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EY Italian Macroeconomic Bulletin

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Index

Executive summary

- According to the latest projections from the International Monetary Fund (IMF), global economic growth is expected to reach 2.8% in 2025 and 3.0% in 2026. Meanwhile, global inflation is projected to ease from 5.7% in 2024 to 3.6% by 2026.
- Major forecasting institutions have revised their growth projections downward, reflecting the increasingly complex global geopolitical and economic landscape. Uncertainty surrounding U.S. trade policy and potential retaliatory measures by other economies may further dampen international trade. Although commodity prices have begun to decline, they remain elevated compared to pre-pandemic levels.
- In the Eurozone, economic growth is projected at 0.9% for 2024, followed by a slight deceleration to 0.8% in 2025, and a subsequent recovery to 1.2% in 2026. Trends in the industrial and services sectors remain mixed, with major economies exhibiting divergent performance patterns.
- At its June meeting, the European Central Bank (ECB) reduced its key policy interest rate by 25 basis points, bringing it to 2.0%. This move supports economic activity across member states amid inflation figures approaching the ECB's price stability target (with inflation averaging2.2% between February and April). However, downside risks persist, primarily due to ongoing geopolitical tensions, industrial sector challenges, and elevated public debt levels relative to the pre-pandemic period.
- The evolving trade policies of the new U.S. administration and responses from other countries continue to introduce uncertainty for the global and Eurozone economies. The EY Economic Advisory team estimates that the cumulative effect of these policies could reduce Eurozone GDP by 0.7 percentage points at their peak impact in 2027. Sectoral impacts are expected to vary significantly over the long term.
- In Italy, industrial production recorded positive growth in April for the first time after twenty-six consecutive months of contraction. Nevertheless, overall economic dynamics remain subdued, with limited momentum in the services sector. Inflation reached 1.7% in May, driven primarily by persistent core inflation and the waning deflationary effect of energy prices. The labour market remains solid, supporting real wage growth and consumer spending. However, real hourly wages remain below 2021 levels, diverging from the growth observed in the previous quarter.
- In evaluating the potential impact of new tariffs on the Italian economy, it is essential to consider not only the direct exposure through exports to the United States but also Italy's deep integration into global value chains. While this integration enhances resilience to domestic demand shocks and traditional trade disruptions, it also increases vulnerability to external shocks, with potential spillovers across sectors.
- In this context, EY forecasts indicate that Italy's real GDP will grow by 0.6% in 2025 and 0.8% in 2026. Inflation is expected to rise modestly, from 1.7% in 2025 to 1.9% in 2026. These projections are subject to a high degree of uncertainty due to conflicting economic signals and the fluid geopolitical environment.

Figure 1: Real GDP, Italy – % change

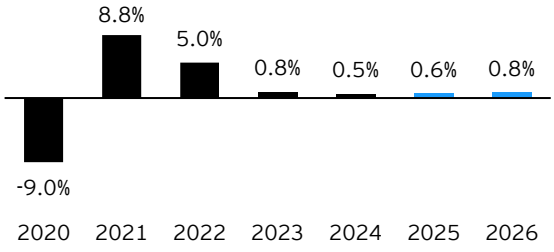
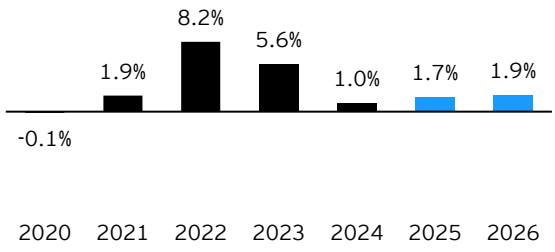


Figure 2: Consumer prices, Italy – % change



The global scenario

The world economy

According to the latest projections by the International Monetary Fund (IMF), after reaching 3.3% in 2024, global GDP growth is expected to decelerate to 2.8% in 2025, before partially recovering to 3.0% in 2026.[1] This trajectory reflects divergent growth patterns among major global economies. Advanced economies are projected to expand at a slower pace, with aggregate growth rates of 1.4% in 2025 and 1.5% in 2026. In contrast, emerging markets and developing economies are forecast to grow by 4.5% in 2025 and 4.6% in 2026, underscoring the persistent growth gap between different regions. These disparities are also evident within individual countries and economic blocs.

