) (+0.6%) • Payment of commercial debt arrears (investment) (+0.5%)
2014	
• ACE and deductibility of labour costs (-0.3%) • Productivity-related tax incentives (-0.1%)	• Savings from higher retirement age (-0.1%) • Cuts to ministerial/local spending (-0.9%)

Note: The budgetary impact in the table is the impact reported in the programme, i.e. by the national authorities, in % of GDP. A plus sign indicates that revenue/expenditure increases as a consequence of the measure. The degree of detail reflects the information made available in the stability programme and in the multiannual budget.

Despite the budgetary consolidation, Italy's general government gross debt-to-GDP ratio is set to rise further in 2013-14. The debt-to-GDP ratio rose further in 2012, by 6.2 percentage points of GDP, due to negative nominal GDP growth, higher interest rates and some debt-increasing stock-flow adjustments, mainly reflecting Italy's contribution to the euro-area financial support mechanisms. In 2013, both the stability programme and the Commission 2013 spring forecast project a further increase in the debt-to-GDP ratio, also due to the planned settlement of around EUR 20 billion of commercial credits owed by the public sector for goods and services purchased from private providers – which, for the part related to current expenditure that was already recorded in past years' deficit, increases the stock-flow adjustment, while the 0.5% of GDP corresponding to capital expenditure impacts on the primary balance. The programme's debt projections incorporate a 1 percentage point of GDP per year reduction impact from the proceeds of privatisations over 2013-17, which remain unspecified. Regarding compliance with the debt criterion, Italy is in a three-year transition period as from 2013, and the debt trajectory in the stability programme ensures sufficient progress towards compliance with it. Medium-term debt projections (see Graph below Table V in annex) suggest that full implementation of the programme, including the planned

[11] The ACE allows companies to deduct part of the notional return on new injections of equity capital from taxable income.

privatisations, would allow reducing the debt by 2020 faster than when using the Commission forecast as a basis, though it would still remain well above the 60% of GDP reference value.

Risks to both the deficit and debt outlook stem mainly from the possible non-implementation of the budgetary measures and structural reforms adopted, both of which are essential to anchor market confidence and boost growth and jobs.

Box 3. Excessive Deficit Procedure (EDP) for Italy

On 2 December 2009, the Council decided that an excessive deficit existed in Italy. The Council recommended that Italy's authorities put an end to the present excessive deficit situation by 2012, by bringing the general government deficit below 3% of GDP in a credible and sustainable manner and by taking action in a medium-term framework. Specifically, to this end, the Italian authorities were recommended to: (a) implement the budgetary measures in 2010 as planned in the three-year fiscal package for 2009-11 approved in summer 2008 and confirmed in the Economic and Financial Planning Document 2010-13; (b) ensure an average annual fiscal effort of at least 0.5 percentage points of GDP over the period 2010-12, which should also contribute to bringing the government gross debt-to-GDP ratio back on a declining path that approaches the 60% of GDP reference value at a satisfactory pace by restoring the primary surplus to an adequate level; (c) specify the measures necessary to achieve the correction of the excessive deficit by 2012, cyclical conditions permitting, and accelerate the reduction of the deficit if economic or budgetary conditions turn out better than currently expected. In addition, the Italian authorities should seize any opportunities beyond the fiscal effort, including from better economic conditions, to accelerate the reduction of the gross debt-to-GDP ratio towards the 60% of GDP reference value. Furthermore, the Council invited the Italian authorities to implement reforms with a view to raising potential GDP growth. This includes reforms conducive to enhancing the quality of public finances, by focusing on spending efficiency and composition, in particular by continuing to improve fiscal governance and the work on a new framework for fiscal federalism that ensures the accountability of local governments and underpins fiscal discipline.

An overview of the current state of the EDPs, including also additional EDP steps adopted after the finalisation of this SWD, is available on:
http://ec.europa.eu/economy_finance/economic_governance/sgp/deficit/index_en.htm (see the country sections at the bottom of the page).

Long-term sustainability

The latest pension reform is set to restrain long-term growth in age-related expenditure. Based on an 'early-detection' indicator (S0), a composite indicator constructed with a whole set of fiscal and financial-competitiveness variables, Italy does not appear to face a risk of fiscal stress in the short term, provided it continues to maintain a prudent fiscal stance and foster growth with ambitious structural measures, which is essential to anchor financial market confidence. The sustainability risks appear to be medium in the medium term, while being contained in a long-term perspective, conditional upon the full implementation of the planned ambitious fiscal consolidation and on maintaining the structural primary balance at around 5% of GDP well beyond 2014. On the basis of current policies, the general government debt would be on a declining path over the medium term and beyond. But, as the improved structural primary fiscal position expected to be reached by 2014 is rather demanding from both cross-country and historical perspectives, strong determination is needed to avoid slippages in the fiscal stance. Indeed, the risks would be much higher in the event of the structural primary balance reverting to the lower values observed in the past. Over the long term, the projected change in age-related expenditure in Italy is below the EU average, partly thanks to measures that contribute to broadly stabilising pension spending as a share of GDP.

Fiscal framework

While significant action has been taken to strengthen the fiscal framework, there is still room for improving the efficiency of public expenditure. In 2012, the Council Recommendation for Italy contained a CSR calling for the appropriate specification of the constitutional balanced budget rule consistently with the EU framework and for action to enhance the efficiency of public expenditure. The part of the CSR covering the balanced budget rule has been addressed through relevant, ambitious and credible action, whereas only some progress has been made on the front of expenditure. Relevant measures have indeed been taken to increase expenditure efficiency, but implementation gaps undermine credibility of action, and there remains considerable scope for further measures.

The balanced budget rule represents a major step towards strengthening Italy's fiscal framework. In line with the 2012 CSR, the introduction of a balanced budget rule in the Italian Constitution, approved in April 2012, was followed in December by legislation specifying the modalities of application of the rule. This has been done in broad consistency with the Stability and Growth Pact and the fiscal compact. It is stipulated that a general government budget balance in structural terms will have to be ensured as from 2014, while subnational governments will have two more years to comply with the rule.[12] In the context of increased tax autonomy envisaged under the ongoing fiscal federalism process, the success of the new provisions depends on the good coordination across government levels. In addition, the correction plan introduced to rectify temporary deviations could be reinforced by specifying the measures envisaged. An independent fiscal council attached to the Italian Parliament will be tasked with overseeing official macroeconomic and fiscal projections. Provided that its independence is safeguarded, the fiscal council can contribute to ensuring that fiscal plans are based on realistic and prudent projections.

To increase the efficiency of public expenditure, progress has been made with the conduct of spending reviews at central government level, but significant scope for improvement remains. Targeted cuts to departmental expenditure have been accompanied by a rationalisation of procurement procedures aimed at reducing unit costs, while local governments are requested to achieve similar efficiency gains within their administrations following the cuts to transfers from the centre. Nevertheless, the enacting decree specifying the envisaged reduction of public employment has not been adopted and the planned reduction in the number of provinces has not been approved by the Italian Parliament. Meanwhile, the lack of a comprehensive strategy in terms of natural disaster risk prevention has weighed on public expenditure as a number of natural disasters have hit the country. The national reform programme announces the launching of another spending review round in 2013, but there is no plan to make this process a regular exercise in Italy.

[12] Regions will have to maintain a balanced budget at their level, while local governments will be allowed to borrow to finance investment.

Tax system

Following important efforts to shift the tax burden away from the factors of production onto consumption and immovable property in 2010-11, the action undertaken in response to the 2012 CSR on taxation has been more limited. In 2012, the Council Recommendation called on Italy to pursue the fight against evasion, reduce the scope of tax expenditures and further shift the tax burden away from the factors of production. Several measures adopted over 2010-11 had already shifted the tax burden from labour and capital onto consumption and property, and intensified the fight against tax evasion. Starting from these steps, the relevance and ambition of the additional measures adopted in 2012 have been limited. Policy action on taxation has focused more on finding the resources – in the form of expenditure savings through the spending review – to replace some of the previously stipulated increases in taxation on consumption than on alleviating the tax burden on labour and capital, with the stated intention to avoid further depressing domestic demand. For instance, the 2.5 percentage points increase in both the standard and the reduced VAT rates that was legislated in 2011 has been scaled down in the second half of 2012 to just 1 percentage point increase in the standard rate as from July 2013. Moreover, a planned reform of the tax system failed to be adopted by the Italian Parliament, hence affecting credibility of action.

There remains room for alleviating the tax burden on the factors of production but in a revenue-neutral way. Italy still taxes labour and capital heavily: in 2011, it had the second highest implicit tax rate on labour in the EU, at 42.3%, and a high tax wedge on low-income workers, especially second-earners. Italy's implicit tax rate on capital was the fourth highest in the EU in 2011. In 2012, the increase in excise duties on fuels and reduced deductibility for company cars helped to stem the long-term decreasing trend in the ratio of environmental tax revenues to GDP. At the same time, taxation on consumption remains rather low in Italy – the implicit tax rate on consumption was the fourth lowest in the EU in 2011 – largely due to the erosion of the tax base through the widespread use of exemptions and reduced rates, as well as sizeable tax evasion. Labour income taxation was only marginally lowered by making the labour component deductible from the regional tax on productive activities (IRAP), with greater deductions in the case of women, young workers and for southern regions; offering tax incentives for productivity-related pay negotiated at firm level; and providing more generous allowances for dependent children. As regards taxation on immovable property, the impact of the increase adopted in December 2011, through the reintroduction of recurrent taxation on primary residences and the proportional increase in the coefficient to revaluate the outdated cadastral values, was further amplified by the higher rates implemented by most local authorities in 2012, bringing the impact of recurrent property taxation in line with the EU average. The redesign of property taxation foreseen by the decree-law adopted on 17 May could be the occasion to improve its distributional impact, without lowering revenues. The government also intends to review the allocation of tax powers between central and local governments, concerning both recurrent taxation of property and other taxes on locally provided services (e.g. waste management). It is worth noting that, in a context where significant reductions in the overall tax level cannot be made yet, taxation on immovable property appears preferable to other taxes, since it is less harmful to growth while being consistent with equity objectives, if properly designed. In addition, since real estate property is by nature immovable, the tax is harder to evade making the revenue generated from it more predictable, and it is consistent with the ongoing decentralisation of fiscal powers in Italy. Finally, the inclusion of primary residences in the tax base contributes to reducing the existing misalignment between taxation of owner-occupied and rented houses, and more generally, between taxation of real estate and of other asset classes, such as equities and bonds.

An ambitious reform of the tax system was in the pipeline but is yet to be adopted. A draft enabling law appropriately foresees a streamlining of tax expenditures, which significantly narrow the tax base, while making the system overly complex. It also envisages an important revision of cadastral values, to bring them closer to market values. Such a move would improve the fairness of recurrent taxation on immovable property. The draft enabling law also envisages measures to improve tax compliance, including monitoring of the tax gap, a simplification of rules and, for the largest corporations, regular exchange of information and pre-assessment of taxes. The draft law, however, has not yet been approved by the Italian Parliament, while the redesign of property taxation foreseen by the May decree-law could spur the reform of cadastral values.

Measures have been taken to improve tax governance, enhance compliance and fight against evasion but the size of the challenge requires further action. Steps towards greater traceability of transactions – notably by imposing lower thresholds for the use of cash – and better targeting tax assessments and inspections appear promising and could effectively help to fight against tax evasion and enhance compliance. Similarly, the recent implementation of a system allowing the tax administration to crosscheck data from banks and financial operators with income tax statements may contribute to deterring evasion and increasing recovery. As also acknowledged in the national reform programme, pursuing this effort is essential. This will require making full use of existing instruments, monitoring their impact and undertaking additional action.

