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COMMISSION OPINION

of 21.11.2023

on the Draft Budgetary Plan of Italy

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(Only the Italian text is authentic)

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GENERAL CONSIDERATIONS

1. Regulation (EU) No 473/2013[1] lays down provisions for enhanced monitoring of budgetary policies in the euro area, in order to ensure that national budgets are consistent with the economic policy guidance issued in the context of the Stability and Growth Pact and the European Semester for economic policy coordination.

2. Article 6 of Regulation (EU) No 473/2013 requires Member States to submit annually to the Commission and to the Eurogroup a Draft Budgetary Plan, by 15 October, setting out the budgetary targets for the forthcoming year, and outlining the main aspects underlying the budgetary outlook for general government and its subsectors.

3. On 8 March 2023, the Commission adopted a Communication[2] providing fiscal policy guidance for 2024, which confirmed that the general escape clause of the Stability and Growth Pact will be deactivated at the end of 2023.

4. On 26 April 2023, the Commission presented three legislative proposals[3] to implement a comprehensive reform of the EU fiscal framework. The central objective of the proposals is to strengthen public debt sustainability and to promote sustainable and inclusive growth through reforms and investments. In its proposals, the Commission aims at improving national ownership, simplifying the framework and moving towards a greater medium-term focus, combined with effective and more coherent enforcement. According to the Council Conclusions adopted on 14 March 2023[4] and on 27 October 2023[5], the objective is to conclude the legislative work in 2023. As a new legal framework, based on the outcome of the ongoing economic governance review, is not yet in place, the current legal framework continues to apply. The fiscal component of the Spring 2023 country-specific recommendations

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[1] Regulation (EU) No 473/2013 of the European Parliament and of the Council of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area, (OJ L 140, 27.5.2013, pp. 11).

[2] Communication from the Commission to the Council, 'Fiscal policy guidance for 2024', 8.3.2023, COM(2023) 141 final.

[3] Commission Proposal for a Regulation of the European Parliament and of the Council on the effective coordination of economic policies and multilateral budgetary surveillance and repealing Council Regulation (EC) No 1466/97, 26.4.2023, COM(2023) 240 final; Commission Proposal for a Council Regulation amending Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure, 26.4.2023, COM(2023) 241 final; Commission Proposal for a Council Directive amending Directive 2011/85/EU on requirements for budgetary frameworks of the Member States, 26.4.2023, COM(2023) 242 final.

[4] Council Conclusions on 'Orientations for a reform of the EU economic governance framework' of the ECOFIN Council meeting, 14.3.2023, 6995/1/23 – REV 1.

[5] European Council meeting (26 and 27 October 2023) – Conclusions, EUCO 14/23.

included elements of the legislative proposals of 26 April 2023 that were consistent with the existing legislation.

5. As announced in its Communication on the 2023 European Semester[6], the Commission will propose to the Council to open deficit-based excessive deficit procedures in spring 2024 on the basis of the outturn data for 2023, in line with the existing legal provisions. Member States were invited to take this into account when executing their 2023 budgets and preparing their Draft Budgetary Plans for 2024.

6. The Recovery and Resilience Facility[7] provides financial support for the implementation of reforms and investments, notably to promote the green and digital transitions. The Facility also aims at increasing the resilience of the Union's energy system by reducing dependence on fossil fuels and diversifying energy supply at Union level ('REPowerEU objectives')[8]. The Facility will strengthen the resilience and potential growth of Member States' economies, which contributes to job creation and sustainable public finances. Part of this support takes the form of non-repayable financial support ("grants"), entailing a fiscal impulse financed by the Union. Together with cohesion policy funds and the Just Transition Mechanism, the Facility is supporting a fair and inclusive recovery in the EU, in line with the European Pillar of Social Rights.