For example, the United States is expected to record growth of 1.8% in 2025, following a stronger performance in 2024 (2.8%), before slightly easing to 1.7% in 2026. In comparison, the Eurozone is projected to grow at a more modest pace, with forecasts of 0.8% in 2025 and 1.2% in 2026, following an estimated 0.9% expansion in 2024.

These trends are corroborated by the Organisation for Economic Co-operation and Development (OECD), which, in its June Economic Outlook, projects global GDP growth at 2.9% for both 2025 and 2026. The OECD forecasts US economic growth at 1.6% and 1.5% for the same period, while Eurozone growth is expected to remain lower, at 1.0% in 2025 and 1.2% in 2026.[2]

On the inflation front, global price growth is gradually returning to levels more consistent with historical norms. Following a global inflation rate of 5.7% in 2024, a decline to 4.3% in 2025 and further to 3.6% in 2026 is anticipated. This downward trend brings inflation closer to its long-term average of 3.7% observed between 2000 and 2019.

Figure 3: Real GDP – % change

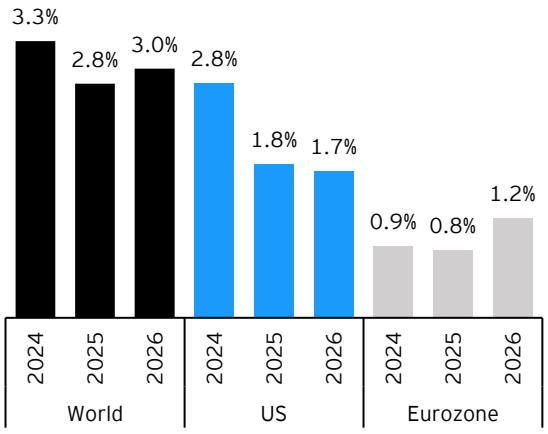
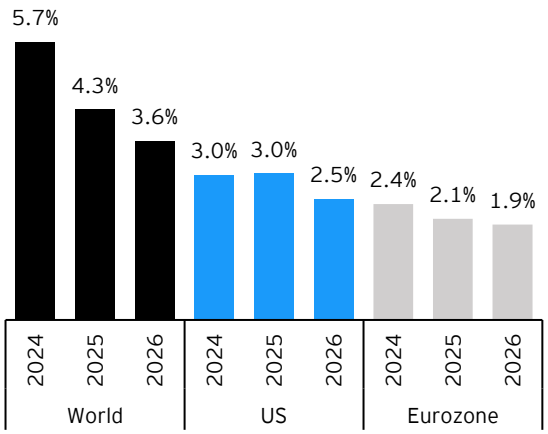


Figure 4: Consumer prices – % change



Source: EY elaborations on IMF World Economic Outlook data, April 2025.

Inflation is gradually declining in both the United States and the Eurozone, although the adjustment appears to be slower in the former. In the US, inflation is projected to remain stable at 3.0% in 2025—roughly in line with the rate observed in 2024—before easing to 2.5% in 2026, marking a 0.5 percentage point decline.

[1]IMF World Economic Outlook, April 2025.