3.2. Financial sector

The Italian banking sector held up quite well in the aftermath of the global financial crisis, but its ability to provide credit to the Italian economy, in particular to small firms, has declined owing to the double-dip recession. The banking sector continues to play a central role in the financing of Italian firms, in particular small and medium-sized enterprises (SMEs). The double-dip recession has worsened banks' profitability as non-performing loans have been rising significantly. This, together with the fragmentation of the euro-area financial system, implied tighter credit conditions for firms, especially SMEs. While restoring the flow of credit to the economy is important, further large increases in firms' leverage could be challenging for financial stability and thus for the economy as a whole, warranting additional efforts to encourage equity financing.

Access to finance

Several measures have been taken to ease Italian firms' access to funding, also by encouraging recourse to non-bank sources, but their scope has so far been limited. In

2012, the Council Recommendation for Italy highlighted the need for easier access to finance for firms; some progress has been made in this area. The corporate sector is highly dependent on banks for its funding: in 2011, over 70% of Italian firms' financial debt consisted of bank loans, significantly more than in other advanced economies.[13] The introduction of the ACE in 2012 carries significant potential to reduce the debt bias in corporate financing by encouraging reliance on equity, but there is room to expand it. Other recent measures include setting up a Fund for Sustainable Growth in charge of streamlining subsidies to firms, allowing SMEs to access capital markets through mini-bonds with tax-deductible interest payments, introducing crowd-funding to support innovative start-ups and offering tax incentives for the use of project bonds for infrastructure investment. Action has also been undertaken to accelerate the payment of commercial debt and ensure swifter payment by the public administration to suppliers of goods and services (see section 3.5). In addition, the Central Guarantee Fund, which provides government-guaranteed loans to SMEs, is refinanced up to 2014 and an additional EUR 10 billion is devoted to SMEs' funding through a state-controlled joint-stock company (Cassa Depositi e Prestiti). These measures appear relevant and credible, but their ambition needs to be weighed against Italy's limited fiscal space.

Banking sector

The capacity of Italian banks to support economic activity and adjustment has weakened due to the protracted recession. Against the background of growing vulnerabilities in the banking sector, as flagged in the 2013 in-depth review for Italy (see Box 1), some initiatives have been taken, notably to improve asset quality, and further policy attention is warranted.

[13] Bank of Italy, 'Annual report 2011', 2012.

Low cost efficiency and increasing non-performing loans affect the profitability of the Italian banking sector. From an international perspective, Italian banks are characterised by low profitability due to structurally low operational efficiency, but also small income margins and high loan-loss provisions due to the increasing stock of non-performing loans in the context of the double-dip recession. The Bank of Italy has launched a round of on-site inspections, which has already resulted in some higher provisioning. The relatively high level of non-performing loans also reflects the slow recovery procedures in Italy as well as the difficulties experienced in repossessing collateral and a strict definition adopted by the Bank of Italy.

Corporate governance of some categories of banks could hinder the effectiveness of financial intermediation. In Italy, cooperative and mutual banks (banche popolari e cooperative) play an important role in financing the real economy, especially SMEs, yet their organisational structure often appears to be weak. Moreover, for some of the largest cooperative banks, the restrictions on ownership and voting rights may not provide adequate incentives to control the banks' management and hence to invest in their equity. Similarly, the de facto control of some commercial banks by banking foundations, which are non-profit entities strongly embedded in local business and politics, may lead to concentration of management power and internal control shortcomings.

Italy's bank resolution framework has proven its effectiveness in the past, but would gain from the availability of complementary powers for the Bank of Italy. Italy has a long experience with bank resolution tools, in particular special administration. The effectiveness of its bank resolution regime would be further enhanced by progress in the field of EU legislation on bank recovery and resolution. Notwithstanding these points, the Bank of Italy's powers to replace the senior management of banks could be extended outside cases of special administration. This complementary power would enhance the Bank of Italy's ability to address problems in banks in a preventive manner.

3.3. Labour market, education and social policies

Further efforts are needed to obtain a well-performing educational system and labour market, as both play a crucial role in restoring competitiveness and fostering growth, as stressed in the AGS. The labour market reform adopted in June 2012 relevantly and ambitiously addresses some important shortcomings that were raised in the 2012 CSR, while some efforts to improve the performance of education have been made. However, the educational system in Italy still shows severe weaknesses in terms of quality and outcomes, which in turn hamper a smooth transition to work, while access to the labour market remains difficult for young people and women.

Labour market

Important steps have been taken to enhance the functioning of the labour market and the wage bargaining framework, however there remains scope for action to address the vulnerable situation of young people and women on the labour market. In 2012, two CSRs covered the labour market and wage bargaining and urged Italy to address youth unemployment, tackle labour market segmentation, encourage female labour market participation and promote the responsiveness of wages to productivity developments. Italy has made some progress with respect to these CSRs. Although the measures adopted so far are broadly relevant to addressing the aforementioned challenges, some of them – notably those aimed at encouraging the participation of young people and women in the labour market – lack ambition relative to the size of the challenges, while credibility of action depends on the effective implementation and monitoring of the enacted measures.

In line with the 2012 CSR, Italy adopted an ambitious reform in June 2012, with a view to addressing the rigidities and segmentation of the labour market. The segmentation of the Italian labour market, with many young workers in precarious employment, hampers job reallocation and is a source of inequity. The June 2012 labour market reform strives to improve exit flexibility and introduces disincentives to the use (or abuse) of temporary and atypical contracts. It also gradually introduces an integrated and more comprehensive insurance-based system of unemployment benefits, which will become fully operational as of 2017. Given its broad scope, the reform is ambitious and relevant to the 2012 CSR and the Europe 2020 target of a 67-69% employment rate, where Italy still lags behind the EU, with an employment rate of 61% in 2012. The success of the new legislation as regards dismissals will depend on its interpretation by the labour courts. Furthermore, the impact of the new constraints on the use of fixed-term and atypical contracts needs to be monitored as regards its impact on reducing segmentation and sustaining job creation.

The effective implementation of the labour market reform still requires the adoption of some enacting legislation, while careful monitoring of its functioning is essential. Before producing all its anticipated benefits, the reform still requires the adoption of enacting decrees, in particular to strengthen active labour market policies. Moreover, the envisaged close monitoring of the impact of the reform, the modalities of which are described in the national reform programme, needs to be ensured. Finally, enhancing the efficiency and strengthening the role of public employment services, deemed crucial in the national reform programme, will also be instrumental to the success of the reform in promoting an efficient activation strategy and to the successful delivery of a Youth Guarantee.[14]

Youth unemployment is on the rise, calling for a more ambitious effort. Youth unemployment has climbed since the onset of the crisis and further deteriorated in 2012, reaching 35.3%.[15] Young tertiary graduates are also affected, with an unemployment rate of 19% in 2012, against 12% across the euro area. Various initiatives have been launched to support youth employability, from reforming the apprenticeship system to introducing fiscal incentives to recruit high-skilled young people – which are, however, not yet operational, pending the adoption of the required implementing acts – and reprogramming structural funds through the Cohesion Action Plan. In addition, measures adopted last October allow older workers to shift from full-time to part-time employment, in order to favour the recruitment of young people with apprenticeship or permanent contracts. Although relevant, these actions are limited in scope and some gaps in implementation hamper their effectiveness. If properly deployed, the Youth Guarantee could prove helpful to combat youth unemployment.

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[14] The Council Recommendation of 22 April 2013 on establishing a Youth Guarantee (2013/C 120/01) calls for Youth Guarantee schemes that ensure that all young people under the age of 25 years receive a good-quality offer of employment, continued education, an apprenticeship or a traineeship within four months of becoming unemployed or leaving formal education.

[15] Report 'Youth Employment Action Teams – Update for the Spring European Council, 14-15 March 2013'.

Obstacles to women's access to the labour market persist. At 57% in 2012, women's participation in the labour force[16] in Italy remains significantly below the EU average of 69.5% and the employment gender gap was the second highest in the EU in 2011. However, there was a slight increase in the female employment rate from 46.5% in 2011 to 47.1% in 2012. The government introduced a National Plan for Families in June 2012, which includes measures to increase the availability, quality and affordability of childcare and long-term care services and to better reconcile work and family life. Similarly, some provisions of the labour market reform encourage women's recruitment, prevent discrimination against pregnant women and facilitate their return to work. The Cohesion Action Plan also includes measures to promote access to childcare and elderly care facilities in Italy's southern regions. Albeit relevant, these measures have a limited scope and many of them are not yet operational. Moreover, high marginal effective tax rates for second-earners, particularly in low-income households, compared with those for single individuals, could also deter labour market entry.

Efforts to further foster decentralisation of wage bargaining should be conducive to greater responsiveness of wages to productivity developments and local labour market conditions. In November 2012, the social partners signed an agreement (the so-called productivity pact) that acknowledges the need to link wages set in national contracts not only to expected inflation, but also to the economic and competitive conditions of the country and sector concerned and promotes further decentralisation of collective bargaining by strengthening the second tier of bargaining. The agreement also calls for a more prominent role of collective bargaining in regulating certain subjects that impact on productivity, currently defined exclusively or prevalently by law, and it commits the parties to a redefinition of the rules on representativeness in collective bargaining. Although the largest trade union, CGIL, did not sign the pact, it has agreed to entrust productivity-related pay to the decentralised level of bargaining. The government is supporting the agreement with tax rebates on productivity-related pay set in second tier contracts. The 2013-15 budget law earmarked EUR 2.1 billion over 2013-14 to these tax rebates.

If properly implemented, the productivity pact could lay the foundations for a more stable and effective industrial relations system. However, the agreement only sets out broad guidelines, and requires further social partners' agreements to be underpinned by specific commitments and to be fully implemented. An enacting decree adopted last January lays down criteria for the applicability of the tax rebates on productivity-related pay, by linking it to measurable results in terms of productivity, profitability, efficiency and quality, based on indicators to be specified in the contract, or by making it subject to a combination of organisational and technological changes that are expected to lead to such improvements. By doing so, the decree represents an important step to prevent deadweight losses and misuses. In April, the Italian authorities and the social partners indicated that agreed changes in the distribution of working hours are a sufficient condition to benefit from the rebates. Although this may extend the number of firms potentially benefitting from the scheme, it could substantially limit the effectiveness of the tax incentives in fostering productivity at systemic level. Steps have been taken also to strengthen union representativeness at the firm level, with

[16] The rate of participation in the labour force includes working-age people who are either employed or unemployed and looking for a job.

a further agreement signed in April by the major trade unions, now being discussed with employers' organisations.

After controls have been stepped up, there is still scope for pursuing the fight against the shadow economy and undeclared work. The shadow economy was estimated to account for between 16.3% and 17.5% of GDP[17] in 2008, while undeclared work represented 12.2% of total employment,[18] with peaks in southern regions. So far, the main concrete step to bring the shadow economy and undeclared work into the open has been the transposition of Directive 2009/52/EC providing for minimum standards on sanctions and measures against employers of illegally staying third-country nationals. Nevertheless, its implementation has yet to be monitored and it covers only third-country nationals, hence the importance of determination in the fight against the shadow economy and undeclared work, as also stated in the national reform programme.

Education

Some measures have been adopted with a view to improving the quality of the education system, but more ambition is needed. In 2012, the Council Recommendation called on Italy to improve the performance of education and transition to work. Some progress has been made towards addressing this CSR: the measures adopted so far are indeed relevant and credible, but their scope remains narrow compared with the size of the challenge.

