

CareEdge Global assigns Long Term Foreign Currency Rating of BBB (Unsolicited) to Republic of Italy

Credit Profile

Italy's credit profile is underpinned by large economic size and consistent surplus in its current account balance, aided by strong exports growth. Also, Italy benefits from being a part of European monetary union and is one of the largest recipients of funding support from European Union through National Recovery and Resilience Plan (NRRP). However, these positives are somewhat offset by Italy's low economic growth, high government debt, and lack of reforms. Moreover, not only rapidly ageing population but also shrinking working age population is a key concern for future growth outlook.

Going forward, Italy's ability to reduce public indebtedness remains critical, given that the adoption of defined contribution scheme, away from defined-benefit pension scheme, has been very gradual. Further, there are predefined quantitative and qualitative targets for structural reforms to enable continued access to NRRP funds. Meeting these targets in a timely manner also remains an important monitorable.

Strengths

- Large and diverse economy.
- High GDP per capita
- Current account surplus country
- Member of European Monetary Union with access to EU funds

Weaknesses

- High government debt burden
- Slow economic growth
- High fiscal deficit and net social benefits
- Limited progress on reforms

Key Monitorables

- Ability to reduce public indebtedness remains critical
- Meeting targets of EU Recovery and Resilience Plan in a timely manner

Key Rating Drivers

Economic Structure & Resilience

Italy's economy is characterized by its large economic size (USD 2.2 trillion in 2023) and high GDP per capita (USD 45099 in 2023), supported by a substantial manufacturing base (accounting for 16% of economy) and an established export hub (exports of goods and services stood at 35% of GDP in 2023). However, Italy faces challenges of low economic growth (5-year annual average of just 0.95% during 2019-2023) arising from low productivity and unfavorable demographic profile. This trend of weak growth is

expected to continue in the medium term too with constrains from the country's inability to implement bold reforms, like addressing labor market rigidities, improving public sector inefficiencies, and adhering to fiscal consolidation.

In order to revive demand, the government introduced a Superbonus scheme in 2020 providing tax credits worth 110% of the home renovations costs to enhance energy efficiency, which pushed up the investment demand post pandemic. Gradual withdrawal of the scheme is expected to partially offset by investments funded through NRRP.

Fiscal Strength

Italy has significantly high public debt, at 137% of GDP in 2023, which is estimated to remain high in medium term too. Policy measures in recent years to mitigate rise in energy prices and provide tax credits under super-bonus scheme, have all added to a widening fiscal deficit. Italy had the highest fiscal deficit of 7.4% in 2023 in Eurozone. Further, high net social benefits (~11% of GDP in 2023) also add to the fiscal challenges.

These challenges are partially offset by low borrowing costs as compared to similarly assessed peers, and relatively longer maturity of debt at an average of 7 years. Additionally, the European Commission has approved grants and funds under the NRRP to Italy worth more than EUR194 (~10.3% of GDP) billion over 2021-2027 supporting structural and investment reforms. Under the NRRP, the funds are released on the basis of achieving the milestones. Spending of the disbursed amount started at a slow pace, however picked up in the second half of 2023. Until Dec 2023, Italy has already received EUR100 billion. Progress in NRRP is a key monitorable going ahead.

External Position & Linkages

Italy has Euro as its currency, with a free-floating exchange regime and enjoys a reserve currency status. Italy's exports mix comprises high value products like luxury goods, textiles, non-electronic machinery, and pharmaceuticals, which helps in maintaining a comfortable and consistent current account balance. The annual current account surplus averaged 1.65% of GDP between 2019-2023 and is expected to maintain a surplus in the medium term too. Italy also has a positive international position of 7.1% in 2023.

These strengths are balanced by low, though positive, net Foreign Direct Investment inflows and a high external debt at 124.4% of GDP in 2023, of which about half of the debt is of government and regional central bank 40% of the external debt is short-term reflecting in high external funding ratio at 2.57 in 2023.

Monetary & Financial Stability

Italy is a core member of the European monetary union. Italy's average HICP inflation declined to 5.9% y-o-y in 2023 and is expected to moderate near 2% levels in 2024. Italy also benefits from having liquidity and inter banking funding support via European Central Bank.