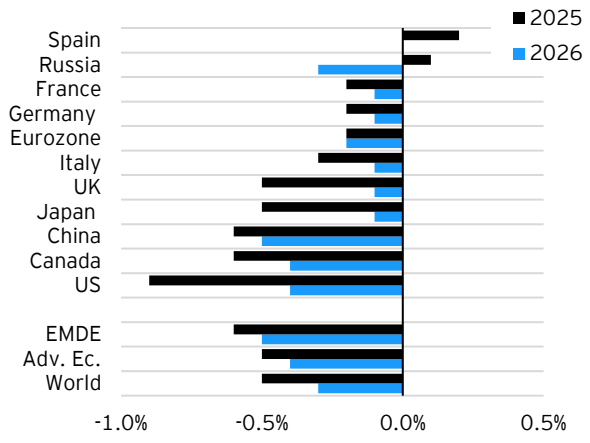
[2]OECD Economic Outlook, Volume 2025 Issue 1 - Tackling Uncertainty, Reviving Growth

This trajectory is influenced in part by evolving inflation expectations, which reflect anticipated effects of the trade policy decisions introduced by the new US administration. These policies may contribute to upward pressure on prices. Notably, in its October 2024 forecast, the IMF projected US inflation at 1.9% in 2025 and 2.1% in 2026, suggesting that recent developments may lead to a reassessment of those earlier estimates.[3]

In contrast to the United States, the inflation outlook for the Eurozone is more aligned with the European Central Bank's price stability target. Inflation in the region is expected to converge towards 2% over the next two years—a projection consistent with the estimates published in the IMF's October 2024 forecast.

Regarding global and national growth trends, the International Monetary Fund has significantly revised its growth projections downward in its latest report. This adjustment reflects heightened global uncertainty stemming from recent shifts in trade policy and the potential retaliatory measures by countries affected by these actions.

Figure 5: International Monetary Fund Forecast Revision – January 2025 vs. April 2025

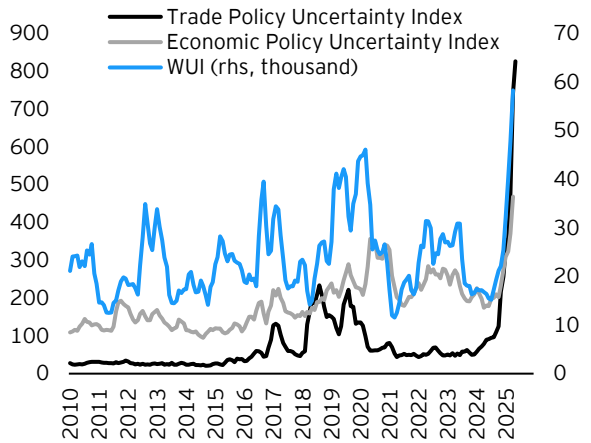


Source: EY elaborations based on IMF World Economic Outlook January 2025 and IMF World Economic Outlook April 2025 data. EMDE: Emerging Market and Developing Economies.

At the global level, economic growth projections for 2025 have been revised downward by approximately 0.5 percentage points, with a further reduction of about 0.3 percentage points for 2026. Among the countries most affected by these downward revisions are the United States, where forecasts have been lowered by 0.9 percentage points for 2025 and 0.4 percentage points for 2026. Similar adjustments have been made for Canada (-0.6 and -0.4 percentage points), China (-0.6 and -0.5), Japan, and the United Kingdom.

This broad-based revision reflects a persistent climate of elevated global uncertainty. Several key indicators underscore the extent of this phenomenon. Notably, measures of economic policy uncertainty and overall global uncertainty have reached—or in some cases surpassed—the levels observed during the 2020 pandemic. Additionally, trade-related uncertainty is now significantly higher than during the pandemic period, highlighting the complex and fragile nature of the current global economic environment.

Figure 6: Uncertainty indices, World – 3m moving average



Source: EY elaborations on ISTAT data, Caldara et al. (2019),[4] Economic Policy Uncertainty database. Latest observation: April 2025.