The early school leaving rate in Italy remains well above the EU average. The early school leaving rate declined further in 2012 – to 17.6%, from 18.2% in 2011 – but remains markedly above the EU average of 12.8% and the Europe 2020 target of 15-16%. With a rate of 44% in 2011, third-country nationals weigh heavily on the overall early school leaving score in Italy. While there is not yet evidence of a comprehensive strategy to address early school leaving, short-term action to tackle this issue could be taken through the Cohesion Action Plan,[19] which identifies education as a priority area, as confirmed in the national reform programme. In the medium to long term, improving school quality and outcomes would contribute to reducing early school leaving. The main measure in this area was approved in March 2013 and establishes a national system for the evaluation of school institutions, which will be coordinated by the school evaluation agency (INVALSI) and could prove useful, if endowed with adequate resources.

Enhancing the performance of education crucially depends on the quality of teaching. The teaching profession in Italy follows a single career pathway with salary progression based on seniority only, limited prospects in terms of professional development, no comprehensive assessment of performance and, compared with other countries, low salary levels relative to other graduate jobs.[20]

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[17] ISTAT, 2010.
[18] ISTAT, 2010.
[19] The Cohesion Action Plan was adopted at the end of 2011, with the ambition to improveof improving the use of structural funds through the prioritisation and the redirection of resources towards four key areas (education, employment, railway transport and the digital agenda), later extended notably to childcare and elderly care structures.
[20] OECD, 'Education at a Glance', 2012.

Italy continues to underperform as regards the Europe 2020 target for tertiary education. Despite some slight progress since 2009, Italy's tertiary attainment rate is still the lowest at EU level, at 21.7% in 2012 against 35.8% in the EU. In order to help students to make a more informed choice and hence contribute to reducing tertiary dropout rates, a single web portal displaying the range of available university courses was launched in July 2012. However, this measure is limited in scope, while targeted action to tailor the supply of high-level skills to labour market needs, notably through career and counselling services, remains insufficient. However, the implementation of the 2010 university reform is progressing. The evaluation and accreditation system led by the university and research evaluation agency (ANVUR) will be gradually introduced from the 2013-14 academic year. This will help to implement one of the principles of the reform, according to which an increasing share of public funding for universities must be allocated on the basis of teaching and research performance. In 2012, performance-related funding represented only 13% of total funding, up from 7% in 2009.

Facilitating the transition from education to work has been at the core of several initiatives. The June 2012 labour market reform aims to make apprenticeships a major port of entry towards stable jobs. To the same end, in December 2012 an agreement was concluded with Germany to foster cooperation on mobility and work-based learning in vocational education and training. Moreover, the recent establishment of 62 higher technical institutes (ITS) providing short-cycle tertiary qualifications in a number of key sectors of the economy is a relevant first step to develop a vocational higher education system, in line with the AGS priority on tackling unemployment. However, avenues for action remain to be explored in order to upgrade the vocational education system, both at upper secondary and tertiary level.

If properly implemented, the measures adopted to encourage the nation-wide recognition of skills could lead to better use of competencies acquired throughout the life. As foreseen by the labour market reform, a legislative decree setting up a national system for the certification of skills, including the recognition of non-formal and informal learning, was adopted in January 2013. It now requires proper implementation, bearing in mind that the regions have exclusive regional responsibility for training policies.

Social policies

In line with the priorities identified in the AGS, Italy increasingly needs to tackle the social consequences of the economic crisis. Italy took action to support vulnerable groups, in a context where protracted recession is putting increasing pressure on social cohesion. Between 2008 and 2011, the risk of poverty or social exclusion rose by around 3 percentage points, to almost 30%, and the increase was particularly pronounced between 2010 and 2011. In addition, the risk of slipping into poverty is high, while the transition out of poverty is low.

Adequate distribution of social transfers and tailored policies are decisive to cope with increasing social needs. The effectiveness of social protection systems in reducing the risk of poverty and social exclusion depends on the composition of social protection expenditure. In Italy, the structure of social transfers is largely oriented towards the elderly and dominated by pension expenditure, which represented 16% of GDP in 2010, one of the highest shares in the EU. Social transfers excluding pensions are thus insufficient to reduce the total rate of poverty risk, and there is no nation-wide minimum income scheme in place.[21] Against the background of growing social vulnerability and in view of the Europe 2020 target on poverty and social exclusion, Italy is introducing the 'new social card', a state-sponsored credit card linked to a compulsory social reinsertion personalised programme, in 12 cities as a pilot experiment for 12 months, starting in 2013 and envisages to extend it, as indicated in the national reform programme. Although possibly relevant, this measure is limited in scope compared with the scale of the challenge. Fostering employability is key to favouring social inclusion and hence mitigating the negative social impact of the crisis. It is crucial that the reform agenda is informed by the principle of social equity and encompasses measures aimed at enhancing the efficiency and effectiveness of social transfers.

3.4. Structural measures promoting growth and competitiveness

Stimulating competitiveness is at the core of the AGS and remains a crucial challenge for Italy, despite the wide-ranging measures already adopted. Measures to encourage competition, liberalise sheltered market segments, promote transparency and ensure that the market operates smoothly in network industries, are crucial to address Italy's productivity challenge. By delivering lower prices, such reforms would also support the economic recovery and households' disposable income. The low innovation capability of the Italian economy also calls for measures to foster research and innovation, as recommended in the 2012 CSR. Notwithstanding the adoption of several key measures in these areas, the scope of the challenge leaves room for further action.

Market opening in services

Notable effort has been made towards liberalisation in the services sector. In 2012, the Council Recommendation for Italy flagged the importance of implementing the liberalisation measures adopted in the services sector. Some progress has been made in this respect: most of the measures that had been adopted before July 2012 have been followed up by the required enacting legislation, and some further relevant measures have been taken, but implementation on the ground is proving challenging and there remains scope for action. Besides, some backward steps in the liberalisation of professional services and local public services have been taken.

The reform of the regulated professions is an important step forward, but does not bring the liberalisation process to an end. The reform of the regulated professions removed some restrictions on fees and access, namely by abolishing minimum tariffs and making it easier for young people to start practising. However, there remain important barriers to access and 'reserves of activities', i.e. whereby the exercise of a service activity is limited to the holders of a specific professional qualification, as well as restrictions on shareholding in professional companies that might constrain their establishment, financing and growth. In addition, some professional orders still need to define rules to make the new provisions applicable. Finally, a reform of the legal profession adopted in December 2012 reversed some of the measures

[21] While acknowledging the possible relevance of introducing a national statutory minimum income scheme in Italy, the working group on socio-economic/European matters established in April 2013 by the President of the Italian Republic recognises that important budgetary constraints limit the feasibility of this avenue and suggests instead assessing the feasibility of the introduction of such a scheme in the context of a wider overhaul of social assistance benefits in Italy.

applicable to lawyers as part of the general reform of the professional orders. In particular, the reform introduces a new reserved activity for lawyers, establishes restrictive conditions for setting up professional law firms and de facto reintroduces minimum tariffs in the event of litigation, through reference to a tariff scale set and regularly updated by the Ministry of Justice. Careful monitoring of the implementing rules is needed to limit incompatibilities with the general thrust of the reform of the regulated professions.

The law on the organisation of non-regulated professions is positive but may entail some barriers to competition. A law adopted in January 2013 regulates the formation of associations on a voluntary basis for the exercise of non-regulated professions and allows self-certification of skills based on technical standards defined at national level, with a view to improving transparency and providing guarantees to clients. However, criteria for memberships and technical standards, if excessively restrictive, could result in obstacles to the entry of potential competitors, in particular with respect to professionals qualified in other Member States.

The process of liberalisation of local public services has come to a halt. As highlighted by the Italian Competition Authority, local public services in Italy remain, to a large extent, sheltered from competition, as they are managed through direct concession without public tendering. This contributes to fragmentation and inefficiencies in supply. The measures aimed at liberalising the provision of local public services were repealed by the Italian Constitutional Court in July 2012 on the ground of incompatibility with the results of the June 2011 referendum on the matter. The national reform programme argues that the current legal uncertainty on the rules governing local public services is the main obstacle to development and investment and calls for an urgent reform of the sector.

The liberalisation measures adopted so far are a step in the right direction but more remains to be done. As highlighted by the Italian Competition Authority, barriers and restrictions to competition, as well as sheltered market segments, are still present in other sectors, including in fuel distribution, insurance and postal services. According to the Commission calculations,[22] significant gains in GDP, of between 1.4% and 2.2%,[23] could be achieved with an additional reduction of obstacles to competition in the areas covered by the Services Directive.[24]

[22] http://ec.europa.eu/economy_finance/publications/economic_paper/2012/pdf/ecp_456_en.pdf
[23] Depending on the scenario: 2.2% corresponds to an ambitious scenario where Member States reduce the level of restrictions to that of the five best countries in the EU per sector – close to the full abolition of barriers – while 1.4% could be obtained under a moderately ambitious scenario.
[24] The end of 2011 is taken as the starting point, so this does not take into account the measures adopted by Italy in 2012.

Despite their potential for facilitating cross-border service provision, the points of single contact are not yet working optimally in Italy. The points of single contact established in Italy, in compliance with the Services Directive, to reduce administrative formalities for service provision through a one-stop-shop, are difficult to access for non-residents, due to lack of adequate information and the limited number of electronic procedures. According to the Commission calculations,[25] the establishment of points of single contact gave rise to a 0.1% GDP increase, and further action could generate additional gains, of 0.3% of GDP in the long term.

Network industries

Some important measures to improve competition and infrastructure capacity in network industries still need to be made operational. In 2012, the Council Recommendation contained one CSR recommending Italy to further improve market access and develop appropriate infrastructure capacity in network industries. Some progress has been made towards this CSR with relevant and ambitious measures, but their implementation has been delayed and there remains room for action.

In the transport sector, several competition-enhancing measures are still to be fully implemented, while scope for action remains. The repeal of the provisions on the liberalisation of local public services last July halted the plan to liberalise regional railway services, which meant to make these services subject to public tendering procedures, with a temporary exemption regime for existing direct concessions. Moreover, the new independent regulatory Transport Authority was not set up by the deadline of 31 May 2012. The Authority was expected to release a report, by June 2013, setting out plans for the unbundling of the transport operator from the infrastructure manager in the railway sector. With a view to improving the efficiency of the port system and facilitating the development of adequate infrastructure, Italy adopted measures to increase the financial autonomy of port authorities and simplify the administrative framework for approving strategic infrastructure projects. However, a comprehensive strategy for port management is still lacking, while fostering synergies and interconnections with the hinterland could also help to upgrade maritime transport.

Important steps have been taken to improve the functioning of the energy market and foster infrastructure investment. The ongoing unbundling of the incumbent operator from the network manager in the gas sector represents important progress towards addressing the 2012 CSR. If timely completed by the stipulated deadline of September 2013, it would be a milestone in enhancing competition, increasing transparency and improving market functioning in the gas sector, which is all the more crucial as electricity generation relies heavily on gas-fired power plants. Furthermore, important measures were adopted in August 2012 to streamline authorisation procedures for energy infrastructure, the implementation of which, though, is under the competence of the local authorities. By contrast, little progress was made to improve the quality of the water network, whose poor condition, particularly in the south of Italy, generates leakages and contributes to the pollution of surface and underground water, thus leading to a water productivity index well below the EU average.[26]

[25] http://ec.europa.eu/economy_finance/publications/economic_paper/2012/pdf/ecp_456_en.pdf
[26] The water productivity index measures the value of goods produced per metric cube of water used.

Moreover, there are still insufficient incentives to increase waste recycling and reduce landfill.

