English translation, the Italian version remains the official document

Rome, 13 November 2018

Dear Vice-President,

Dear Commissioner,

In reply to your letter of 23 October 2018, in which you forwarded the European Commission's opinion on Italy's Draft Budgetary Plan 2019 and requested the submission of a revised version, I would like to share the following considerations.

The reasons underlying the policy approach of the document were explained in detail in previous correspondence. The Government considers that the motivations that we already illustrated remain valid, even after carefully weighing the arguments set out in your opinion on the DBP.

In particular, improving the growth outlook remains a priority in order to close the lingering gap between Italy's GDP and the levels reached before the economic and financial crisis — and to address the ongoing cyclical slowdown.

Tackling the social problems caused by the negative trend in the economy is equally important and urgent, through a broad policy initiative (Citizenship Income) aimed at alleviating hardship and poverty, and improving social inclusion and sustainability.

The Government also confirms its intention to reduce the rigidities and constraints introduced in the pension system during the economic crisis, which sharply raised the statutory retirement age, with negative consequences on the turnover of the workforce and on firms' restructuring.

Though introducing innovative stimulus measures and easing retirement rules, the fiscal expansion decided by the Government is confined to what is strictly necessary to counter the slowdown in the business cycle.

In addition, a notable feature of the policy plan is an increase in the resources devoted to public investment, which over the next three years will make it possible to recover at least part of the drop recorded during the crisis. The increase in resources is accompanied by streamlined administrative procedures, which will speed up the implementation of investment projects. A new dedicated administrative entity will provide advanced design services to public administrations that need to carry out investment programs.

Thanks to the fiscal expansion, the reforms introduced, the revitalization of public investment, and a reduction in the tax burden on small businesses, the policy plan will allow us to achieve a higher GDP growth rate than the baseline scenario and reduce the gap vis-à-vis other European countries. The Government remains confident that the growth projections of the DBP can be achieved.

I emphasize once again that the budgetary plan was built on the basis of the baseline macroeconomic projections and does not include second-round effects of higher GDP growth on government revenue and expenditure. This prudential approach introduces a safeguard buffer in the Budget, as it prevents an overshoot as long as growth exceeds the baseline forecast.

The revised DBP contains some important innovations.

First, in order to accelerate the reduction of the debt ratio and to preserve it from the risk of possible macroeconomic shocks, the Government decided to raise the 2019 target for the sale of public assets to 1 % of GDP. Proceeds from privatization provide a safety margin to ensure that the debt reduction targets adopted by Parliament are met even if GDP growth falls short of the baseline projection. Taking into account these revenues and their impact in terms of lower debt issuance on the market, and thus lower interest payments, the decline in the debt ratio in 2019-2021 would be larger than in the original DBP. After posting a 0.3 percentage point decline this year, the debt ratio would decrease by 1.7 points in 2019, 1.9 in 2020 and 1.4 in 2021. All in all, the ratio would fall from 131.2 % in 2017 to 126.0 in 2021.

Secondly, I would like to point out that expenditure of an exceptional nature of around 0.2 % of GDP are included in the Budget for each of the next three years. In recent weeks, Italy was hit by particularly serious flooding, with very high costs in terms of human losses and damages. These events, though extraordinary and unexpected, have once again exposed Italy's hydrogeological vulnerability, which must be redressed.

The resources indicated will be allocated to an extraordinary plan to combat hydrogeological vulnerability and, for 2019 only, to additional emergency maintenance to repair the transportation network. The Government will also draw up a longer-term hydrogeological protection plan, to be swiftly rolled out and implemented over the next five years with a stringent timetable. Actions will be taken to simplify and speed up the decision-making and implementation process, and to strengthen the technical competency of the public entities involved.

In addition, with regard to transportation networks, the collapse of the Morandi bridge in Genoa highlighted the need to undertake an extraordinary maintenance program. To this end, the Budget earmarks EUR 1 billion for 2019 to safety and maintenance of road infrastructure such as viaducts, bridges and tunnels. The intervention will focus on infrastructure similar in design or maintenance needs to the Morandi bridge. The plan will be treated as an emergency intervention eligible for simplified tender procedures under Italian law. This will significantly reduce the time needed to allot the contracts.

In relation to these expenditures on extraordinary hydrogeological interventions and transportation network maintenance, the Government requests the application of budgetary flexibility for exceptional events.

Finally, the Government confirms its commitment to ensuring that budget balances do not exceed the targets set in the DBP and authorized by the Italian Parliament. In particular, the 2.4 percent of GDP deficit level for 2019 will be considered an absolute limit. Net borrowing will be continuously monitored, in terms of both macroeconomic performance and evolution of revenue and expenditure.

The national legislation contains a series of provisions that oblige the Government to report to Parliament in a timely manner in case of discernible deviations from the official targets. The Economy and Finance Minister is responsible for monitoring the public finances. The Minister must also verify that the implementation of new laws does not undermine the achievement of the agreed objectives and take timely corrective action in the event of a deviation, in accordance with constitutional principles.

Yours faithfully,

Giovanni Tria
Minister of economy and finance

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Vice-President of the
European Commission,
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Pierre Moscovici
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