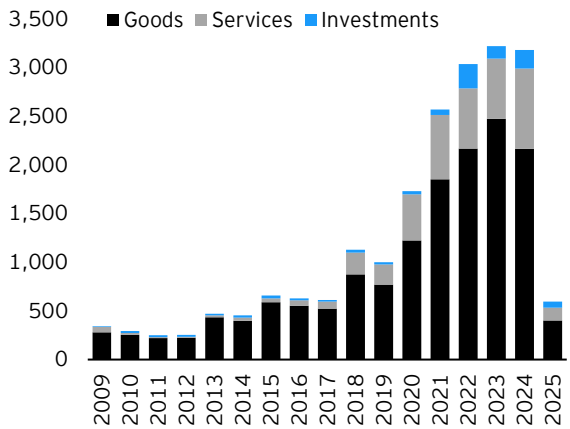
Trade-related uncertainty continues to escalate, driven in part by the steady increase in protectionist measures implemented in recent years. In the first quarter of 2025 alone, the number of newly announced trade-distorting measures rose by 16% compared to December 2024, with a notable acceleration observed from April 2 onward.

From a historical standpoint, the volume of such measures in 2024 was approximately 200% higher than in 2019 and nearly 400% above 2015 levels, underscoring the intensifying shift towards

[3]IMF World Economic Outlook, October 2024.
[4]Caldara, Dario, Matteo Iacoviello, Patrick Molligo, Andrea Prestipino, and Andrea Raffo, "The Economic Effects of Trade Policy Uncertainty," revised November 2019, Journal of Monetary Economics, forthcoming.

trade protectionism. While the majority of these actions still target goods, there is a growing trend towards restrictions in services and, increasingly, foreign investment.

Figure 7: Number of restrictive measures, World



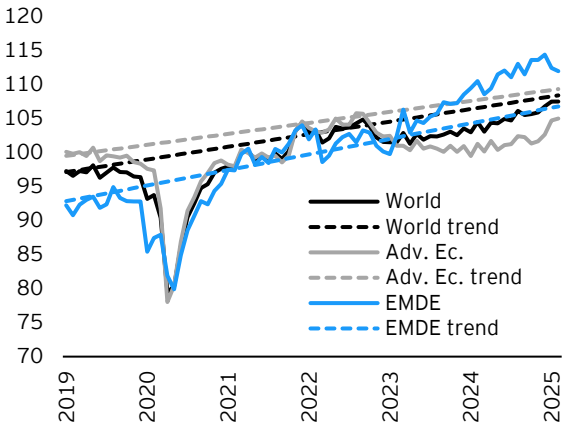
Source: International Monetary Fund.

The implementation of new trade policies, along with potential retaliatory measures by affected countries, may contribute to a further slowdown in global trade in goods. Recent analysis of goods trade trends reveals that, over the past two years, trade volumes have consistently remained below the linear growth trend observed between 2010 and 2019, despite a partial recovery in the early months of 2025.

A closer examination of trade performance by economic blocs shows that this recovery has been predominantly driven by emerging and developing economies. In contrast, advanced economies have exhibited weaker trade dynamics relative to the pre-pandemic trend.

Furthermore, recent months have witnessed a decline in goods trade volumes within emerging economies, which may impede the ongoing recovery process in global trade.

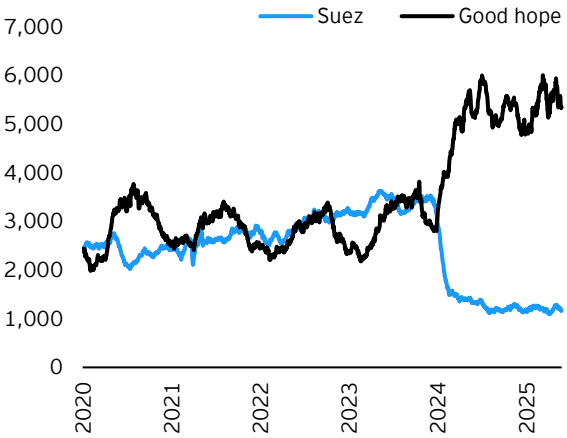
Figure 8: Trade in goods by volume and linear trend (2010-2019), World – index, 2010=100



Source: EY elaborations on CPB data Netherlands Bureau for Economic Policy Analysis. Reference is made to trade in goods. Latest observation: February 2025.