Italy's banking sector has slightly higher non-performing loans at 2.7% of total loans in 2023, compared to the EU average of 2% in 2023, though much lower than its peak of 16.5% in 2014. However, in order to build a buffer, the regional central bank (Bank of Italy) has raised capital requirements over the minimum reserve

ratios for the banks. Going forward, higher delinquency rates due to economic uncertainty and higher interest rates could pose a risk.

Institutions & Quality of Governance

Italy ranks well with respect to quality of governance and accountability. However, Italy's inability to reduce fiscal deficits and meet the targets under the ambitious NRRP, for instance implementation of public investments was one-quarter lower than initially anticipated in 2022, reflects low government effectiveness. Frequent changes in the political leadership, 70 governments in 77 years, has also resulted in slow policy reforms.

Italy – Select Indicators									
	Unit	2018	2019	2020	2021	2022	2023	2024 F	2025 F
Economic Indicators									
Nominal GDP	USD Billion	2,093	2,012	1,896	2,156	2,069	2,256	2,328	2,390
GDP Per Capita (Constant-PPP)	USD	42,593	42,885	39,151	42,695	44,552	45,099	45,443	45,836
Real GDP Growth	%	0.9	0.5	-9.0	8.3	4.0	0.9	0.7	0.9
GFCF/ GDP	%	17.8	18.0	18.0	20.4	21.7	21.2	-	-
Gross Domestic Savings/ GDP	%	20.9	21.6	21.3	23.9	21.5	22.3	-	-
Exports (G&S)/GDP	%	31.4	31.6	29.4	32.1	36.5	35.1	-	-
Working-Age (15-64) Population (% Share in Total)	%	64.0	63.9	63.8	63.7	63.5	63.3	63.1	62.9
Old-Age (65+) Population (% Share in Total)	%	22.8	23.1	23.4	23.7	24.1	24.5	24.9	25.4
Fiscal Indicators – General Government									
Fiscal Balance/ GDP	%	-2.2	-1.5	-9.4	-8.7	-8.6	-7.4	-4.6	-4.1
Revenue/ GDP	%	46.2	47.0	47.4	47.5	47.7	47.8	46.3	47.1
Expenditure/ GDP	%	48.4	48.5	56.8	56.3	56.3	55.0	50.9	50.3
GG Gross Debt/ GDP	%	134.5	134.2	154.9	147.1	140.5	137.3	139.1	140.6
GG External Debt (by Creditor)/ GG Gross Debt	%	30.2	35.5	33.9	32.0	26.2	28.0	-	-
Interest/ Revenue	%	7.9	7.2	7.3	7.4	8.9	7.9	-	-
External Indicators									
Current Account Balance/ GDP	%	2.6	3.3	3.9	2.4	-1.5	0.5	0.8	1.3
FDI, Net Inflows/ GDP	%	2.11	1.78	-0.90	1.15	3.03	1.25	-	-
Outstanding FII Liabilities/ GDP	%	62.9	76.9	87.7	72.3	58.6	63.9	-	-
NIIP/ GDP	%	-5.0	-2.0	1.0	7.2	4.8	7.1	-	-
Foreign Exchange Reserves	USD Billion	152.5	175.3	211.0	227.7	225.2	247.5	-	-
Import Cover	Months	3.0	3.7	5.2	4.2	3.4	3.9	-	-
External Debt/GDP	%	116.7	125.1	150.6	129.6	128.4	124.4	-	-
Monetary and Financial Indicators									
HICP Inflation	%	1.2	0.6	-0.1	1.9	8.7	5.9	-	-
Exchange Rate (Average)	LC per USD	0.85	0.89	0.88	0.85	0.95	0.93	-	-
Non-Performing Loans/ Total Gross Loans	%	8.4	6.7	4.4	3.3	2.8	2.7	-	-
Private debt, loans and debt securities/ GDP	%	110.4	109.4	122.2	116.9	110.3	-	-	-

Sources: International Monetary Fund, World Bank, Bank for International Settlements, National Sources, CareEdge Global

Note: F - Forecast; PPP – Purchasing Power Parity; GFCF – Gross Fixed Capital Formation; Exports (G&S) – Exports of Goods and Services; GG – General Government; FDI – Foreign Direct Investment; FII – Foreign Institutional Investment; NIIP – Net International Investment Position; Data refers to fiscal/calendar year and actual/estimate as reported by the source; Where general government data is unavailable, central government data is used; Latest available data for 2023

