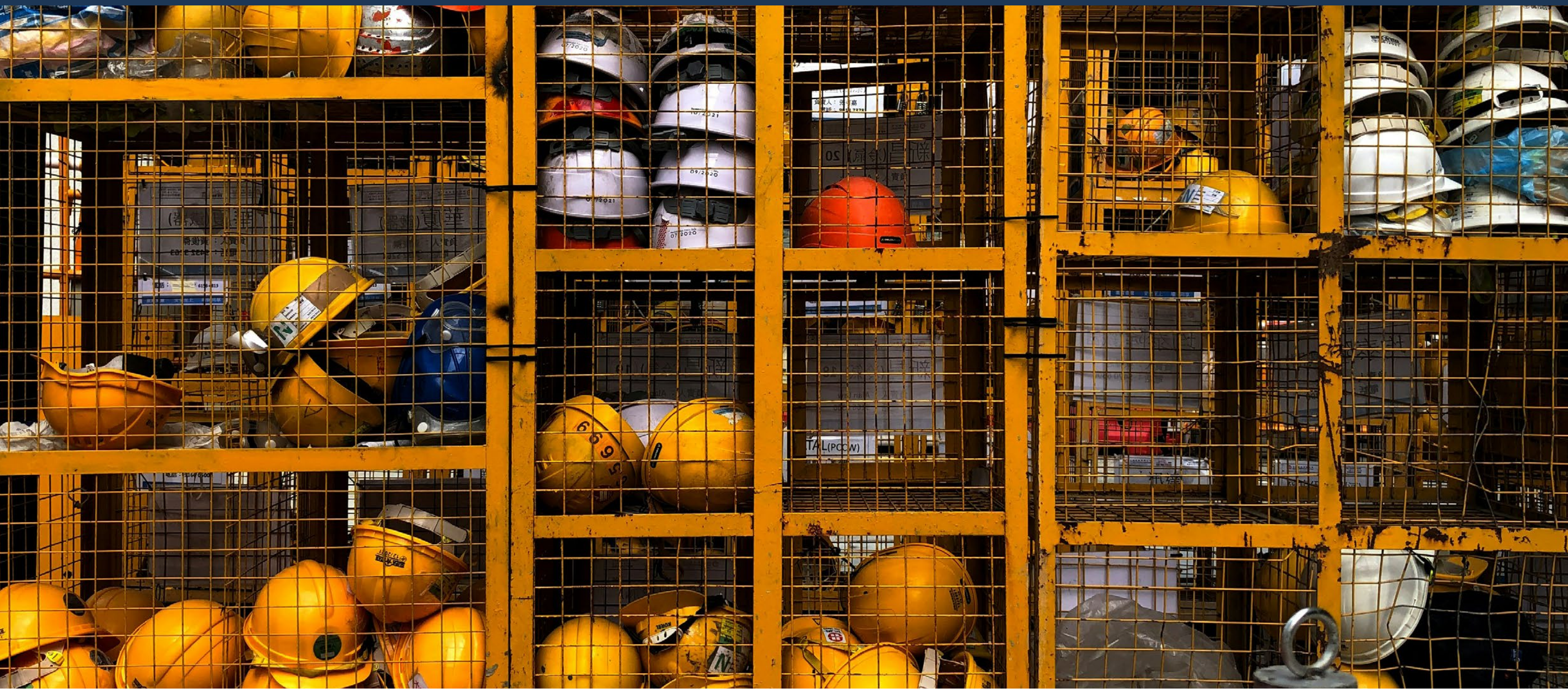

The recovery is full of employment and more work means more growth. Italy beats France and Germany, and even the USA.

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At a glance

- In GDP the Italian economy is doing better than France and Germany
- In creating new jobs it exceeds the powerful American job-machine
- Italy's higher growth is due both to stimuli, such as the "superbonus", and to export performance
- In the coming quarters, manufacturing will benefit from strengthened global demand
- Global recovery gains speed and broadens geographically and to commodities
- Inflation continues to decelerate slowly
- The scenario is favourable for lower interest rates and higher corporate profits
- Immigration expands labour supply and boosts economic development

Rising recovery

The **Italian ship** is advancing in the storms of the world economy. And it sails the stormy global seas better than the French and German ships. **Three indicators** prove this: GDP, employment and exports.