Beyond trade tensions, the resurgence or emergence of geopolitical risks, coupled with the subdued economic performance of several major global economies, represents significant risk factors for the stability and growth of international trade.

Figure 9: Volume of trade passing through the Panama Canal and Cape of Good Hope – metric tonnes



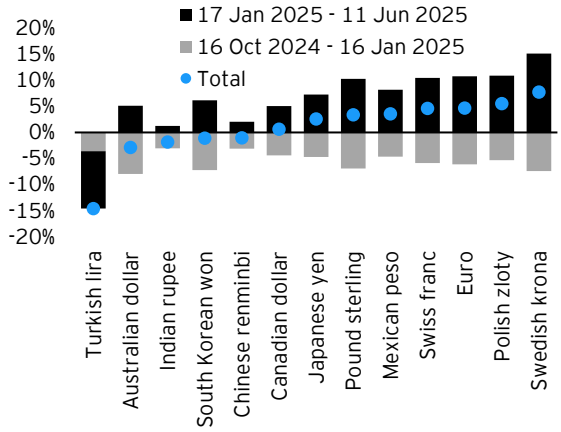
Source: EY calculations based on IMF PortWatch data. Data is represented as a 30-day moving average of trade volume expressed in thousands of metric tonnes. Latest observation: 25 May 2025.

For instance, trade volumes passing through the Suez Canal remain significantly below pre-tension levels following renewed conflicts in the Middle East. Consequently, a portion of trade has been rerouted through alternative passages, such

as the Cape of Good Hope leading to partial delays and increased transportation costs.

In the period surrounding the November elections, the US dollar initially strengthened markedly, driven by expectations of robust economic growth and a tighter monetary policy in the United States. However, since February 2025, the dollar has reversed course, depreciating against major global currencies. This decline reflects a less favourable growth outlook for the US economy, compounded by prevailing global uncertainty.[5]

Figure 10: Exchange rate movement against the US dollar

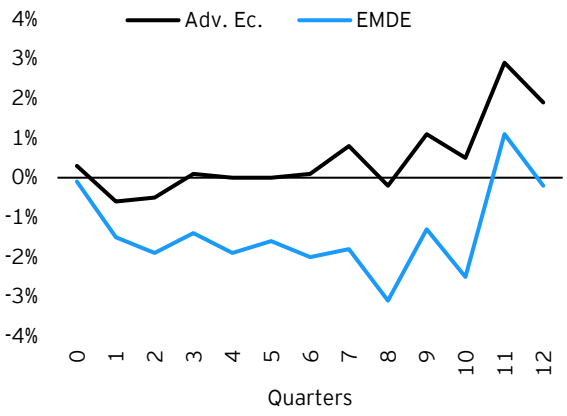


Source: EY elaborations on Eurostat data. An increase represents a revaluation of the currency under analysis against the dollar (i.e., a devaluation of the dollar).

Understanding foreign exchange market fluctuations is crucial due to their wide-ranging impacts on global economies. For example, past episodes of elevated trade policy uncertainty have been accompanied by a sustained appreciation of the US dollar.[6] This appreciation has, in turn, dampened exports from both the United States and dollar-linked countries—such as those with fixed exchange rate regimes—thereby generating adverse spillover effects on emerging and developing economies. A stronger dollar can also exacerbate inflationary pressures, particularly in countries where the pass-through from exchange rates to domestic prices is amplified, for instance, through increased costs of dollar-denominated raw materials.[7]

Emerging economies are expected to bear the most significant negative consequences of a continued appreciation of the US dollar.