7. Economic policy should continue to tackle the risks linked to high inflation and address long-term challenges. Although declining, inflation in the euro area remains a concern. It is essential that inflation continues to fall and that inflation expectations remain well anchored, with consistent monetary and fiscal policies, while remain agile in the face of high uncertainty. In particular, emergency energy support measures taken to respond to the energy price shock should be wound down, using the related savings to reduce the government deficits, as soon as possible in 2023 and 2024. Should renewed energy price increases necessitate new or continued support measures, these should be targeted at protecting vulnerable households and firms, as well as be fiscally affordable and preserve incentives for energy savings. Furthermore, Member States should continue to preserve nationally financed public investment and ensure the effective absorption of grants under the Recovery and Resilience Facility and of other EU funds, in particular to foster the green and digital transitions.

CONSIDERATIONS CONCERNING ITALY

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[6] Communication from the Commission to the Council, 'Fiscal policy guidance for 2024', 8.3.2023, COM(2023) 141 final.

[7] Regulation (EU) 2021/241 of the European Parliament and of the Council of 12 February 2021 establishing the Recovery and Resilience Facility, (OJ L 57, 18.2.2021, p. 17).

[8] Regulation (EU) 2023/435 of the European Parliament and of the Council of 27 February 2023 amending Regulation (EU) 2021/241 as regards REPowerEU chapters in recovery and resilience plans and amending Regulations (EU) No 1303/2013, (EU) 2021/1060 and (EU) 2021/1755, and Directive 2003/87/EC (OJ L 63, 28.2.2023, p. 1).

8. On 16 October 2023, Italy submitted its Draft Budgetary Plan for 2024. On that basis and taking into account the Council Recommendation to Italy of 14 July 2023[9], the Commission has adopted the following opinion in accordance with Article 7 of Regulation (EU) No 473/2013.

9. On 24 May 2023, the Commission adopted a report under Article 126(3) of the TFEU[10]. That report assessed the budgetary situation of Italy, as its general government deficit in 2022 exceeded the 3% of GDP Treaty reference value, while its general government debt exceeded the 60% of GDP Treaty reference value and did not respect the debt-reduction benchmark. The report concluded that the deficit and debt criteria were not fulfilled.

10. According to the Draft Budgetary Plan, Italy's real GDP is projected to grow by 1.2% in 2024 (0.8% in 2023), while inflation is forecast at 2.5% in 2024 (6.1% in 2023). In turn, according to the Commission 2023 autumn forecast, Italy's real GDP is projected to grow by 0.9% in 2024 (0.7% in 2023), while HICP inflation is forecast at 2.7% in 2024 (6.1% in 2023). The main differences between the two sets of projections reflect the Plan's more positive outlook for private consumption and particularly investment in 2024, while it expects net exports to subtract from GDP growth (small positive contribution in the Commission's forecast). Overall, the macroeconomic scenario underpinning the budgetary projections in the Draft Budgetary Plan appears to be slightly more favourable than the Commission's 2023 autumn forecast for 2024 (while it is in line for 2023). Italy complies with the requirement of Article 4(4) of Regulation (EU) No 473/2013, since the Draft Budgetary Plan is based on independently endorsed macroeconomic forecasts.

11. According to the Draft Budgetary Plan, Italy's general government deficit is projected to decrease to 4.3% of GDP in 2024 (from 5.3% in 2023)[11], remaining above 3% of GDP. This decrease is mainly driven by the reduced budgetary impact in 2024 of tax credits for the energy-efficient renovation of residential buildings, following a sizeable upward revision of their impact in 2023 due to a higher-than-expected take up. At the same time, the savings related to the phase-out of energy support measures are partly offset by new deficit-increasing discretionary measures included in the Draft Budgetary Plan. The general government debt-to-GDP ratio is set to decrease marginally to 140.1% at the end of 2024 (from 140.2% at the end of 2023). In turn, according to the Commission 2023 autumn forecast, Italy's general government deficit is projected to decrease to 4.4% of GDP in 2024 (from 5.3% in 2023), while the general government debt-to-GDP ratio is set to increase to 140.6% at the end of 2024 (from 139.8% at the end of 2023). The main differences between the two sets of debt projections reflect differences in nominal GDP growth both in 2023 and 2024.