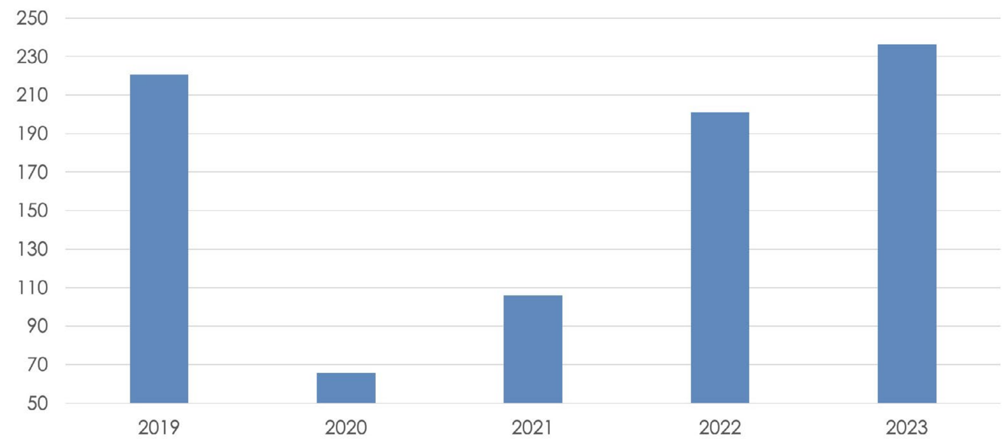
The **increase in Italy's GDP** went far beyond what would have been expected on the basis of the poor pre-pandemic data and significantly exceeded the results obtained by its transalpine cousins and the rigorous Germans: +4.4% against +3.4% and +0.6% in the first quarter of '24 compared to the first quarter of '19. The winning spurt is due to three factors.

The first is the post-Covid return of normal **international tourist travel**; Italy, along with Spain, particularly benefited from people's desire to get back on the road and visit places of rare monumental or natural beauty (Chart 1).

It is likely that the pandemic experience has **changed consumer preferences** in favour of this use of leisure time and spending capacity, rather than material goods, which are increasingly favoured for use rather than ownership (e.g. renting cars and appliances rather than buying them). However, qualitative-quantitative information suggests that the rise in arrivals and visitors from abroad is continuing in 2024.

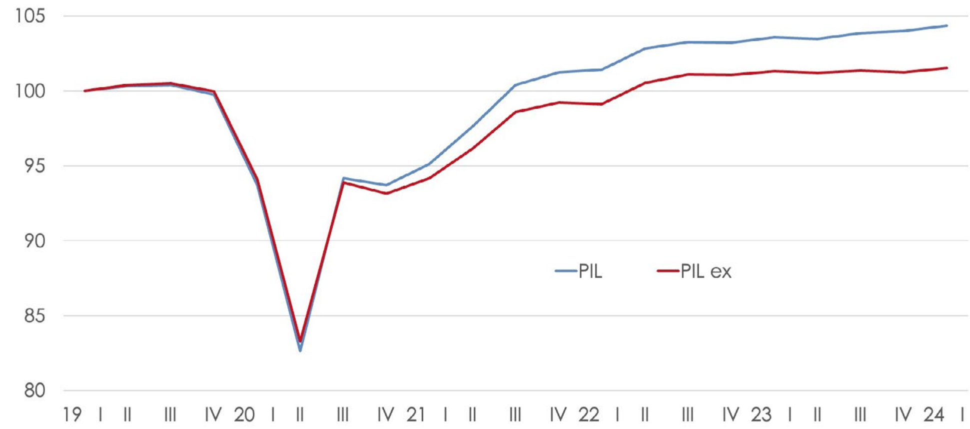
The second factor is the **"superbonus" effect,** which has both a direct and indirect aspect. Although many continue to deny substantial real benefits from the incentives and criticise the policies for excessive generosity (perhaps) and poor legislative design (a typical trait of Italian regulations), the numbers do not lie: excluding **investment in housing** (which includes renovation work), Italian GDP rose by 1.5% over the same period used above (Chart 2).

