

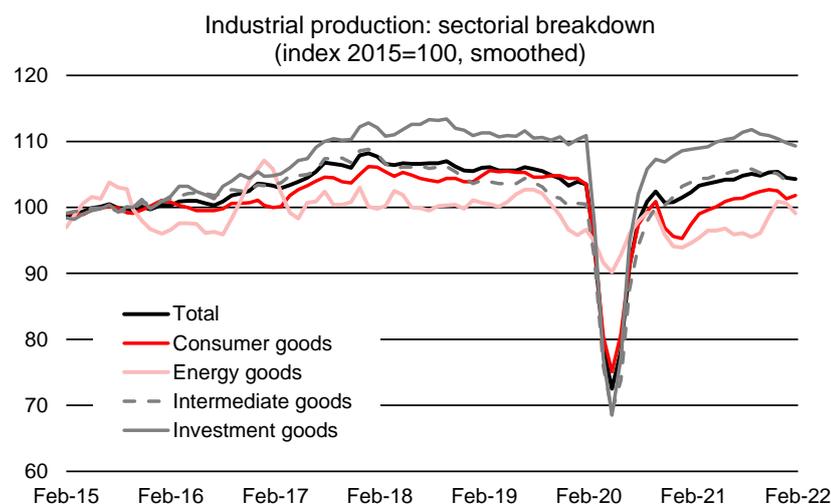
## Italy's GDP dragged down by high energy costs and COVID-19 restrictions

- According to the preliminary estimate, Italy's real GDP declined by 0.2% qoq in 1Q22, showing a deterioration compared to 4Q21, when it rose by 0.7% qoq (revised slightly upward compared to 0.6% previously). Real GDP remains below its pre-pandemic level of 4Q19 (-0.4%). Today's outcome seems to hint at some resilience of industry in March, after the start of the Russia-Ukraine conflict.
- The weak GDP reading in 1Q22 was mainly triggered by a stabilization in activity in industry (including construction) and a decline in services. For the former, this probably reflects some weakness in manufacturing output, which has been affected by high energy costs, and the intensification of supply-side constraints, while construction activity held up relatively well, also thanks to fiscal support. The decline in services activity was probably largely due to the spread of the Omicron variant, which was already weighing, for example, on food and accommodation service activity in 4Q21.
- Net exports were a drag on economic activity, while domestic demand (including inventories) provided a positive contribution. When more details are made available at the end of May, we expect to see a quarterly contraction in private consumption and a slowdown in fixed investment, as COVID-19 restrictions limited spending on services and high energy costs started to dent household purchasing power and firms' profits. The household savings rate stopped declining in 4Q21 (close to 13%), remaining well above its pre-pandemic level. Sharp deterioration in consumer sentiment induced by the Russia-Ukraine conflict might have further discouraged households' propensity to consume, despite the availability of large excess savings. A worsening of firms' profit margins and liquidity had already started at the end of 2021 and is likely to have continued in 1Q22.
- Looking ahead, we expect another weak reading in 2Q22, as the Russia-Ukraine crisis will take its toll on business activity and demand, as suggested by the latest confidence indicators. Services activity is likely to partly benefit from a lower Omicron-variant infection rate and the reopening of the economy that started at the end of 1Q22, which has already supported tourism activity in April. A constructive picture remains dependent on a stabilization in market prices for natural gas. As seen recently, this trend might swiftly shift as a result of negative news regarding oil and gas supply, increasing uncertainty.

In greater detail:

Industrial production (excluding construction) was down by 1.6% in the period January-February, compared to 4Q21. The output reduction was widespread among almost all sectors (including energy).

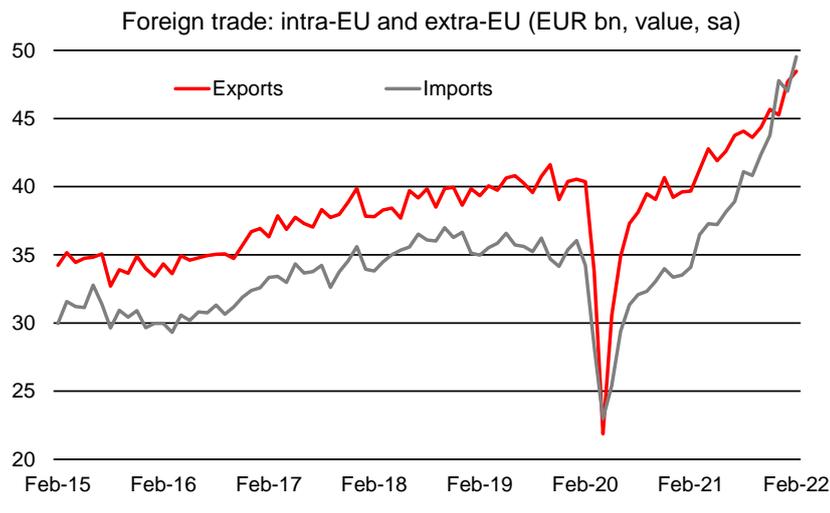
### CHART 1: CONTRACTION IN INDUSTRIAL PRODUCTION DUE TO HIGH ENERGY COSTS



Source: Istat, UniCredit Research

Monthly data on foreign trade mainly reflect a surge in imports that began in 2H21, driven by price rather than quantity effects. Despite a good performance by exports (in volume) to both EU and non-EU countries, their increase was more than offset by a stronger increase in imports (in volume), which was probably also related to higher net demand for energy products at the beginning of the year.

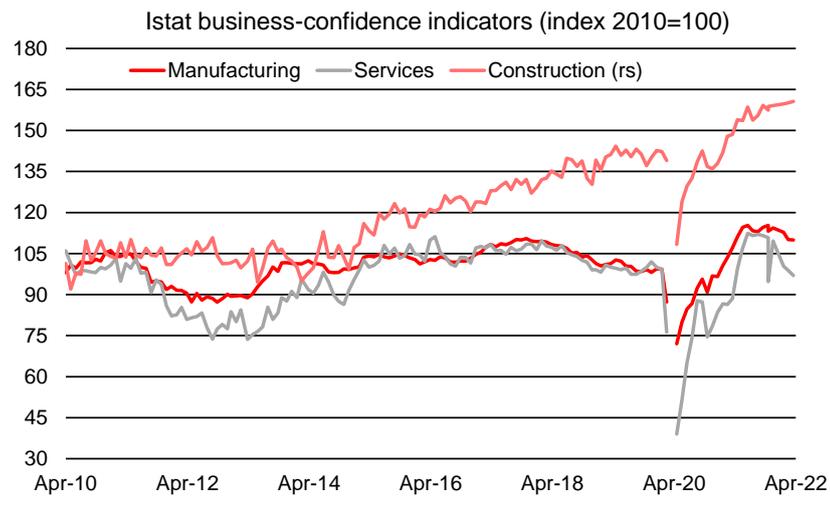
**CHART 2: FOREIGN TRADE HAS BEEN MAINLY AFFECTED BY STRONG PRICE CHANGES**



Source: Istat, UniCredit Research

The manufacturing-confidence indicator broadly stabilized in April at its lowest level in about one year, while the service-confidence indicator declined further, mainly as a result of firms' concerns about both current order books and business activity, while there was improvement in opinions regarding future order books. Sentiment of construction firms has remained upbeat.

**CHART 3: BUSINESS-CONFIDENCE INDICATORS COME UNDER CLOSE SCRUTINY**



Source: Istat, UniCredit Research

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