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[9] Council Recommendation on the 2023 National Reform Programme of Italy and delivering a Council opinion on the 2023 Stability Programme of Italy, OJ C 312, 1.9.2023, p. 105.

[10] Report from the Commission, prepared in accordance with Article 126(3) of the Treaty on the Functioning of the European Union, 24.5.2023, COM(2023) 631 final.

[11] According to the Draft Budgetary Plan, one-off measures have a deficit-increasing impact of 0.2% of GDP in 2024 (0.0% of GDP in 2023). These one-off measures relate to various withholding taxes compensated by emergency interventions related to the floods which hit Italy in May 2023. This is in line with the assessment embodied in the Commission 2023 autumn forecast.

12. Based on the Commission's estimates, the fiscal stance[12] is projected to be contractionary by 1.6% of GDP in 2024, following a contractionary fiscal stance of 1.6% in 2023.

13. The Draft Budgetary Plan does not provide information on expenditure financed by non-repayable support ("grants") from the Recovery and Resilience Facility in 2024 nor on expenditure backed by loans from the Recovery and Resilience Facility. The Commission 2023 autumn forecast assumes expenditure financed by non-repayable financial support ("grants") from the Recovery and Resilience Facility amounting to 0.7% of GDP in 2023 and 0.6% of GDP in 2024. The Commission 2023 autumn forecast also assumes expenditure backed by loans from the Recovery and Resilience Facility, with a direct impact on the general government deficit and debt, amounting to 0.3% of GDP in 2023 and 1.4% in 2024.

14. According to the Commission forecast, taking into account the information contained in the Draft Budgetary Plan, the measures adopted to mitigate the economic and social impact of the increase in energy prices are planned to be wound down by the end of 2023, with a deficit-decreasing impact in 2024 of 1% of GDP. At the same time, the Draft Budgetary Plan includes several new and extended revenue and expenditure measures for 2024 that are not directly related to energy price developments. These include, on the revenue side, the prolongation to 2024 of cuts to social security contributions for those on low- and medium-incomes; a tax deduction for enterprises hiring employees on a permanent basis; and a first step of the general tax reform which (i) merges the first and second income tax brackets, (ii) increases the no-tax area and (iii) revises tax deductions on high incomes. On the expenditure side, the draft budget includes additional funds for the renewal of the 2022-2024 public wage contracts (including for the health sector), the prolongation to 2024 of some early retirement schemes (with some modifications), measures aimed at supporting natality, and additional funds for the health sector, local authorities and the areas hit by floods in May 2023. These measures are partly compensated by expenditure savings together with a limited spending review for public administrations, as well as some small revenue increasing measures. The aggregate cost of these measures is estimated by the Commission at 0.7% of GDP in 2024 and most of them are expected to have a permanent effect.

15. On 14 July 2023, the Council recommended that Italy ensure a prudent fiscal policy, in particular by limiting the nominal increase in nationally financed net primary expenditure[13] in 2024 to not more than 1.3%. According to the Commission 2023 autumn forecast, Italy's net nationally financed primary expenditure is projected to increase by 0.9% in 2024[14], which is below the recommended maximum growth rate.

[12] The fiscal stance is measured as the change in general government primary expenditure, net of the incremental budgetary impact of discretionary revenue measures, excluding one-off and cyclical unemployment expenditure, but including expenditure financed by non-repayable support (grants) from the Recovery and Resilience Facility and other EU funds, relative to medium-term (10-year) average potential GDP growth rate, expressed as a ratio to nominal GDP.

[13] Net primary expenditure is defined as nationally financed expenditure net of discretionary revenues measures and excluding interest expenditure as well as cyclical unemployment expenditure.

[14] This takes into account 0.0% of GDP one-off measures in 2024 and 0.2% of GDP in 2023, both relating to various withholding taxes compensated by emergency interventions related to the floods which hit Italy in May 2023. On 14 July 2023, the Council also referred to the devastating floods that hit Italy in May 2023 and agreed that the cost of direct emergency support related to those floods would be taken into account in subsequent assessments of compliance with its fiscal recommendations and would, in principle, be considered as one-off and temporary measures.