Gr. 1 - Tourism takes flight
(Italy, foreign presences in millions)



Source: elaborazione REF Ricerche su dati ISTAT

Gr. 2 - Put a superbonus in GDP
(Italy, GDP at chained prices, 1st tr. '19=100)



Source: elaborazione REF Ricerche su dati ISTAT

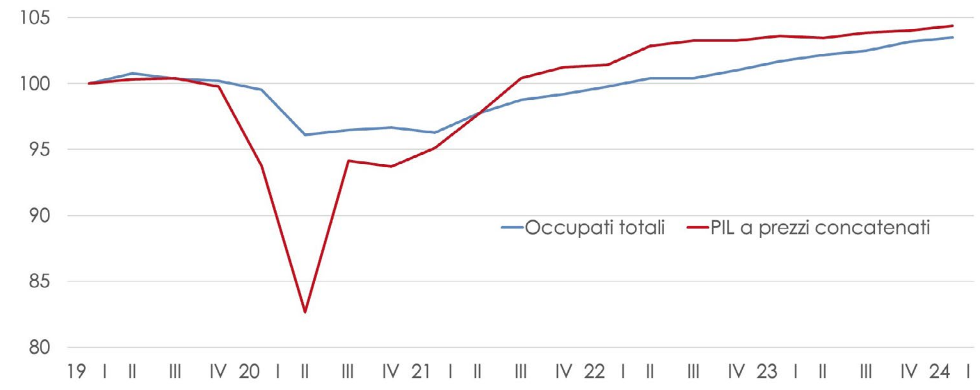
This rough but effective calculation does not take into account the first indirect effect, that economists call a **multiplier**, which is all the greater the more depressed the economic conditions are, as was certainly the case in Italy when it emerged from the pandemic. But there is another indirect effect, completely imponderable, which is the **strengthening of the socio-economic fabric** when the economy expands more rapidly. Technically speaking, this refers to the increase in potential GDP, both as a level and as a rate of increase; the existence of this effect is demonstrated by the upward revision of Italy's **potential growth** to 1%, from less than 0.5% a few years ago. Economists always make actual GDP dependent on potential GDP, but in reality the relationship is biunivocal: higher actual GDP also increases potential GDP. After all, this is what happens to athletes with training, which improves performance.

The third factor is precisely related to the second indirect effect and consists of the **budgetary policies** that have supported demand and supply in the economy with targeted interventions to protect them from the blows of lockdowns first, and the energy crisis subsequently. The risk is that now, under pressure from 'frugal' European partners, we will try to **reduce the public deficit** in forced stages, with negative consequences similar to those caused by the sovereign debt crisis. We need to be judicious in our choices, avoiding wasting resources with further electoral tirades (such as pension advances) and keeping the bar set on strengthening the production system thanks to the PNRR.

Italian employment is at an all-time high and it continues to rise faster than GDP would suggest (Chart 3). The temptation to claim that productivity is falling is strong, while in fact it is much more likely that the estimates of Italian output are too low.

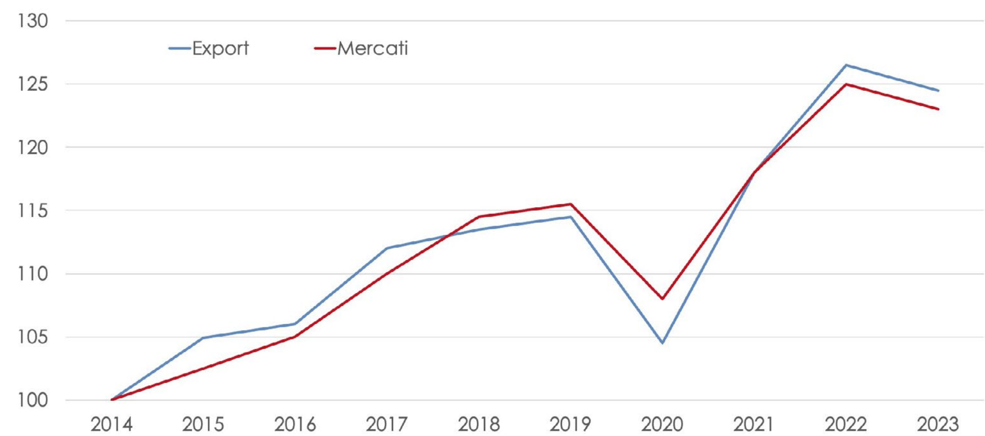
Indeed, the figures for 2021 have been revised upwards from the initial +6.6% to the current +8.3% and those for 2022 from +3.7% to +4.0%; but the **biggest adjustment** will occur with the next recalculation, which will be based on full information. Chart 3 shows, in fact, the flattening of the GDP curve in the last two years, those that are still subject to revision, while employment is running at an almost constant pace (slope of the line).