Figure 11: Effect of a dollar appreciation on GDP – % change

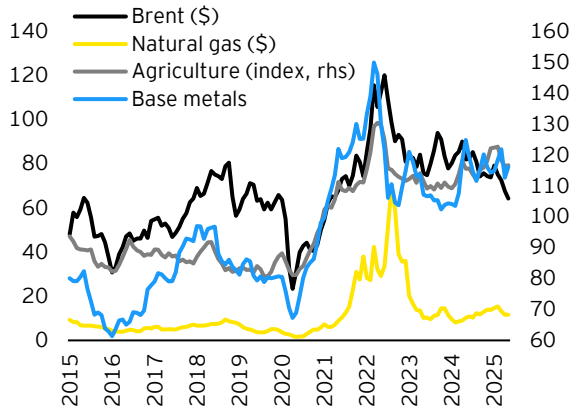


Source: IMF External Sector Report 2023. The chart shows the effects of a 10% appreciation of the US dollar on the real GDP of the countries analyzed.

Conversely, excessive depreciation of the dollar is not without risks. Political uncertainty and diminished growth prospects in the United States could trigger heightened volatility in financial markets, especially if abrupt currency swings occur. Broad uncertainty also tends to suppress aggregate demand through declines in consumer confidence and income over the medium term. Moreover, uncertainty can slow investment and global trade activity, while potentially affecting commodity price trends.[8,9]

[5]IMF World Economic Outlook, April 2025.
[6]Albrizio, Silvia, Alejandro Buesa, Moritz Roth, and Francesca Viani. Forthcoming. "Unraveling Uncertainty: Disentangling Trade Policy Risks from Broader Uncertainty." IMF Working Paper, International Monetary Fund, Washington, DC.
[7]Carrière - Swallow, Yan, Melih Firat, Davide Furceri, and Daniel Jim is nez. 2024. " State - Dependent Exchange Rate Pass - Through. " Oxford Bulletin of Economics and Statistics, ahead of print, October 26, 2024.
[8]Handley, Kyle, and Nuno Limão. 2017. "Policy Uncertainty, Trade, and Welfare: Theory and Evidence for China and the United States." American Economic Review 107(9): 2731–83.
[9]Caldara, Dario, Matteo Iacoviello, Patrick Molligo, Andrea Prestipino, and Andrea Raffo. 2020. "The Economic Effects of Trade Policy Uncertainty." Journal of Monetary Economics 109: 38–59.

Figure 12: Energy commodity prices ($) and agricultural and basic metals price index (2010=100)



Source: EY elaborations on World Bank data. Brent and natural gas prices are expressed in $/bbl and $/mmbtu respectively. The price of natural gas refers to natural gas quoted in the Title Transfer Facility (TTF). The agricultural price index considers the price of various goods and derivatives related to agriculture at a global level (for example, the price of wheat). Latest observation: May 2025.

Regarding commodity prices, Brent crude oil recorded a price of $64.2 per barrel in May 2025, down from $67.7 per barrel in the previous month.[10] This marks the lowest level since February 2021 and primarily reflects concerns about a potential slowdown in global demand amid ongoing trade tensions. Additional downward pressure has been exerted by increased oil production outside the OPEC+ group—which includes OPEC members alongside non-member producers such as Russia—and the cessation of OPEC+ supply cuts.[11]

Similarly, European gas prices experienced a notable decline in May, falling from $13.2 per MMBtu[12] in March to $11.7 per MMBtu, returning to levels last seen in September 2024. This decrease is likely linked to heightened global uncertainty and fears regarding the trajectory of global economic growth.

Prices of agricultural commodities, after accelerating in late 2024 and early 2025, fell by approximately 2% relative to the average of the first quarter of 2025. The issue of agricultural price volatility is closely intertwined with food security considerations. It is important to emphasise that, alongside price levels, targeted redistributive policies play a critical role in ensuring food security, particularly by enabling lower-income populations to better cope with price fluctuations.[13]

Base metal prices have exhibited trends similar to other raw materials: although they have declined from the peaks reached in 2022, current price levels remain significantly elevated compared to the pre-pandemic period. The behaviour of metal prices is particularly important due to their influence on core inflation, which excludes highly volatile components such as energy and unprocessed food.