However, current estimates of net nationally financed primary expenditure in 2023 are higher than expected at the time of the recommendation (by 0.8% of GDP). This is mainly driven by two factors concerning the tax credits for energy-efficiency renovation of residential buildings: (i) the Commission 2023 autumn forecast revised upwards their impact on the 2023 deficit following the higher-than-expected take up and reflecting information in the Draft Budgetary Plan; and (ii) legislative amendments changing the nature of the tax credits[15], which imply that they have no expected impact on the 2024 expenditure. Therefore, as the recommendation for 2024 was formulated as a growth rate, the assessment of compliance also takes into account the base effect from 2023. If net expenditure in 2023 had been the same as expected at the time of the recommendation, the resulting growth rate of net expenditure in 2024 would be above the recommended growth rate, by 0.6% of GDP. Therefore, net nationally financed primary expenditure is assessed as not being fully in line with the recommendation.

16. Moreover, the Council recommended that Italy take action to wind down the emergency energy support measures in force, using the related savings to reduce the government deficit, as soon as possible in 2023 and 2024. The Council further specified that, should renewed energy price increases necessitate new or continued support measures, Italy should ensure that these were targeted at protecting vulnerable households and firms, fiscally affordable, and preserve incentives for energy savings. According to the Commission 2023 autumn forecast, the net budgetary cost[16] of energy support measures is projected at 1.0% of GDP in 2023 and 0.0% in 2024 and 2025. If the related savings were used to reduce the government deficit, as recommended by the Council, these projections would imply a fiscal adjustment of 1% of GDP in 2024, whereas net nationally financed primary expenditure[17] provides a contractionary contribution to the fiscal stance of 1.1% of GDP in that year. The latter is driven by the contractionary contribution of other capital expenditure of 1.6% of GDP, which is mainly related to the discontinuation of expenditure on tax credits for the energy-efficient renovation of residential buildings, down from 1.8% of GDP in 2023 to 0% in 2024. At the same time, the contribution of net nationally financed current primary expenditure to the fiscal stance, which is affected by the phase-out of energy support measures, is projected to be expansionary by 0.1% of GDP, pointing to the full use of the 1% of GDP savings from those measures for policies increasing net current spending in 2024.

    The energy support measures are projected to be wound down as soon as possible in 2023 and 2024. This is in line with what was recommended by the Council. However, the related savings are not projected to be fully used to reduce the government deficit. This risks being not fully in line with the Council recommendation.

17. In addition, the Council recommended that Italy preserve nationally financed public investment and ensure the effective absorption of Recovery and Resilience Facility

[15] Eurostat advice of September 2023: [IT+Advice+on+recording+of+2023+Superbonus.pdf (europa.eu)](IT+Advice+on+recording+of+2023+Superbonus.pdf).

[16] The figure represents the level of the annual budgetary cost of those measures, including revenue and expenditure and, where applicable, net of the revenue from taxes on windfall profits of energy suppliers.

[17] This contribution is measured as the change in general government primary expenditure, net of the incremental budgetary impact of discretionary revenue measures, excluding one-off and cyclical unemployment expenditure, as well as expenditure financed by non-repayable support (grants) from the Recovery and Resilience Facility and other EU funds, relative to the medium-term (10-year) average potential nominal GDP growth rate, expressed as a ratio to nominal GDP.

grants and other EU funds, in particular to foster the green and digital transitions. According to the Commission 2023 autumn forecast, nationally financed public investment is projected to increase to 3.0% of GDP in 2024 (from 2.6% of GDP in 2023) and, therefore, it is expected to be preserved. This is in line with what was recommended by the Council. In turn, public expenditure financed from revenues from EU funds, including Recovery and Resilience Facility grants, is expected to decrease to 0.7% of GDP in 2024 (from 1.2% of GDP in 2023), also driven by the end of the ReactEU programme in 2023.