High energy prices continue to weigh on household budgets and company balance sheets. Despite the measures adopted, electricity and gas prices for households and industrial customers remain high, due to still insufficient competition in the gas sector and remaining infrastructure bottlenecks. Italy's heavy reliance on long-term contracts for gas imports and the limited development of the gas spot markets further contribute to high energy prices. In particular, the 2010 report by the European Regulators' Group for Electricity and Gas highlighted the low level of free pipeline import capacity in Italy, which indicates that gas transport routes are operating at near full capacity. The easing of the capacity constraint observed over the last two years seems to result from a depressed domestic demand for gas in the context of the recession, rather than by greater infrastructure capacity. The situation is similar as regards electricity, with significant north-south disparities, in terms of facilities and length of the lines.

The actions envisaged in the National Strategy for Energy could help to further enhance market functioning in the energy sector, improve infrastructure and develop renewable sources, in line with the Europe 2020 targets. A National Strategy for Energy was approved in March 2013 and now needs to be translated into concrete actions. It intends to reduce costs, ensure security of supply, promote industrial development in the energy sector and encourage the development of renewable energy sources, with a view to meeting the Europe 2020 environmental targets and fostering energy efficiency. In particular, the strategy sets ambitious objectives for reducing greenhouse gas emissions. From 2005 to 2011, greenhouse gas emissions fell by 13% in sectors not covered by the Emissions Trading Scheme (ETS), hence reaching the target for 2020. Nevertheless, the latest available Italian projections point to a reversal of this positive trend in the coming years.

Limited market opening and infrastructure shortcomings also affect telecommunications. Although noticeable progress has been achieved since the late 1990s in opening up the telecommunication sector to competition, some restrictions are still in place. The Italian Competition Authority advocates better use of the spectrum, while also suggesting the unbundling of the network owner from the provider of telecommunication services as a potential avenue for action. It also highlights infrastructure weaknesses as one of the causes of the low broadband penetration in Italy.

If properly implemented, the reform of rules on 'golden shares' could help to improve market functioning in a range of network sectors. Last year, a revision of the rules governing 'golden shares' – particularly in energy, transport and telecommunications – was initiated for the purpose of aligning them with European legislation. The envisaged new rules stipulate the automatic repeal of any existing 'golden share' clause in state-owned companies' statutes, while maintaining some special powers. However, the required legislation still needs to be adopted before the reform can produce benefits.

Research and innovation

Limited progress has been made in the area of research and innovation. The 2012 Council Recommendation called for easier access to finance for firms as a key driver to stimulate innovation. The 2013-15 budget law introduces a tax credit to promote research and development (R&D) within firms. Measures to encourage the creation and development of innovative start-ups were taken[27], but the focus on innovative start-ups limits the number of firms concerned. Moreover, a Fund for Sustainable Growth was set up to promote R&D and innovation and the internationalisation of firms. Although relevant and credible, the level of ambition of these measures appears insufficient to improve Italy's performance in terms of innovation[28], reduce the gap with the EU average in terms of R&D intensity and meet the Europe 2020 target – with 1.25% of GDP invested in R&D in 2011, Italy is still far from the objective of 1.53% of GDP to be achieved by 2020. The framework for project financing remains cumbersome for companies, while measures to facilitate equity investment and venture capital, such as the introduction of the ACE, are limited in scope. Ultimately, fostering innovation also crucially depends on enhancing the skill level in the labour force.

3.5. Modernisation of public administration

Enhancing the efficiency of the public administration remains a challenge. An effective and efficient public administration contributes to the quality and functioning of the business environment and favours absorption of structural funds. Despite the adoption of several measures aimed at reducing the administrative burden and improving transparency and efficiency, there remains large scope to improve the quality of the Italian public administration. In particular, heavy inefficiencies in civil justice result in lengthy proceedings and a large backlog of cases, as shown by the Commission's EU justice scoreboard.[29]

Business environment

The significant measures aimed at improving the quality of the business environment will start bearing fruit only when fully implemented. In 2012, the Council Recommendation for Italy advocated further administrative simplification and increased efficiency of civil justice. Some progress has been made towards addressing this CSR. However, some relevant measures aimed at administrative simplification are still in the pipeline, while some of the adopted ones have not yet been implemented. This is also the case for some of the relevant and ambitious measures taken in the area of civil justice, where there have also been some backward steps.

In line with the 2012 CSR, the administrative simplification effort has been pursued. Taking forward the steps taken at the beginning of 2012, a draft law on simplification was adopted by the government in October 2012 and envisages, inter alia, the setting-up of a simplified framework for infrastructure investment. Some of the measures aimed at facilitating entrepreneurship have started to produce an impact: more than 5 000 simplified limited liability companies for entrepreneurs under 35 years of age and 2 000 limited liability companies with reduced capital for entrepreneurs over 35 years of age have indeed been created since they were launched in August and June 2012 respectively. This was further enriched with steps towards the completion of the Digital Agenda, through increased

[27] Innovative start-ups are defined as companies that invest more than 30% of their production costs in research or more than 30% of whose workforce are researchers or PhDs or that have been assigned industrial property rights.
[28] Italy still ranks as a moderate innovator in the Commission's 2013 Innovation Union Scoreboard.
[29] COM(2013) 160 final.

computerisation of procedures, more e-government services and the establishment of the Agency for Digital Italy, which is, however, not yet fully operational.

Some obstacles to reaping the benefits of administrative simplification remain, mainly in the form of gaps in implementation. The screening of ex ante authorisation schemes for starting a business and subsequent repeal and substitution with ex post controls of unnecessary ones, as foreseen in earlier legislation, have so far not been translated into practice. Moreover, the draft law on simplification from October 2012 has not been approved by the Italian Parliament. This results in a still heavy administrative burden weighing on businesses. In particular, despite the measures adopted in this area, Italy's ranking as regards the ease of starting a business worsened significantly over the last year.[30] Moreover, despite the availability of e-government services, citizens and small firms continue to make very low – below EU average – use of them, with very limited progress since 2010. This can be explained by the overall low level of information and communication technology skills and low public awareness of the availability of such services.

Action was taken to promote the internationalisation of businesses and attract foreign investment. Action in this field notably builds on the creation of the Italy Desk, which consists of a one-stop access point for foreign investors on administrative requirements related to investment projects. If properly deployed and taken up by firms and investors, this measure could in turn favour a more business-friendly environment.

Action to enhance the efficiency of the judicial system has been determined, yet challenges remain. In line with the 2012 CSR calling for the implementation of the planned reorganisation of courts, enacting legislation adopted in August 2012 started a crucial revision of the territorial distribution of judicial offices, aimed at rationalising and enhancing the efficiency of Italy's judicial geography. Rigorous implementation by the September 2013 deadline will be fundamental to allow this reform to deploy its benefits. This key measure was complemented by action to reduce the length and costs of proceedings and curb the high level of litigation, principally by fostering the specialisation of courts – the 21 courts specialised in company law became operational last September – setting up accelerated procedures and introducing disincentives to the use of the judicial service. Initiatives to modernise and digitalise the judicial service are also helping to improve efficiency. Given the high level of litigation in Italy, out-of-court dispute settlements carry a strong potential for reducing the length of civil proceedings and alleviating judges' and courts' workload. This was underlined in the 2012 CSR and in the national reform programme. However, in October 2012 the Italian Constitutional Court rejected provisions that make mediation compulsory in a number of civil fields.

The anticorruption law represents an important and long-awaited step in the right direction, but some issues remain unaddressed. The pervasiveness of corruption generates heavy costs for Italy's productive system, estimated at EUR 60 billion by the Italian Court of Auditors in 2012, and erodes citizens' trust in the government and the institutions. By establishing a dedicated authority, introducing new offences and increasing transparency

[30] As evidenced by the 2013 edition of Doing Business by the World Bank, where Italy ranks 84th (out of 185 economies) as regards the framework for starting a business (in terms of time, cost and the number of procedures involved in creating a company), against 76th in 2012.

obligations in administrations, the anticorruption law approved in November 2012 represents a positive step towards a more favourable business environment in Italy. Nevertheless, not only does the law still require implementing acts but it also does not tackle some critical issues. Namely, the short prescription terms in the statute of limitations is depicted by the Group of States against Corruption (GRECO) as a major weakness of the Italian criminal system. To embed integrity in the public administration, additional improvements in the prosecution of some common offences against the public administration, such as accounting fraud and 'self-laundering', are also important.

The institutional framework for handling state aid displays some weaknesses. Unlike other Member States, Italy coordinates the recovery of illegal aid and infringement proceedings centrally, but the central government has no power to coordinate notifications, legislation and data collection. Additional gaps compared with other Member States concern the lack of control mechanisms and knowledge about aid granted, and weaknesses in the recovery of illegal aid, as underlined by the Italian Competition Authority. Italy has adopted a new law addressing some of these issues, but its effects remain to be seen.

The coordination between the various layers of government needs to be clarified. The implementation of the adopted measures and the appropriate application of EU legislation has often been hampered by insufficient coordination between the central and local levels of government and lack of clarity on the division of responsibilities across them. For instance, this has undermined the correct implementation of the Services Directive, especially in the tourism and retail sectors. Building on the 2001 reform of Title V of the Italian Constitution, which governs the allocation of regulatory and spending powers across government levels, a constitutional amendment bill was adopted last October, with the ambition of further revising this chapter of the Constitution. In particular, the constitutional amendment bill brings some competences[31] back to the central level and strives to reduce conflicts over the division of responsibilities. This reform has not yet been approved by the Italian Parliament.

Late payment of commercial credits

Italy's transposition of the EU directive on late payments in commercial transactions is a positive step in improving relations between the public administration and service providers. Italy has the second worst record in the EU for delayed payment of commercial credits, in particular by the public sector. Timely implementation of Directive 2011/7/EU, which applies to contracts signed from 1 January 2013 onwards, is expected to reduce payment times, both among private commercial partners and between private suppliers and the government, and will help to avoid the further accumulation of commercial debt by the public administration. The accumulated stock of commercial debt owed by the general government sector is estimated to be sizeable, at around 5.8% of GDP in 2011, although it also covers commercial credits that are still within contractual payment time limits.

The government adopted a plan to accelerate payment of the substantial stock of commercial debt, notably by regional and local authorities, over 2013-14. The plan increases the cash resources of subnational governments, which owe most of the commercial

[31] Among these competences are coordination of public finances and the tax system, the main transport networks, education, foreign trade, and the national production, transport and distribution of energy.

debt arrears, and is thus expected to be more effective than the measures taken in 2012 to promote the certification of credit claims and use them as guarantee to obtain bank credit. It is important to ensure that debt is effectively paid to creditors to improve the liquidity of firms and that adequate safeguards against moral hazard by the administrations responsible for the debt overhang are put in place.

Structural funds

The efficiency of Italy's response to enhance the absorption of structural funds contrasts with the lack of initiative to improve the management of funds. In 2012, the Council Recommendation highlighted the importance of improving the absorption and management of structural funds particularly in the south of Italy, as part of the effort to enhance the efficiency of public expenditure. Some progress has been made in this field. The implementation of the Cohesion Action Plan is on track and led to an increase in the absorption of funds by 10 percentage points in 12 months, from 21% to 31%. However Italy has not yet taken structural and long-lasting measures to address the deficiencies in the management of funds in the southern regions, as shown by the experience of the dedicated task forces in Sicily and Campania, notably as regards project conception, preparation and implementation capacity, and the prevention and early detection of irregularities in the use of EU funding. In view of the next programming period and as underlined in the Commission's position paper on the development of partnership agreements and programmes in Italy over 2014-20, the persistence of these problems is a major source of concern as it inhibits the regular flow of EU assistance to Italy's less developed regions and their chances of developing.

