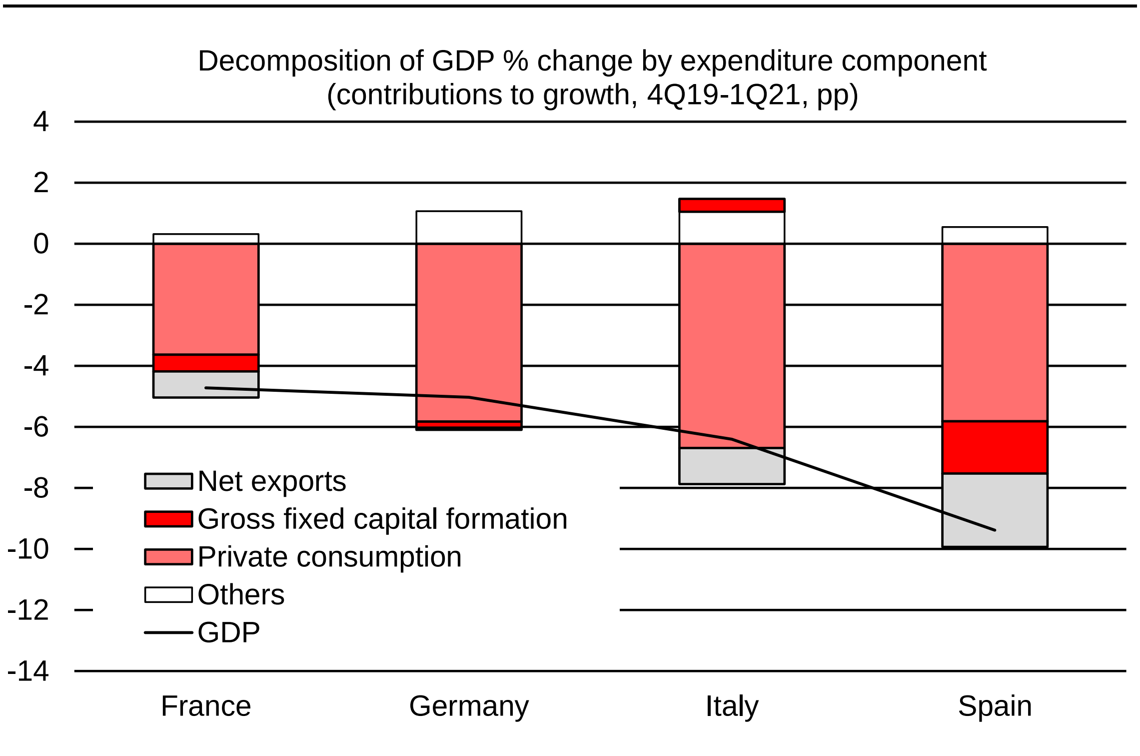
Italy: Household spending will be key to recovering pre-crisis GDP levels



Source: Eurostat, UniCredit Research

- This week, Istat published its updated estimate and details of Italy's 1Q21 GDP. The good news is that GDP growth was revised upwards to 0.1% qoq, compared to -0.4% in the flash estimate. At the end of 1Q21, real GDP was 6.4% below its pre-pandemic level in 4Q19, with Italy between France (-4.7%) and Germany (-5.0%) on the one hand and Spain (-9.4%) on the other.

- Our *Chart of the Week* breaks down the GDP loss from the pre-crisis peaks in the four largest eurozone countries[1]. The reduction of economic activity in Italy can mainly be explained by a collapse in private consumption, which declined much more than overall GDP. A significant contraction in private consumption is a common feature of this crisis and it is related to the fact that household spending on services was significantly hampered by COVID-19-related restrictions, voluntary social distancing and precautionary behavior. The relatively smaller negative contribution of private consumption to GDP loss in France, compared to Italy, can be explained by the fact that, despite the savings rate significantly exceeding that of the pre-crisis period in both countries, French households benefitted from an improvement in their gross disposable income, which contracted in Italy, albeit moderately. Household disposable income fell much more in Spain, but here households reduced their savings rate in both 3Q20 and 4Q20, somewhat cushioning the decline in their spending.