18. Furthermore, on 14 July 2023, the Council also recommended that, for the period beyond 2024, Italy continue to pursue a medium-term fiscal strategy of gradual and sustainable consolidation, combined with investments and reforms conducive to higher sustainable growth, to achieve a prudent medium-term fiscal position. The Draft Budgetary Plan includes medium-term budgetary projections until 2026. The general government deficit is projected to decrease gradually to 3.6% of GDP in 2025 and 2.9% in 2026. By contrast, in the 2023 Stability Programme the general government deficit was planned to not exceed 3% of GDP from 2025. In turn, the general government debt is projected to decrease marginally, to 139.9% of GDP in 2025 and 139.6% in 2026. These projections are based on the control of public expenditure dynamics, along with an increase in its quality underpinned by spending reviews, while preserving the investments needed for the green and digital transitions, including those funded by the Recovery and Resilience Facility and other EU funds. The debt-to-GDP ratio projections incorporate a debt-increasing stock-flow adjustment, driven by the delayed impact of housing “payable” tax credits on debt. At the same time, a prudent debt management and the planned programme of public assets disposals, the details of which are not included in the Draft Budgetary Plan, are expected to support the decline of the debt-to-GDP ratio.

19. Finally, on 14 July 2023, the Council also recommended Italy to further reduce taxes on labour and make the tax system more efficient by adopting and duly implementing the enabling law on tax reform while preserving the progressivity of the tax system and improving fairness, in particular by streamlining and reducing tax expenditures, including VAT and environmentally harmful subsidies, and by reducing the complexity of the tax code. The Council also recommended Italy to align the cadastral values with current market values. The Draft Budgetary Plan illustrates the main objectives of the enabling law on the reform of the taxation system approved by Parliament on 21 August 2023. Among others, the enabling law has the stated aims of stimulating economic growth and natality, through increased efficiency of the tax system and a reduced tax burden, of simplifying the tax system, reducing its distortions and complexity, of fighting tax evasion and tax avoidance more effectively and of encouraging tax compliance. The enabling law envisages a redesign of corporate taxation to set lower tax rates on reinvested profits and on new hires and the progressive phase out of the regional tax on productive activities. It also contains specific guiding principles and criteria for the rationalisation of micro-taxes and to reduce the complexity of the current system. In the area of excise duties and other indirect taxes on production and consumption, the enabling law provides for the revision of energy taxation, with the aim of promoting the reduction of greenhouse gas emissions and support the production of electricity from renewable sources. Among the main measures contained in the enabling law, the Draft Budgetary Plan mentions the review and gradual reduction of personal income tax, also through the reduction of tax rates and brackets, while preserving progressivity and promoting horizontal equity. While implementing decrees will need to be

adopted within 24 months of its adoption, in October 2023 the government adopted a legislative decree which includes a first implementing step in the reduction of income taxation for low- and medium-income earners, by merging the first and second tax brackets together at the lower tax rate and revising tax deductions on incomes above EUR 50,000, which is at the moment legislated only for the year 2024. These interventions, including the revision of tax deductions, are quite limited in scope and do not address the erosion of the tax base, which was further reduced last year with the extension of flat-rate tax schemes for the self-employed. The legislative decree of October also provides for the abolition of the possibility for companies to deduct part of the notional return on new injections of equity capital from taxable income (ACE), which is expected to increase the cost of capital and the debt bias in corporate financing. Overall, frequent changes in tax policy increase uncertainty in the economy, making the tax system more complex and increasing the burden on compliant firms and households.

20. According to the Commission's forecast, the growth of net nationally financed primary expenditure is projected to respect the recommended maximum growth rate in 2024. However, if net expenditure in 2023 had been the same as expected at the time of the recommendation, the resulting growth rate of net expenditure in 2024 would be above the recommended one.

According to the Commission 2023 autumn forecast, and taking into consideration the information included in Italy's Draft Budgetary Plan, the emergency energy support measures are expected to be wound down by the end of 2023. However, the related savings are not projected to be fully used to reduce the general government deficit in 2024.

At the same time, Italy is expected to preserve nationally financed public investment. Italy should also continue to ensure the effective absorption of Recovery and Resilience Facility grants and other EU funds.