4. OVERVIEW TABLE

2012 commitments	Summary assessment
Country-specific recommendations (CSRs)	
CSR 1: Implement the budgetary strategy as planned, and ensure that the excessive deficit is corrected in 2012. Ensure the planned structural primary surpluses so as to put the debt-to-GDP ratio on a declining path by 2013. Ensure adequate progress towards the MTO, while meeting the expenditure benchmark and making sufficient progress towards compliance with the debt reduction benchmark.	**Some progress has been made towards addressing this CSR**. On 10 April, the government presented the new Economic and Financial Planning Document (DEF) for 2013-17, with a worsened economic and budgetary outlook. The deficit reached 3.0% of GDP in 2012 (EDP deadline set by the Council). The government deficit is planned to decrease slightly to 2.9% of GDP in 2013, to allow for the liquidation of commercial debt of around 0.5% of GDP, and to fall to 1.8% in 2014, 1.5% in 2015, 0.9% in 2016 and 0.4% in 2017. The deficit targets as from 2015 will require some additional consolidation measures. Also due to the payment of commercial debt, the debt is projected to rise to 130.4% of GDP this year and fall steadily thereafter, to 117.3% in 2017. Consolidation measures taken so far are ambitious but the achievement of fiscal commitments could be at stake, not only due to the fragile economic outlook but also because of possible relaxation of the fiscal stance. Italy must pursue the fiscal consolidation effort in a growth-friendly manner and in full consistency with the requirements of the strengthened Stability and Growth Pact. In particular, Italy should ensure the planned high structural primary surpluses, which are key to putting the debt-to-GDP ratio on a steadily declining path.
CSR 2: Ensure that the specification in the implementing legislation of the key features of the balanced budget rule set out in the Constitution, including appropriate coordination across levels of government, is consistent with the EU framework. Pursue a durable improvement of the efficiency and quality of public expenditure through the planned spending review and the implementation of the 2011 Cohesion Action Plan leading to improving the absorption and management of EU funds, in particular in the South of Italy.	**The part of the CSR dedicated to the balanced budget rule has been fully addressed, while some progress has been made towards addressing the recommendation on public expenditure and structural funds**. In line with the CSR, the secondary legislation related to the introduction of a balanced budget rule in the Italian Constitution was adopted in December 2012, in broad consistency with the EU strengthened fiscal framework. A spending review law was adopted last August and complemented by measures to cut the costs of elected bodies and further expenditure reshuffling provisions in the December 2012 budget law for 2013-15. However, some of the measures provided for in the spending review have not yet been adopted and/or implemented. As regards the implementation of the Cohesion Action Plan, while the part of the recommendation regarding absorption has seen positive developments, the management issue, especially in the south of Italy, remains unaddressed.

CSR 3: Take further action to address youth unemployment, including by improving the labour market relevance of education and facilitating transition to work, also through incentives for business start-ups and for hiring employees. Enforce nation-wide recognition of skills and qualifications to promote labour mobility. Take measures to reduce tertiary education dropout rates and fight early school leaving.	**Some progress has been made towards addressing this CSR**. Some measures have been taken to tackle early school leaving and tertiary education dropout rates and to adapt the supply of high-level skills to labour market needs, yet they are still insufficient. Nation-wide recognition of skills and qualifications has been implemented through the national system for the certification of skills. Several measures have been introduced to favour the creation of innovative start-ups and the recruitment of high-skilled young people but their scope is limited and some of them still lack implementing legislation.
CSR 4: Adopt the labour market reform as a priority to tackle the segmentation of the labour market and establish an integrated unemployment benefit scheme. Take further action to incentivise labour market participation of women, in particular through the provision of childcare and elderly care. Monitor and if needed reinforce the implementation of the new wage setting framework in order to contribute to the alignment of wage growth and productivity at sector and company level.	**Some progress has been made towards addressing this CSR**. In line with the CSR, an ambitious reform of the labour market was adopted in June 2012, but still requires the adoption of implementing decrees for some of its provisions. Although measures were adopted to encourage female participation in the labour market, their scope remains narrow. Furthermore, the measures regarding the provision of childcare and elderly care remain at a general stage and have limited scope. On wage bargaining, an agreement was signed by the social partners – with the exception of the CGIL trade union – in November 2012. It promotes decentralised bargaining and acknowledges the need to link wages not only to inflation but also to the economic and competitive conditions of the country of the sector concerned. This agreement is a promising step to contribute to a better alignment of wages to productivity developments and sustain competitiveness. However, since it sets out only guidelines, requiring further agreements by social partners for the practical implementation, its effectiveness remains to be seen. The government is supporting the agreement with tax rebates on productivity-related pay, recently enacted with decree law endorsed by social partners.
CSR 5: Pursue the fight against tax evasion. Pursue the shadow economy and undeclared work, for instance by stepping up checks and controls. Take measures to reduce the scope of tax exemptions, allowances and reduced VAT rates and simplify the tax code. Take further action to shift the tax burden away from capital and labour to property and consumption as well as environment.	**Limited progress has been made towards addressing this CSR**. After the ambitious measures adopted over 2010-11, progress towards further shifting the tax burden from labour and capital to property and consumption has been limited. Relevant measures were contained in a draft enabling law for reforming the tax system to improve tax compliance, simplify the tax system and enhance its efficiency – notably by bringing cadastral values closer to market values for property taxation – but remained at the stage of projects since the law has not been adopted by the Italian Parliament. Italy has implemented targeted measures to enhance the tools available to the tax administration to efficiently tackle tax evasion. Their impact will depend on the administration's capacity to make use of these tools. The shadow

	economy and undeclared work remain pressing challenges.
CSR 6: Implement the adopted liberalisation and simplification measures in the services sector. Take further measures to improve market access in network industries, as well as infrastructure capacity and interconnections. Simplify further the regulatory framework for businesses and enhance administrative capacity. Improve access to financial instruments, in particular equity, to finance growing businesses and innovation. Implement the planned reorganisation of the civil justice system, and promote the use of alternative dispute settlement mechanisms.	**Some progress has been made towards addressing this CSR**. Important measures have been adopted to improve market functioning in services – in particular professional services – and network industries – notably through the ongoing unbundling in the gas sector. Yet, risks can be identified as regards the proper implementation of some of them (the reform of the legal profession potentially conflicts with the general reform of the regulated professions; the Transport Authority has not yet been set up; enacting decrees are still needed for the reform of the discipline governing 'golden shares'), the liberalisation of local public services halted, and areas for further action remain, for instance in fuel distribution, insurance, and postal services. Besides, only limited progress has been registered regarding the improvement of infrastructure in the electricity and gas sectors. Work on administrative simplification has continued, together with greater digitalisation of public services, with a view to improving the efficiency of the public administration and the business environment. However, the draft law on simplification expected to supplement this effort has not been approved by the Italian Parliament. Several tools were introduced to ease firms' access to finance and improve research and innovation, but remain limited in scope. As regards the judicial system, the enacted revision of the judicial geography is a key step in order to optimise the organisation of the courts. It was complemented by measures to accelerate court proceedings, foster the specialisation among courts and judges, reduce litigation and modernise the judicial service. However, the introduction of compulsory mediation in a number of civil matters was repealed by the Italian Constitutional Court.
Europe 2020 (national targets and progress)	
Employment rate target: 67-69 %	The employment rate was 61.2% in 2011 and 61.0% in 2012. No progress has been achieved towards meeting the target.
R&D target: 1.53 % of GDP	Gross domestic expenditure on R&D was 1.26% of GDP in 2010 and 1.25% of GDP in 2011. No progress has been achieved towards meeting the target.
Greenhouse gas (GHG) emissions target: -13 % (compared with 2005 emissions); ETS emissions are not covered by this national target	The change in non-ETS greenhouse gas emissions between 2005 and 2011 was -13%. According to the latest available projections, the total change over 2005-20 will be -9% and the target would thus be missed. So far, substantial progress has been achieved towards meeting the target, but it may be reversed.

Renewable energy target: 17 % Share of renewable energy in the transport sector: 10 %	The share of total renewable energy in gross final energy consumption was 11.5% in 2011 and 4.7% in the transport sector. Some progress has been achieved towards meeting the target.
Indicative national energy efficiency target: 20 Mtoe primary energy reduction by 2020 and 15 Mtoe final energy reduction by 2020.	Italy has set an indicative national energy efficiency target in accordance with Articles 3 and 24 of the Energy Efficiency Directive (2012/27/EU). The savings achieved amounted to 5.12 Mtoe in 2011. Some progress has been achieved towards meeting the target.
Early school leaving target: 15-16 %	The early school leaving rate (the percentage of the population aged 18-24 with at most lower secondary education and not in further education or training) was 18.2% in 2011 and 17.6% in 2012. Some progress has been achieved towards meeting the target.
Tertiary education target: 26-27 %	The tertiary educational attainment rate was 20.3% in 2011 and 21.7% in 2012. Some progress has been achieved towards meeting the target.
Target to reduce the share of the population at risk of poverty or social exclusion, in number of persons: - 2 200 000	People at risk of poverty or social exclusion (in thousand of persons): 14 757 000 in 2010 and 17 126 000 in 2011. No progress has been achieved towards meeting the target.

5. ANNEX

Table I. Macroeconomic indicators

	1995-1999	2000-2004	2005-2009	2010	2011	2012	2013	2014
Core indicators								
GDP growth rate	1.8	1.5	3.0	1.7	0.4	-2.4	-1.3	0.7
Output gap [1]	0.4	1.5	0.9	-1.8	-1.6	-3.1	-4.0	-3.2
HICP (annual % change)	3.0	2.5	2.1	1.6	2.9	3.3	1.6	1.5
Domestic demand (annual % change) [2]	2.2	1.6	-0.2	2.1	-1.0	-5.3	-2.5	0.6
Unemployment rate (% of labour force) [3]	11.2	8.8	7.0	8.4	8.4	10.7	11.8	12.2
Gross fixed capital formation (% of GDP)	19.3	20.6	20.8	19.4	19.4	18.2	17.8	18.2
Gross national saving (% of GDP)	21.9	20.7	19.4	16.5	16.4	17.1	17.8	18.4
General Government (% of GDP)								
Net lending (+) or net borrowing (-)	**-4.4**	**-2.8**	**-3.5**	**-4.5**	**-3.8**	**-3.0**	**-2.9**	**-2.5**
Gross debt	**117.2**	**105.8**	**107.6**	**119.3**	**120.8**	**127.0**	**131.4**	**132.2**
Net financial assets	**-102.5**	**-94.0**	**-92.4**	**-99.5**	**-94.2**	**n.a**	**n.a**	**n.a**
Total revenue	45.8	44.4	45.4	46.1	46.2	47.7	48.2	47.7
Total expenditure	50.2	47.2	48.9	50.5	50.0	50.7	51.1	50.2
of which: Interest	9.3	5.6	4.8	4.6	5.0	5.5	5.3	5.5
Corporations (% of GDP)								
Net lending (+) or net borrowing (-)	**-0.3**	**-1.0**	**-1.4**	**-0.5**	**-0.4**	**1.4**	**2.5**	**2.0**
Net financial assets; non-financial corporations	**-83.9**	**-107.1**	**-126.4**	**-129.4**	**-119.8**	**n.a**	**n.a**	**n.a**
Net financial assets; financial corporations	**-2.7**	**-13.1**	**0.8**	**23.8**	**27.4**	**n.a**	**n.a**	**n.a**
Gross capital formation	10.4	11.4	11.1	10.6	10.3	8.9	8.1	8.9
Gross operating surplus	23.9	23.9	22.1	21.1	20.6	19.8	19.5	19.8
Households and NPISH (% of GDP)								
Net lending (+) or net borrowing (-)	**7.1**	**3.7**	**3.3**	**1.3**	**1.0**	**1.1**	**1.4**	**1.5**
Net financial assets	**186.0**	**204.5**	**195.2**	**180.6**	**168.1**	**n.a**	**n.a**	**n.a**
Gross wages and salaries	28.8	28.9	30.3	31.1	31.2	31.4	31.4	31.2
Net property income	18.9	15.7	14.4	12.0	11.8	11.4	10.7	10.5
Current transfers received	20.7	20.7	21.9	24.0	23.9	24.4	25.0	25.2
Gross saving	14.2	11.1	10.8	8.6	8.2	7.9	8.0	8.2
Rest of the world (% of GDP)								
Net lending (+) or net borrowing (-)	**2.4**	**-0.1**	**-1.6**	**-3.5**	**-3.1**	**-0.4**	**1.1**	**1.3**
Net financial assets	**5.2**	**11.7**	**25.9**	**30.3**	**25.0**	**n.a**	**n.a**	**n.a**
Net exports of goods and services	3.5	0.9	-0.5	-1.9	-1.5	1.2	2.7	3.0
Net primary income from the rest of the world	-1.0	-0.6	-0.3	-0.5	-0.6	-0.7	-0.7	-0.8
Net capital transactions	0.2	0.1	0.1	0.0	0.0	0.1	0.2	0.2
Tradable sector	47.5	45.2	42.4	41.0	40.8	40.4	n.a	n.a
Non tradable sector	42.3	44.7	47.3	48.6	48.8	49.1	n.a	n.a
of which: Building and construction sector	4.7	5.0	5.7	5.4	5.4	5.3	n.a	n.a
Real effective exchange rate (index, 2000=100)	92.4	91.7	103.1	104.0	104.3	102.7	104.6	104.1
Terms of trade goods and services (index, 2000=100)	103.5	101.7	98.4	97.6	94.4	93.4	94.5	94.9
Market performance of exports (index, 2000=100)	133.2	110.4	96.8	90.9	92.0	93.9	94.3	93.6