- The chart also shows that real GDP in Italy was dragged down by a negative contribution from net exports. This was mainly due to a decline in exports of services as a result of the restrictions on tourism. Exports of goods held up relatively well. However, given the comparatively larger weighting of exports of goods in total Italian exports (in volume terms), the impact of the fall in exports of services was much lower than, for example, in Spain, which has one of the highest weightings of exports of services among the four countries. On the other hand, investments recovered quickly from the impact of the COVID-19 crisis, with Italy in particular (but also Germany) benefitting from good performance of construction investment, as opposed to France and Spain.

[1] Others" captures the contribution of public consumption and inventories.

- Our key takeaway is that the recovery of pre-crisis GDP levels will largely hinge on the speed with which households boost their spending now that restrictions have gradually been eased thanks to the progress of the vaccination campaign and the warmer weather. In Italy, the strong improvement in consumer confidence in May – the indicator is almost back to its February 2020 level – is surely an encouraging sign and might prompt households to start reducing some of their accumulated savings. However, as fiscal support for incomes will gradually fade over the coming quarters, a recovery in household income will greatly depend on a recovery in labor compensation and thus on a recovery in employment.

Dr. Loredana Maria Federico,
Chief Italian Economist
(UniCredit Bank, Milan)
+39 02 8862-0534
loredanamaria.federico@unicredit.eu

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UniCredit Research* Macro Research


Erik F. Nielsen
Group Chief Economist
Global Head of CIB Research
+44 207 826-1765
erik.nielsen@unicredit.eu


Dr. Ingo Heimig
Head of Research Operations
& Regulatory Controls
+49 89 378-13952
ingo.heimig@unicredit.de

Head of Macro Research


Marco Valli
Head of Macro Research
Chief European Economist
+39 02 8862-0537
marco.valli@unicredit.eu

European Economics Research


Dr. Andreas Rees
Chief German Economist
+49 69 2717-2074
andreas.rees@unicredit.de


Dr. Loredana Federico
Chief Italian Economist
+39 02 8862-0534
loredanamaria.federico@unicredit.eu


Stefan Bruckbauer
Chief Austrian Economist
+43 50505-41951
stefan.bruckbauer@unicreditgroup.at


Tullia Bucco
Economist
+39 02 8862-0532
tullia.bucco@unicredit.eu


Edoardo Campanella
Economist
+39 02 8862-0522
edoardo.campanella@unicredit.eu


Walter Pudschedl
Economist
+43 50505-41957
walter.pudschedl@unicreditgroup.at


Chiara Silvestre
Economist
chiara.silvestre@unicredit.eu


Dr. Thomas Strobel
Economist
+49 89 378-13013
thomas.strobel@unicredit.de

International Economics Research


Daniel Vernazza, Ph.D.
Chief International Economist
+44 207 826-7805
daniel.vernazza@unicredit.eu

EEMEA Economics Research


Dan Bucşa
Chief CEE Economist
+44 207 826-7954
dan.bucsa@unicredit.eu


Gökçe Çelik
Senior CEE Economist
+44 207 826-6077
gokce.celik@unicredit.eu


Mauro Giorgio Marrano
Senior CEE Economist
+43 50505-82712
mauro.giorgiomarrano@unicredit.de


Artem Arkhipov
Head, Macroeconomic Analysis
and Research, Russia
+7 495 258-7258
artem.arkhipov@unicredit.ru


Hrvoje Dolenec
Chief Economist, Croatia
+385 1 6006-678
hrvoje.dolenec@unicreditgroup.zaba.hr


Dr. Ágnes Halász
Chief Economist, Head, Economics and
Strategic Analysis, Hungary
+36 1 301-1907
agnes.halasz@unicreditgroup.hu


Ľubomír Koršňák
Chief Economist, Slovakia
+421 2 4950 2427
lubomir.korsnak@unicreditgroup.sk


Anca Maria Negrescu
Senior Economist, Romania
+40 21 200-1377
anca.negrescu@unicredit.ro


Kristofor Pavlov
Chief Economist, Bulgaria
+359 2 923-2192
kristofor.pavlov@unicreditgroup.bg


Pavel Sobíšek
Chief Economist, Czech Republic
+420 955 960-716
pavel.sobisek@unicreditgroup.cz

UniCredit Research, Corporate & Investment Banking, UniCredit Bank AG, Am Eisbach 4, D-80538 Munich, globalresearch@unicredit.de
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