Gr. 3 - Employment and GDP converging
(Italy, indexes 1sttr. '19=100)



Finally, **exports** are doing as well as or better than reference markets (Chart 4). Meaning, Italy is defending or gaining share. Above all, the position with respect to France and Germany has reversed: if until 2019 (included) these countries were able to grow their sales abroad faster than Italy, in the following period foreign purchases of 'Made in Italy' products increased in volume to a greater degree, to the point that in 2023 they were almost 9% above the level of four years earlier, while France and Germany recorded lower values compared to then.

Gr. 4 - Made in Italy gallops
(Italy, exports of goods and its markets, volumes, '14=100)



This was due to greater **production diversification**, the complexity of exported goods (a function of the number of products and countries of outlet), the steady increase in **quality** (measured by the rise in the ratio of average unit values to producer prices of exported goods, Chart 5), innovation and **workers' skills**.

Gr. 5 - The upgrading of Italian quality
(Export unit value divided by export prices, g. '00=100)

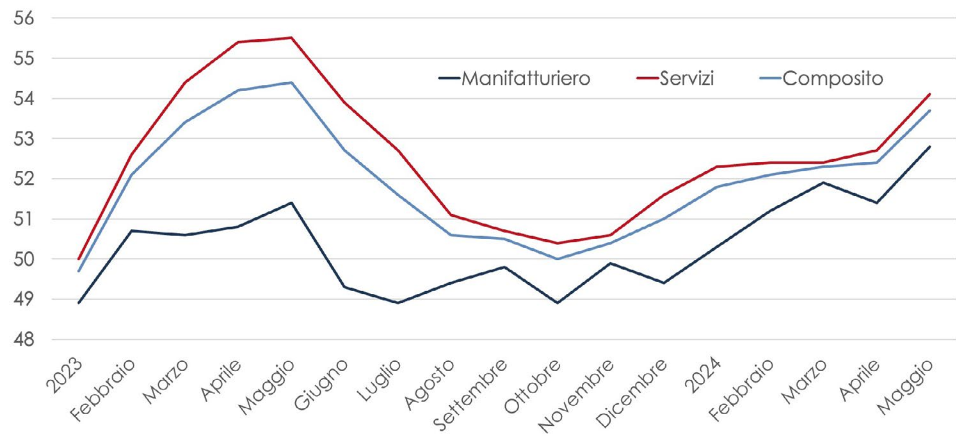
Source: elaborazione REF Ricerche su dati ISTAT

In addition to these factors, there is **nearshoring** and **friendshoring**, where Made in Italy can benefit as it owns complete production chains and is firmly embedded in global value chains.

How will it end? In the coming quarters the effects of the superbonus will fade, after the stop decreed by the Minister of the Economy, even with retroactive fiscal effects; on the other hand, the **global recovery** is gaining strength, as the Osservatorio has been repeating for some time and as the latest **PMI data** also confirm (Chart 6). And it increasingly involves **manufacturing** and thus foreign trade (of which industrial goods are the overwhelming majority). Thus, the weakening of construction, which will in any case be limited by the acceleration of NRP investment, will be replaced by a rebound in manufacturing, which had suffered most from rising interest rates. The conclusion is that the 2024 vintage of Italian GDP will be better than the estimates of a few months ago and even the most recent ones. Bets are being taken on an increase of more than +1%.

Talking of global recovery, in a nutshell, its **extension to countries and sectors** should be emphasised, and it should be noted that chorality adds strength and that manufacturing, being cyclical, revs up the engine. Like **turbo boosting**, a term that in a few years with the diffusion of electric motors will become unknown to most. All this has implications for financial investments, because it means higher earnings growth and stock rotation.