Notes:

[1] The output gap constitutes the gap between the actual and potential gross domestic product at 2005 market prices.

[2] The indicator on domestic demand includes stocks.

[3] Unemployed persons are all persons who were not employed, had actively sought work and were ready to begin working immediately or within two weeks. The labour force is the total number of people employed and unemployed. The unemployment rate covers the age group 15-74.

Source :

Commission services' 2013 spring forecasts (COM); Stability programme (SP).

Table II. Comparison of macroeconomic developments and forecasts

	2012		2013		2014		2015	2016	2017
	COM	SP	COM	SP	COM	SP	SP	SP	SP
Real GDP (% change)	-2.4	-2.4	-1.3	-1.3	0.7	1.3	1.5	1.3	1.4
Private consumption (% change)	-4.2	-4.3	-2.0	-1.7	0.4	1.4	1.1	1.1	1.2
Gross fixed capital formation (% change)	-8.0	-8.0	-3.5	-2.6	2.5	4.1	3.2	2.6	2.4
Exports of goods and services (% change)	2.3	2.3	1.6	2.2	3.8	3.3	4.1	4.0	3.9
Imports of goods and services (% change)	-7.7	-7.7	-2.2	-0.3	3.8	4.7	4.4	4.1	3.8
Contributions to real GDP growth:									
- Final domestic demand	-4.7	-4.8	-2.2	-1.9	0.6	1.4	1.3	1.2	1.2
- Change in inventories	-0.6	-0.6	-0.3	-0.1	0.0	0.1	0.1	0.0	0.0
- Net exports	3.0	3.0	1.1	0.7	0.1	-0.2	0.1	0.1	0.1
Output gap[1]	-3.1	-3.2	-4.0	-4.2	-3.2	-3.1	-2.0	-1.2	-0.4
Employment (% change)	-0.3	-0.3	-0.8	-0.4	0.0	0.4	0.7	0.6	0.8
Unemployment rate (%)	10.7	10.7	11.8	11.6	12.2	11.8	11.6	11.4	10.9
Labour productivity (% change)	-1.3	-1.3	-0.2	-1.0	0.4	0.7	0.7	0.6	0.5
HICP inflation (%)	3.3	3.3	1.6	2.0	1.5	2.0	1.9	1.8	1.8
GDP deflator (% change)	1.6	1.6	1.5	1.8	1.5	1.9	1.8	1.8	1.8
Comp. of employees (per head, % change)	1.0	1.0	1.2	1.0	1.1	1.2	1.5	1.6	1.6
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	-0.4	-0.4	1.1	0.2	1.3	-0.2	-0.1	-0.1	0.0

Note:

[1] In percent of potential GDP, with potential GDP growth recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

Source :

Commission services' 2013 spring forecasts (COM); Stability programme (SP).

Table III. Composition of the budgetary adjustment

(% of GDP)	2012	2013		2014		2015	2016	2017	Change: 2012-2017
	COM	COM	SP	COM[1]	SP	SP	SP	SP	SP
Revenue[6]	**47.7**	**48.2**	**48.2**	**47.7**	**48.0**	**47.7**	**47.5**	**47.3**	**-0.4**
of which:									
- Taxes on production and imports	14.9	15.0	15.3	14.9	15.4	15.5	15.4	15.3	0.4
- Current taxes on income, wealth, etc.	15.1	15.2	15.0	15.0	15.0	14.7	14.7	14.8	-0.3
- Social contributions	13.8	14.0	14.0	13.9	13.9	13.8	13.7	13.6	-0.2
- Other (residual)	3.8	3.9	3.9	3.9	3.7	3.7	3.7	3.6	-0.2
Expenditure[6]	**50.7**	**51.1**	**51.1**	**50.2**	**49.8**	**49.4**	**48.8**	**48.3**	**-2.4**
of which:									
- Primary expenditure	45.2	45.7	45.8	44.6	44.2	43.6	42.8	42.2	-3.0
of which:									
Compensation of employees	10.6	10.4	10.4	10.1	10.0	9.8	9.5	9.2	-1.4
Intermediate consumption	5.7	5.5	5.4	5.4	5.3	5.2	5.2	5.1	-0.5
Social payments	22.6	23.1	23.1	23.2	23.0	22.9	22.7	22.6	0.0
Subsidies	1.0	1.0	1.0	1.0	0.9	0.9	0.8	0.8	-0.2
Gross fixed capital formation	1.9	2.1	1.8	1.6	1.7	1.7	1.7	1.6	-0.3
Other (residual)	3.4	3.7	4.1	3.4	3.2	3.2	3.0	2.9	-0.5
- Interest expenditure	5.5	5.3	5.3	5.5	5.6	5.8	6.0	6.1	0.6
General government balance (GGB)	**-3.0**	**-2.9**	**-2.9**	**-2.5**	**-1.8**	**-1.5**	**-0.9**	**-0.4**	**2.6**
Primary balance	**2.5**	**2.4**	**2.4**	**3.1**	**3.8**	**4.3**	**5.1**	**5.7**	**3.2**
One-off and other temporary measures	0.1	-0.2	-0.2	-0.1	-0.1	-0.1	0.0	0.0	-0.1
GGB excl. one-offs	**-3.1**	**-2.7**	**-2.7**	**-2.4**	**-1.7**	**-1.4**	**-0.9**	**-0.4**	**2.7**
Output gap[2]	-3.1	-4.0	-4.2	-3.2	-3.1	-2.0	-1.2	-0.4	2.7
Cyclically-adjusted balance[2]	-1.3	-0.7	-0.6	-0.7	-0.1	-0.4	-0.2	-0.2	1.2
Structural balance (SB)[3]	**-1.4**	**-0.5**	**-0.4**	**-0.7**	**0.0**	**-0.3**	**-0.2**	**-0.2**	**1.3**
Change in SB	*2.2*	*0.9*	*1.0*	*-0.2*	*0.4*	*-0.3*	*0.1*	*0.1*	-
Two year average change in SB	*1.1*	*1.6*	*1.6*	*0.4*	*0.7*	*0.0*	*-0.1*	*0.1*	-
Structural primary balance[3]	4.1	4.8	4.9	4.9	5.6	5.5	5.8	5.9	1.8
Change in structural primary balance		*0.7*	*0.8*	*0.0*	*0.7*	*-0.1*	*0.3*	*0.2*	-
Expenditure benchmark									
Applicable reference rate[4]	-0.81	-0.81	-0.81	-1.07	-1.07	0.04	-1.07	0.04	-
Deviation[5] (% GDP)	-3.4	-0.6	-0.3	0.0	-0.4	0.0	0.1	0.1	-
Two-year average deviation (% GDP)	-1.9	-2.0	-1.4	-0.3	-0.4	-0.2	0.1	0.1	-

Notes:

[1]On a no-policy-change basis.

[2]Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

[3]Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.

[4] Reference medium-term rate of potential GDP growth. The (standard) reference rate applies from year t+1, if the country has reached its MTO in year t. A lower rate applies as long as the country is adjusting towards its MTO, including in year t.The reference rates applicable to 2014 onwards have been updated in 2013.

[5] Deviation of the growth rate of public expenditure net of discretionary revenue measures and revenue increases mandated by law from the applicable reference rate. The expenditure aggregate used for the expenditure benchmark is obtained following the commonly agreed methodology. A positive sign implies that expenditure growth exceeds the applicable reference rate.

[6]Revenue and expenditure (total and sub-components) as from 2015 provided in the programme according to unchanged legislation

Source :

Stability programme (SP); Commission services' 2013 spring forecasts (COM); Commission services' calculations.

Table IV. Debt dynamics

(% of GDP)	Average 2007-2011	2012	2013		2014		2015	2016	2017
			COM	SP	COM	SP	SP	SP	SP
Gross debt ratio[1]	**113.2**	**127.0**	**131.4**	**130.4**	**132.2**	**129.0**	**125.5**	**121.4**	**117.3**
Change in the ratio	2.9	6.2	4.4	3.4	0.8	-1.4	-3.5	-4.1	-4.1
Contributions [2] :									
1. Primary balance	**-1.3**	**-2.5**	**-2.4**	**-2.4**	**-3.1**	**-3.8**	**-4.3**	**-5.1**	**-5.7**
2. "Snow-ball" effect	**3.6**	**6.5**	**5.1**	**4.6**	**2.6**	**1.6**	**1.7**	**2.1**	**2.4**
Of which:									
Interest expenditure	4.9	5.5	5.3	5.3	5.5	5.6	5.8	6.0	6.1
Growth effect	0.6	2.9	1.7	1.6	-0.9	-1.6	-1.9	-1.6	-1.6
Inflation effect	-1.9	-2.0	-1.9	-2.3	-2.0	-2.4	-2.2	-2.3	-2.1
3. Stock-flow adjustment	**0.5**	**2.1**	**1.7**	**1.1**	**1.2**	**0.8**	**-0.9**	**-1.1**	**-0.7**
Of which:									
Cash/accruals diff.	0.0	0.1	0.0	0.0	0.2	0.2	-0.4	-0.5	-0.1
Acc. financial assets	0.5	2.0	1.7	1.1	1.0	0.6	-0.5	-0.6	-0.6
Privatisation	*-0.1*	*-0.5*	*0.0*	*-1.0*	*0.0*	*-1.0*	*-1.0*	*-1.0*	*-1.0*
Val. effect & residual	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

	2012	2013		2014		2015	2016	2017
		COM / SP[3]	SP[4]	COM / SP[3]	SP[4]	SP	SP	SP
Gap to the debt benchmark[5,6]	n.r.	n.r.	n.r.	n.r.	n.r.	-1.6	-0.7	-1.6
Structural adjustment[7]	n.r.	0.9	0.9	0.4	0.4	n.r.	n.r.	n.r.
To be compared to:								
Required adjustment[8]	n.r.	-0.1	0.0	-0.6	-0.5	n.r.	n.r.	n.r.