Rating History

Instrument	Type	Rating	Date
Issuer Rating	Long Term Foreign Currency (Unsolicited)	BBB	October 3, 2024

Analytical Contacts

Shobana Krishnan

C-shobana.krishnan@careedge.in

Akanksha Bhende

akanksha.bhende@careedge.in

Kiran Kavala

kiran.kavala@careedgeglobal.com

Media Contact

Mradul Mishra

mradul.mishra@careedge.in

Criteria Applied

CareEdge Sovereign Rating Methodology

About Us

CareEdge Global IFSC Limited (CareEdge Global) is a full-service Credit Rating Agency (CRA) with a mission of **Empowering Global Capital Market Participants Through Unrivalled Insights and Expertise**. As the first CRA registered and authorized by the International Financial Services Centres Authority (India), CareEdge Global is uniquely positioned to provide comprehensive ratings on a global scale. A part of the CareEdge Group, which is a knowledge-based analytical organisation offering a wide range of services in Credit Ratings, Analytics, Consulting, and Sustainability. Established in 1993, our parent company, **CARE Ratings Limited (CareEdge Ratings)**, stands as India's second-largest rating agency.

Disclaimer

This disclaimer applies to each credit rating report and/ or credit rating rationale ('report') that is provided by CareEdge Global IFSC Limited ('CareEdge Global').

Ratings from CareEdge Global are statements of opinion as of the date they are expressed and not statements of fact or recommendations to purchase, hold or sell any securities/ instruments or to make any investment decisions. The report is not a solicitation of any kind to enter into any deal or transaction with the entity to which the report pertains. Any opinions expressed here are in good faith, are subject to change without notice, and are only current as of the stated date of their issue. CareEdge Global assumes no obligation to update its opinions following publication in any form or format although CareEdge Global may disseminate its opinions and analysis. The rating contained in the report is not a substitute for the skill, judgment and experience of the investor, user, its management, employees, advisors and/ or clients when making investment or other business decisions. The recipients of the report should rely on their own judgment and take their own professional advice before acting on the report in any way. Therefore, the report is not intended to and does not constitute an investment advice. The report should not be the sole or primary basis for any investment decision. CareEdge Global is not responsible for any errors and states that it has no financial liability whatsoever to the users of the ratings of CareEdge Global. CareEdge Global does not act as a fiduciary by providing the rating.

Any unsolicited ratings assigned by CareEdge Global are based on publicly available information as CareEdge Global may or may not have access to documents / information or participation from management of such issuers. While CareEdge Global has obtained information from sources it believes to be reliable, CareEdge Global does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives and/ or relies on in its reports. CareEdge Global ratings are subject to a periodic review, which may lead to revision in ratings. CareEdge Global has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process. CareEdge Global has in place a ratings code of conduct and policies for managing conflict of interest.

Neither CareEdge Global nor its affiliates, third-party providers, as well as their directors, officers, shareholders, employees or agents guarantee the accuracy, completeness or adequacy of the report, and shall not have any liability for any errors, omissions or interruptions therein, regardless of the cause, or for the results obtained from the use of any part of the report. CareEdge Global DISCLAIMS ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING BUT NOT LIMITED TO ANY WARRANTIES OF MERCHANTABILITY, SUITABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE. In no event shall any CareEdge Global or its associated entities or persons be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees or losses (including, without limitation, lost income or lost profits and opportunity costs) in connection with any use of any part of the report even if advised of the possibility of such damages.

This report does not constitute an offer of services. This report is for use in the jurisdiction of IFSCA, GIFT City in Gandhinagar. Without limiting the generality of the foregoing, nothing in the report is to be construed as CareEdge Global providing or intending to provide any services in jurisdictions where CareEdge Global does not have the necessary licenses and/ or registration to carry out its business activities referred to above. Access or use of this report does not create a client relationship between CareEdge Global and the user.

For latest rating information on any instrument of any company rated by CareEdge Global, you may visit our website www.careedgeglobal.com.

This report should not be reproduced or redistributed to any other person or in any form without prior written consent from CareEdge Global.

All rights reserved @CareEdge Global IFSC Limited.

CareEdge Global IFSC Limited
(A subsidiary of CARE Ratings Ltd.)
Unit No. 06, 11 T-2, Block-11, GIFT SEZ, Gift City, Gandhi Nagar, Gujarat – 382355
CIN-U66190GJ2024PLC151103