Gr. 6 - Global recovery accelerates
(Global PMI, output, >50=expansion)



Source: elaborazione REF Ricerche su dati S&P Global

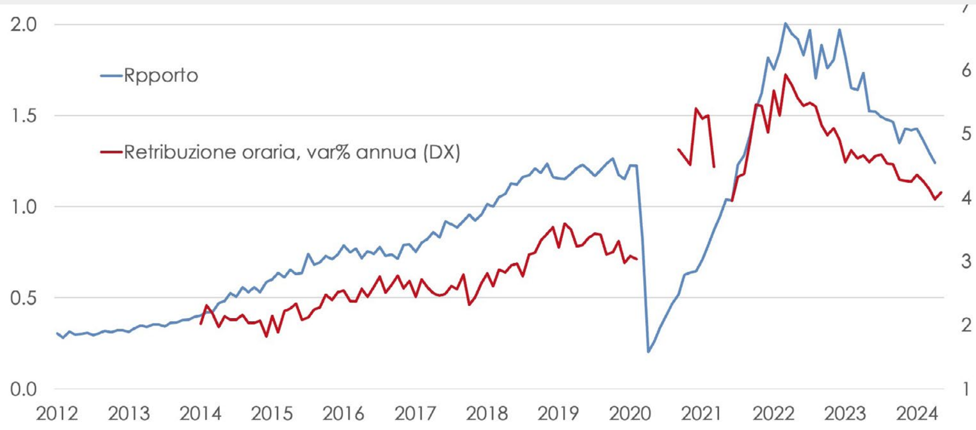
Falling inflation

Recent and outgoing numbers confirm the picture outlined in the last Monitor: **US inflation** has started to fall again. There are both **statistical and real factors** behind the cooling. The statistical ones have to do with the difficulty of capturing changes in sectors with filters that remove seasonal variations; these filters were developed using long time series spanning the period of almost zero consumer price dynamics (for a more in-depth examination see the Osservatorio May 2024).

The **real factors** are concentrated in the reduction of tension in the **US labour market**: the ratio of vacancies to the unemployed has returned to the values of 2019, which were high compared to the period after the Great Financial Crisis but did not lead to worrying wage increases (Chart 7).

The May figures for employment and wages at first glance are hardly reassuring, with increases still strong. Trends, however, should be observed over a longer time span, which is not affected by monthly volatility.

Gr. 7 - Fewer vacancies in the U.S.
(Ratio of job vacancies to unemployed)



NB: sono stati esclusi i dati distorti dagli effetti dei lockdown sull'occupazione
Source: elaborazione REF Ricerche su dati US BLS

Wages offered for new hires are also moving in the direction of moderation, with increases returning to those of 2019.

By contrast, in the **Eurozone**, the **wage bargaining system** has allowed the run-up between prices and wages to be bridged in the past two years, but now generates a longer echo for the recovery of purchasing power, which takes place with a delay and according to the dictate of collective agreements (Chart 8).

Gr. 8 - Wages on the brakes
(Annual % change in wages offered for new hires, three-month moving average)

Source: elaborazione REF Ricerche su dati Indeed

Falling rates and rising stock markets

The macroeconomic picture with a strengthening recovery and deflating inflation leads to expectations of **further rate cuts**, dismissing the fears that had run through the markets of further tightening by the **Fed**. This explains the downward move in yields on long bonds (Chart 9). But it is also an unhurried reduction, because the economy is healthy and does not need emergency room treatment. And the **ECB**, which was the first to move? It will have to be even more patient in making other cuts after the first, precisely because wage pressure is more persistent.

Gr. 9 - Rates smelling a decline
(Yields % 10-year sovereign bonds)

Source: elaborazione REF Ricerche su dati Datastream

French and Italian bonds did not participate in the latest fall in yields, due to the political tensions coming out of the **European polls**. The worst is yet to come, think those who fear there will be a Brexit in continental sauce. On the contrary, it is this very **Brexit** that shows how costly it is to decide to move the clock of history backwards towards an autarkic nationalism. Hence the **British lesson** will serve to harness political choices in the EU.
The behaviour of **stocks** confronted with falling rates can have two effects: to queue or to oppose. **To queue up** when the cut in the cost of money is the cure for recession. To oppose when instead it is mitigation of the **anti-recession therapy**. Since the current case is the latter, it is to be expected that profits will rise. True, lower inflation means that the nominal rise in **profits** will be more moderate. But everything cannot be had and it will be a good thing. Moreover, if inflation drives up the returns of all companies, the absence of inflation **will reward the best ones**, and stock-picking will be a winner.