Notes:

[1]End of period.

[2]The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

[3] Assessment of the consolidation path set in SP assuming growth follows the COM forecasts.

[4]Assessment of the consolidation path set in the SP assuming growth follows the SP projections.

[5]Not relevant for Member Sates that were subject to an EDP procedure in November 2011 and for a period of three years following the correction of the excessive deficit.

[6]Shows the difference between the debt-to-GDP ratio and the debt benchmark. If positive, projected gross debt-to-GDP ratio does not comply with the debt reduction benchmark.

[7]Applicable only during the transition period of three years from the correction of the excessive deficit for EDP that were ongoing in November 2011.

[8]Defines the remaining annual structural adjustment over the transition period which ensures that – if followed – Italy will comply with the debt reduction benchmark at the end of the transition period, assuming that COM (SP) budgetary projections for the previous years are achieved.

Source :
Stability programme (SP); Commission services' spring 2013 forecasts (COM); Commission services' calculations.

Table V. Sustainability indicators

	IT		EU27	
	No-policy change scenario	**Programme (SCP) scenario**	**No-policy change scenario**	**Programme (SCP) scenario**
S2	-2.1	-3.2	3.0	1.3
of which:				
Initial budgetary position (IBP)	-2.8	-4.2	0.8	-0.9
Long-term cost of ageing (CoA)	0.7	0.9	2.2	2.2
of which:				
Pensions	-0.3	-0.1	1.0	1.1
Health care	0.6	0.6	0.9	0.8
Long-term care	0.6	0.6	0.6	0.6
Others	-0.2	-0.2	-0.4	-0.3
S1 (required adjustment)*	1.1	-0.3	2.2	0.5
of which:				
Initial budgetary position (IBP)	-2.6	-4.0	0.0	-1.8
Debt requirement (DR)	4.1	4.1	1.9	1.9
Long-term cost of ageing (CoA)	-0.3	-0.4	0.3	0.4
S0 (risk for fiscal stress)**	0.28		:	
Debt, % of GDP (2012)	127.0		87.0	
Age-related expenditure, % of GDP (2012)	28.1		25.8	

Note:
The 'No-policy change' scenario depicts the sustainability gap under the assumption that the budgetary position evolves according to the Commissions' spring 2013 forecast until 2014. The 'Programme (SCP)' scenario depicts the sustainability gap under the assumption that the budgetary plans in the programme are fully implemented.
* The required adjustment of the primary balance until 2020 to reach a public debt of 60% of GDP by 2030.
** The critical threshold for the S0 indicator is 0.44.

Source :
Commission services; 2013 stability programme.

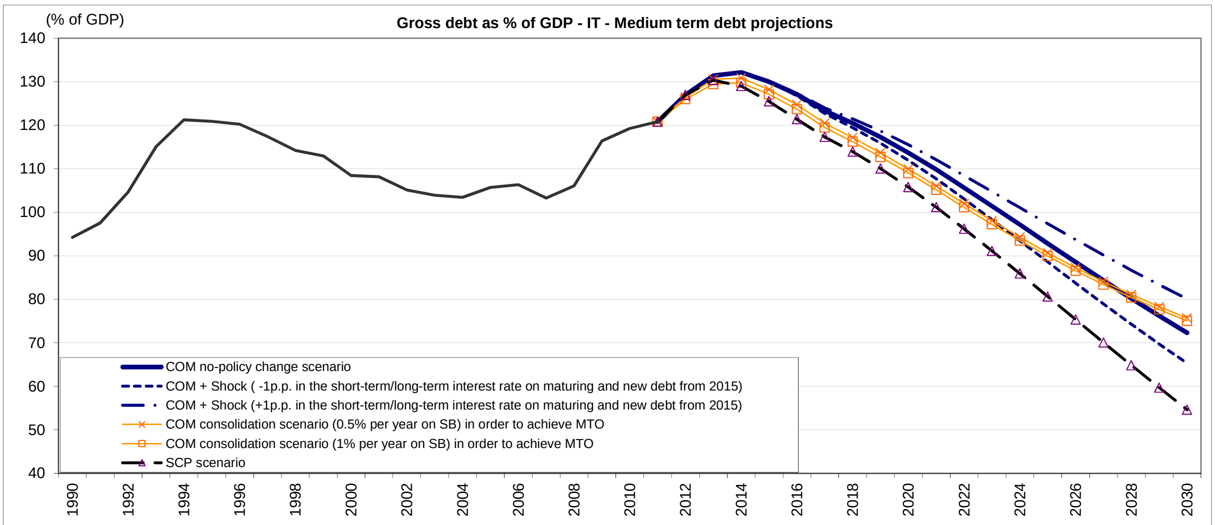

Table VI. Taxation indicators

	2002	2006	2008	2009	2010	2011
Total tax revenues (incl. actual compulsory social contributions, % of GDP)	40.5	41.7	42.7	43.0	42.5	42.5
Breakdown by economic function (% of GDP)[1]						
Consumption	10.4	10.6	10.1	10.1	10.6	10.8
of which:						
- VAT	6.2	6.2	5.9	5.7	6.3	6.2
- excise duties on tobacco and alcohol	0.7	0.8	0.8	0.8	0.8	0.8
- energy	2.3	2.2	1.9	2.1	2.0	2.1
- other (residual)	1.3	1.4	1.5	1.6	1.5	1.6
Labour employed	18.0	18.1	19.3	19.5	19.3	19.2
Labour non-employed	2.1	2.2	2.3	2.6	2.7	2.6
Capital and business income	7.4	8.3	8.8	7.9	7.5	7.4
Stocks of capital/wealth	2.6	2.5	2.2	3.0	2.4	2.6
p.m. Environmental taxes[2]	2.9	2.8	2.5	2.7	2.6	2.8
VAT efficiency[3]						
Actual VAT revenues as % of theoretical revenues at standard rate	43.1	42.8	40.6	37.4	41.7	41.3

Note:

[1] Tax revenues are broken down by economic function, i.e. according to whether taxes are raised on consumption, labour or capital. See European Commission (2013) Taxation trends in the European Union, for a more detailed explanation.

[2] This category comprises taxes on energy, transport and pollution and resources included in taxes on consumption and capital.

[3] The VAT efficiency is measured via the VAT revenue ratio. The VAT revenue ratio is defined as the ratio between the actual VAT revenue collected and the revenue that would theoretically be raised if VAT was applied at the standard rate to all final consumption. A low ratio can indicate a reduction of the tax base due to large exemptions or the application of reduced rates to a wide range of goods and services ('policy gap') or a failure to collect all tax due to e.g. fraud ('collection gap'). See European Commission (2012), Tax reforms in EU Member States, European Economy 6/2012 and Taxation Papers 34/2012 for a more detailed explanation.

Source: Commission

Table VII. Financial market indicators

	2008	2009	2010	2011	2012
Total assets of the banking sector (% of GDP)	234.5	246.5	244.6	257.6	269.6
Share of assets of the five largest banks (% of total assets)	31.2	31.0	39.8	39.5	…
Foreign ownership of banking system (% of total assets)	13.4	12.3	…	…	…
Financial soundness indicators:					
- non-performing loans (% of total loans)[1),2)]	6.3	9.5	10.0	11.7	12.9
- capital adequacy ratio (%) [1)]	10.4	11.7	12.1	12.7	13.3
- return on equity (%) [1), 3)]	4.9	4.0	3.7	-13.0	1.0
Bank loans to the private sector (year-on-year % change)	5.8	2.4	3.9	1.0	1.4
Lending for house purchase (year-on-year % change)	0.0	5.9	7.5	4.4	-0.2
Loan to deposit ratio	136.6	131.2	123.0	125.7	117.4
CB liquidity as % of liabilities	1.7	0.9	1.6	5.9	7.3
Banks' exposure to countries receiving official financial assistance (% of GDP)[4)]	4.9	4.8	4.3	4.2	3.5
Private debt (% of GDP)	102.9	109.5	116.0	115.9	119.0
Gross external debt (% of GDP)[5)]					
- Public	45.0	52.2	52.1	42.5	44.6
- Private	23.0	25.0	25.6	25.0	25.6
Long term interest rates spread versus Bund (percentage points)*	0.7	1.1	1.3	2.8	4.0
Credit default swap spreads for sovereign securities (5-year)*	88.4	108.2	164.4	299.4	399.9

Notes:

1) Latest data (June 2012).

2) A change in the definition of the Non Performing Loan was made in 2012.

3) After extraordinary items and taxes.

4) Covered countries are CY, EL, ES, LV, HU, IE, PT and RO.

5) Latest data 2012Q3.

* Measured in percentage points.

Source :

Bank for International Settlements and Eurostat (exposure to macro-financially vulnerable countries), IMF (financial soundness indicators), Commission (long-term interest rates), World Bank (gross external debt) and ECB (all other indicators).

Table VIII. Labour market and social indicators

Labour market indicators	2007	2008	2009	2010	2011	2012
Employment rate (% of population aged 20-64)	62.8	63.0	61.7	61.1	61.2	61.0
Employment growth (% change from previous year)	1.3	0.3	-1.6	-0.7	0.3	-0.3
Employment rate of women (% of female population aged 20-64)	49.9	50.6	49.7	49.5	49.9	50.5
Employment rate of men (% of male population aged 20-64)	75.8	75.4	73.8	72.8	72.6	71.6
Employment rate of older workers (% of population aged 55-64)	33.8	34.4	35.7	36.6	37.9	40.4
Part-time employment (% of total employment, 15 years and more)	13.6	14.3	14.3	15.0	15.5	17.1
Part-time employment of women (% of women employment, 15 years and more)	26.9	27.9	27.9	29.0	29.3	31.1
Part-time employment of men (% of men employment, 15 years and more)	5.0	5.3	5.1	5.5	5.9	7.2
Fixed term employment (% of employees with a fixed term contract, 15 years and more)	13.2	13.3	12.5	12.8	13.4	13.8
Transitions from temporary to permanent employment	3.0	2.4	3.3	1.6	2.1	:
Unemployment rate1 (% of labour force, age group 15-74)	6.1	6.7	7.8	8.4	8.4	10.7
Long-term unemployment rate2 (% of labour force)	2.9	3.1	3.5	4.1	4.4	5.7
Youth unemployment rate (% of youth labour force aged 15-24)	20.3	21.3	25.4	27.8	29.1	35.3
Youth NEET rate (% of population aged 15-24)	16.2	16.6	17.7	19.1	19.8	21.1
Early leavers from education and training (% of pop. 18-24 with at most lower sec. educ. and not in further education or training)	19.7	19.7	19.2	18.8	18.2	17.6
Tertiary educational attainment (% of population 30-34 having successfully completed tertiary education)	18.6	19.2	19.0	19.8	20.3	21.7
Formal childcare (from 1 to 29 hours; % over the population less than 3 years)	10.0	12.0	9.0	6.0	9.0	:
Formal childcare (30 hours or over; % over the population less than 3 year)	15.0	16.0	16.0	16.0	17.0	:
Labour productivity per person employed (annual % change)	0.7	-0.8	-2.7	2.8	0.2	-1.3
Hours worked per person employed (annual % change)	0.1	-0.7	-1.7	0.1	0.0	-1.1
Labour productivity per hour worked (annual % change; constant prices)	0.3	-0.7	-2.2	2.4	0.1	-1.0
Compensation per employee (annual % change; constant prices)	-0.1	1.2	-0.4	2.4	-0.1	-0.6
Nominal unit labour cost growth (annual % change)	1.6	4.5	4.0	-0.2	1.1	2.1
Real unit labour cost growth (annual % change)	-0.7	2.0	1.9	-0.6	-0.2	0.5

Notes:

[1] Unemployed persons are all persons who were not employed, had actively sought work and were ready to begin working immediately or within two weeks. The labour force is the total number of people employed and unemployed.