Overall, the Commission is of the opinion that the updated Draft Budgetary Plan of Italy is not fully in line with the Council Recommendation of 14 July 2023. Therefore, the Commission invites Italy to stand ready to take the necessary measures within the national budgetary process to ensure that fiscal policy in 2024 will be in line with the Council Recommendation of 14 July 2023.

Moreover, the Commission projects Italy's headline budget deficit at 4.4% of GDP in 2024, above the Treaty reference value of 3% of GDP, and the government debt ratio at 140.6% of GDP in 2024, above the Treaty reference value of 60% of GDP but 6.5 percentage points below the ratio at end-2021.

The Commission is also of the opinion that Italy has made limited progress with regard to the structural elements of the fiscal recommendations made by the Council on 14 July 2023, and thus invites the Italian authorities to accelerate progress.

A comprehensive description of progress made with the implementation of the Council's country-specific recommendations will be included in the 2024 Country Report and assessed in the context of the Council's country-specific recommendations to be recommended by the Commission in spring 2024.

Table: Key macroeconomic and fiscal figures

	2022	2023		2024	
	Outturn	DBP	COM	DBP	COM
Real GDP (% change)	3.7	0.8	0.7	1.2	0.9
HICP inflation (%; annual average)	8.7	6.1	6.1	2.5	2.7
General government balance (% of GDP)	-8.0	-5.3	-5.3	-4.3	-4.4
Primary balance (% of GDP)	-3.8	-1.5	-1.4	-0.2	-0.2
General government gross debt (% of GDP; at end-year)	141.7	140.2	139.8	140.1	140.6
	COM	COM		COM	
Fiscal stance (*) (% of GDP)	-3.5	1.6		1.6	
Fiscal adjustment (**) (% of GDP)	-3.1	2.0		1.1	
Change in total net budgetary cost of energy support measures (***) (% of GDP)	2.1	-1.4		-1.0	
Growth in net nationally financed primary expenditure (% change) (A)				0.9	
Recommended maximum growth rate of net nationally financed primary expenditure (****) (% change) (B)				1.3	
Difference from recommended growth in net nationally financed primary expenditure (pps.) (B-A)				0.5	
Impact on fiscal adjustment of deviation in net nationally financed primary expenditure compared with the Council recommendation (*****) (% of GDP)				n.a.	

Notes:

(*) Change in general government primary expenditure, net of the incremental budgetary impact of discretionary revenue measures (and COVID-19 pandemic-related temporary emergency measures), excluding one-off and cyclical unemployment expenditure, but including expenditure financed by non-repayable support (grants) from the Recovery and Resilience Facility and other EU funds, relative to the medium-term (10-year) average potential nominal GDP growth rate. A negative (positive) sign indicates an excess (a shortfall) of net primary expenditure growth over medium-term potential GDP growth, corresponding to an expansionary (a contractionary) fiscal stance.

(**) Change in general government primary expenditure, net of the incremental budgetary impact of discretionary revenue measures (and COVID-19 pandemic-related temporary emergency measures), excluding one-off and cyclical unemployment expenditure, as well as expenditure financed by non-repayable support (grants) from the Recovery and Resilience Facility and other EU funds, relative to the medium-term (10-year) average potential nominal GDP growth rate. A negative (positive) sign indicates an excess (a shortfall) of net nationally financed primary expenditure growth over medium-term potential GDP growth, corresponding to an expansionary (a contractionary) fiscal adjustment.

(***) Energy support measures less revenue from new taxes and levies on windfall profits by energy producers.

(****) According to the Council Recommendation 'on the 2023 National Reform Programme of Ialy and delivering a Council opinion on the 2023 Stability Programme of Italy', (OJ C 312, 1.9.2023, p. 105).

(*****) Excess in growth of net nationally financed primary expenditure over the recommended maximum growth rate, expressed as a percentage of GDP.

'DBP' 2024 Draft Budgetary Plan, 'COM' Commission 2023 autumn forecast.

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