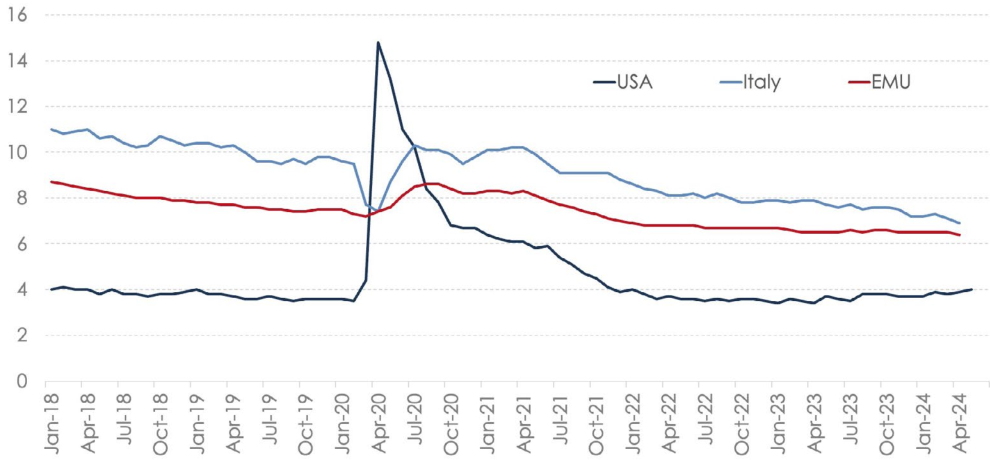
Employment expansion supports economic growth

Employment expansion on both sides of the Atlantic continues to impress with its strength, growing undisturbed despite two years of interest rate hikes. The Eurozone unemployment rate at 6.4 per cent is at an all-time low since the creation of the Eurozone, while in the United States, after hitting a low at 3.4 per cent in early 2023, it has risen moderately to 4 per cent. The Italian unemployment rate at 6.9% is also significantly below the 9.6% average of the last 25 years and down from the 10% pandemic peak. A genuine labour market recovery, also supported by rising participation rates.

The expansion of labour supply in these advanced economies has significantly helped to sustain both economic growth but also the disinflation process, avoiding a price-wage inflationary spiral. The expansion of the labour force has often reflected an increase in migration flows, with, starting in the post-pandemic period, a faster growth of the foreign-born labour force than the domestically-born.

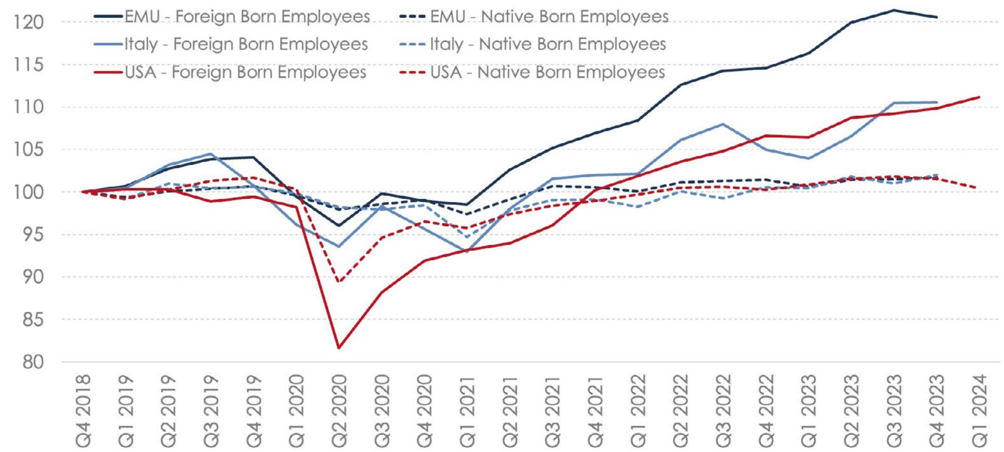
In both Europe (including Italy) and the US, in contrast with domestic employment returning to just above 2018 levels, foreign-born employment increased by 20% in the Eurozone (with the Russian-Ukrainian war causing significant immigration) and 10% in the US. Italy is in line with the US, with a 10% increase in foreign-born employment (from 3.1mn to 3.4mn in 5 years, compared to domestic employment rising from only 19.2 to 19.6mn).

Gr. 10 - Unemployment Rate



Source: Uffici statistici nazionali

Gr. 11 - Domestic & Foreign Born Employees
(rebased to 100 at Q418)



Source: Bureau of Labor Statistics & Eurostat

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