[2] Long-term unemployed are unemployed persons for at least 12 months.

Sources:
Commission (EU Labour Force Survey and European National Accounts)

Expenditure on social protection benefits (% of GDP)	2006	2007	2008	2009	2010
Sickness/Health care	6.84	6.60	6.93	7.30	7.30
Invalidity	1.50	1.52	1.56	1.73	1.70
Old age and survivors	15.39	15.54	16.07	17.13	17.33
Family/Children	1.14	1.24	1.28	1.44	1.31
Unemployment	0.51	0.45	0.51	0.79	0.84
Housing and Social exclusion n.e.c.	0.02	0.02	0.02	0.02	0.02
Total	25.47	25.43	26.42	28.47	28.57
of which: means tested benefits	1.59	1.68	1.75	1.98	0.00
Social inclusion indicators	**2007**	**2008**	**2009**	**2010**	**2011**
At-risk-of-poverty or social exclusion[1] (% of total population)	26.0	25.3	24.7	24.5	28.2
At-risk-of-poverty or social exclusion of children (% of people aged 0-17)	29.3	29.1	28.8	28.9	32.2
At-risk-of-poverty or social exclusion of elderly (% of people aged 65+)	25.3	24.4	22.8	20.3	24.1
At-Risk-of-Poverty rate[2] (% of total population)	19.8	18.7	18.4	18.2	19.6
Severe Material Deprivation[3] (% of total population)	6.8	7.5	7.0	6.9	11.2
Share of people living in low work intensity households[4] (% of people aged 0-59)	10.0	9.8	8.8	10.2	10.4
In-work at-risk-of poverty rate (% of persons employed)	9.8	8.9	10.3	9.4	10.7
Impact of social transfers (excluding pensions) on reducing poverty	17.8	20.1	20.7	21.9	19.7
Poverty thresholds, expressed in national currency at constant prices[5]	9003	9194	8878	8982	8855
Gross disposable income (households)	1074439	1095209	1065726	1073912	1098825
Relative median poverty risk gap (60% of median equivalised income, age: total)	22.4	23.0	22.6	24.5	26.0

Notes:

[1] People at-risk-of poverty or social exclusion (AROPE): individuals who are at-risk-of poverty (AROP) and/or suffering from severe material deprivation (SMD) and/or living in household with zero or very low work intensity (LWI).

[2] At-risk-of poverty rate (AROP): share of people with an equivalised disposable income below 60% of the national equivalised median income.

[3] Share of people who experience at least 4 out of 9 deprivations: people cannot afford to i) pay their rent or utility bills, ii) keep their home adequately warm, iii) face unexpected expenses, iv) eat meat, fish, or a protein equivalent every second day, v) enjoy a week of holiday away from home once a year, vi) have a car, vii) have a washing machine, viii) have a colour tv, or ix) have a telephone.

[4] People living in households with very low work intensity: share of people aged 0-59 living in households where the adults (excluding dependent children) work less than 20% of their total work-time potential during the previous 12 months.

[5] For EE, CY, MT, SI, SK, thresholds in nominal values in Euros; HICP - index 100 in 2006 (2007 survey refers to 2006 incomes)

Sources:
For expenditure for social protection benefits ESSPROS; for social inclusion EU-SILC.

Table IX. Product market performance and policy indicators

Performance indicators	2003-2007	2008	2009	2010	2011	2012
Labour productivity[1] total economy (annual growth in %)	0.6	-1.4	-3.9	2.5	0.1	-2.1
Labour productivity[1] in manufacturing (annual growth in %)	2.4	-2.8	-12.4	11.7	1.5	-2.2
Labour productivity[1] in electricity, gas, steam and air conditioning supply (annual growth in %)	3.5	4.9	-1.5	7.3	3.7	n.a.
Labour productivity[1] in the construction sector (annual growth in %)	-0.8	-3.1	-7.1	-1.2	-0.8	-1.1
Total number of patent[2] applications per million of labour force	194.1	185.9	183.8	177.9	n.a.	n.a.
Policy indicators	**2003-2007**	**2008**	**2009**	**2010**	**2011**	**2012**
Enforcing contracts[3] (days)	1318	1210	1210	1210	1210	1210
Time to start a business[3] (days)	15	10	10	6	6	6
R&D expenditure (% of GDP)	1.1	1.2	1.3	1.3	1.3	n.a.
Tertiary educational attainment (% of 30-34 years old population)	16.6	19.2	19.0	19.8	20.3	21.7
Total public expenditure on education (% of GDP)	4.53	4.56	4.70	4.50	n.a.	n.a.
	2007	**2008**	**2009**	**2010**	**2011**	**2012**
Product market regulation[4], Overall (Index; 0=not regulated; 6=most regulated)	n.a.	1.4	n.a.	n.a.	n.a.	n.a.
Product market regulation[4], Retail (Index; 0=not regulated; 6=most regulated)	n.a.	2.6	n.a.	n.a.	n.a.	n.a.
Product market regulation[4], Network Industries[5] (Index; 0=not regulated; 6=most regulated)	2.0	n.a.	n.a.	n.a.	n.a.	n.a.

Notes:

[1] Labour productivity is defined as gross value added (in constant prices) divided by the number of persons employed.

[2] Total number of patent applications to the European Patent Office (EPO) per million of labour force

[3] The methodologies, including the assumptions, for this indicator are presented in detail on the website http://www.doingbusiness.org/methodology.

[4] The methodologies of the product market regulation indicators are presented in detail on the website http://www.oecd.org/document/1/0,3746,en_2649_34323_2367297_1_1_1_1,00.html. The latest available product market regulation indicators refer to 2003 and 2008, except for Network Industries.

[5] Aggregate Energy, Transport and Communications Regulation (ETCR).

*figure for 2007.

Source:
Commission, World Bank - *Doing Business* (for enforcing contracts and time to start a business) and OECD (for the product market regulation indicators).

Table X. Green Growth

		2002-2006	2007	2008	2009	2010	2011
Green Growth performance							
Macroeconomic							
Energy intensity	kgoe / €	0.15	0.14	0.14	0.14	0.14	0.14
Carbon intensity	kg / €	0.46	0.42	0.42	0.40	0.40	n.a.
Resource intensity (reciprocal of resource productivity)	kg / €	0.65	0.61	0.60	0.56	n.a.	n.a.
Waste intensity	kg / €	n.a.	n.a.	0.14	n.a.	0.13	n.a.
Energy balance of trade	% GDP	-1.6%	-1.9%	-2.2%	-2.7%	-3.3%	-3.8%
Energy weight in HICP	%	n.a.	9	8	8	8	8
Difference between change energy price and inflation	%	n.a.	-0.6	7.4	-5.8	-3.3	5
Environmental taxes over labour taxes	ratio	14.2%	13.0%	11.6%	12.4%	11.9%	n.a.
Environmental taxes over total taxes	ratio	7.0%	6.3%	5.9%	6.3%	6.1%	n.a.
Sectoral							
Industry energy intensity	kgoe / €	0.15	0.14	0.13	0.13	0.13	n.a.
Share of energy-intensive industries in the economy	% GDP	9.5	9.8	9.6	8.4	n.a.	n.a.
Electricity prices for medium-sized industrial users**	€ / kWh	n.a.	n.a.	0.14	0.15	0.14	0.16
Gas prices for medium-sized industrial users***	€ / kWh	n.a.	0.03	0.04	0.03	0.03	0.03
Public R&D for energy	% GDP	n.a.	0.02%	0.04%	0.03%	0.04%	0.04%
Public R&D for the environment	% GDP	n.a.	0.02%	0.03%	0.02%	0.02%	0.02%
Recycling rate of municipal waste	ratio	52.4%	61.9%	42.4%	46.3%	46.6%	n.a.
Share of GHG emissions covered by ETS*	%	n.a.	40.8%	40.8%	37.7%	38.3%	38.9%
Transport energy intensity	kgoe / €	n.a.	0.45	0.44	0.44	n.a.	n.a.
Transport carbon intensity	kg / €	n.a.	1.28	1.24	1.24	n.a.	n.a.
Security of energy supply							
Energy import dependency	%	n.a.	85.1%	85.3%	82.8%	83.8%	81.3%
Diversification of oil import sources	HHI	n.a.	0.14	0.13	0.13	0.11	n.a.
Diversification of energy mix	HHI	n.a.	0.35	0.34	0.34	0.33	0.31
Share renewable energy in energy mix	%	n.a.	6.5%	7.5%	9.4%	10.3%	11.5%

Country-specific notes:
The year 2012 is not included in the table due to lack of data.
General explanation of the table items:
Source: Eurostat unless indicated otherwise; ECFIN elaborations indicated below
All macro intensity indicators are expressed as a ratio of a physical quantity to GDP (in 2000 prices)
- Energy intensity: gross inland energy consumption (in kgoe) divided by GDP (in EUR)
- Carbon intensity: Greenhouse gas emissions (in kg CO2 equivalents) divided by GDP (in EUR)
- Resource intensity: Domestic Material Consumption (in kg) divided by GDP (in EUR)
- Waste intensity: waste (in kg) divided by GDP (in EUR)

Energy balance of trade: the balance of energy exports and imports, expressed as % of GDP
Energy weight in HICP: the share of the "energy" items in the consumption basket used in the construction of the HICP
Difference between energy price change and inflation: energy component of HICP, and total HICP inflation (annual %-change)
Environmental taxes over labour or total taxes: from DG TAXUD's database "Taxation trends in the European Union"
Industry energy intensity: final energy consumption of industry (in kgoe) divided by gross value added of industry (in 2005 EUR)
Share of energy-intensive industries in the economy: share of gross value added of the energy-intensive industries in GDP
Electricity and gas prices medium industrial users: consumption band 500 - 2000MWh and 10000 - 100000 GJ; figures excl. VAT.
Recycling rate of municipal waste: ratio of municipal waste recycled over total municipal waste
Public R&D for energy or for the environment: government spending on R&D (GBAORD) for these categories as % of GDP
Share of GHG emissions covered by ETS: based on greenhouse gas emissions as reported by Member States to EEA (excl LULUCF)
Transport energy intensity: final energy consumption of transport activity (kgoe) divided by transp industry gross value added (2005 EUR)
Transport carbon intensity: greenhouse gas emissions in transport activity divided by gross value added of the transport sector
Energy import dependency: net energy imports divided by gross inland energy consumption incl. energy consumption international bunkers
Diversification of oil import sources: Herfindahl index (HHI), calculated as the sum of the squared market shares of countries of origin
Diversification of the energy mix: Herfindahl Index over natural gas, total petrol products, nuclear heat, renewable energies and solid fuels
Share renewable energy in energy mix: %-share in gross inland energy consumption, expressed in tonne oil equivalents
*Provisional data (15 April 213). Commission Services and EEA.
** For 2007 average of S1 & S2 for DE, LU, NL, FI, SE & UK. Other countries only have S2.
*** For 2007 average of S1 & S2 for IT, NL, FI, SE & UK. Other countries only have S2.