Price shocks in metals have substantial and persistent effects, especially in economies where production systems rely heavily on metals as intermediate inputs. This dynamic differs from energy supply shocks—such as those affecting oil prices—that primarily impact headline inflation. The global economy's shift towards more metal-intensive production, driven largely by the energy transition, is likely to increase the influence of metal price shocks on core inflation. As a result, these shocks may become less immediately visible but more enduring over time. Additionally, as fossil fuel use declines and metals become increasingly central inputs in energy systems, the global economy may become less dependent on oil and more reliant on metals.[14] For instance, the International Energy Agency (IEA) projects that copper demand will rise by 150%, while oil consumption could decline by 25% by 2030 in a net-zero emissions scenario.[15]

Recent geopolitical tensions have also contributed to greater volatility in metal prices, exacerbated by trade-distorting and restrictive measures implemented since the conflict in Ukraine.[16] Given that metal production is often geographically concentrated and not easily

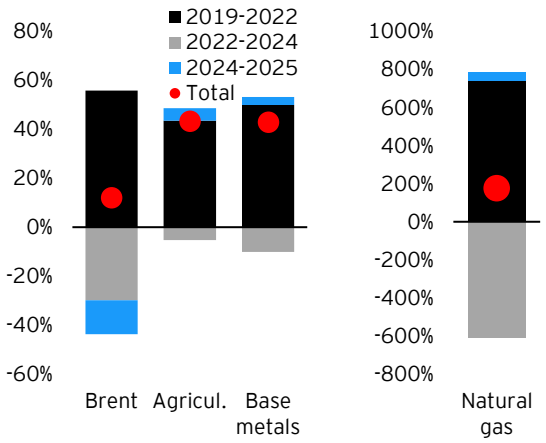
[10]Dollars per barrel of oil. One barrel is equal to approximately 159 liters.
[11]This refers to the group of oil exporting countries. The OPEC group consists of Algeria, Angola, Saudi Arabia, Congo, United Arab Emirates, Gabon, Equatorial Guinea, Iran, Iraq, Kuwait, Libya, Nigeria, Venezuela. The OPEC+ group consists of the OPEC countries plus Azerbaijan, Bahrain, Brunei, Kazakhstan, Malaysia, Mexico, Oman, Russia, Sudan, South Sudan.
[12]Dollars per million British thermal units, a measure of the amount of gas.
[13]Bogmans, Christian, Pescatori, Andrea, Prifti, Ervin (2024). "How do Economic Growth and Food Inflation Affect Food Insecurity?". IMF Working Paper WP/24/188. International Monetary Fund, Washington DC.
[14]Boer, Lukas, Andrea Pescatori, and Martin Stuermer. 2024. "Energy Transition Metals: Bottleneck for Net-Zero Emissions?" Journal of the European Economic Association 22.
[15]IEA. 2022. "The Role of Critical Minerals in Clean Energy Transitions." Report, International Energy Agency, Paris.
[16]Gopinath, Gita, Pierre-Olivier Gourinchas, Andrea Presbitero, and Petia B Topalova. 2024. "Changing Global Linkages: A New Cold War?" IMF Working Paper 2024/076.

substitutable, trade tensions typically result in pronounced price fluctuations, with adverse repercussions for the global economy.[17]

Looking ahead, it is important to note that commodity prices remain substantially higher than their pre-pandemic levels. Specifically, Brent crude oil prices are approximately 12% above 2019 averages, while prices for agricultural commodities and base metals remain elevated by roughly 43% in both categories. Natural gas prices in Europe are markedly higher, with May 2025 levels about 177% above the 2019 average.

In the broader context, commodity prices are not independent of macroeconomic conditions. The recent decline in commodity prices can be partly attributed to the restrictive monetary policies adopted by major central banks worldwide, which have dampened economic activity and influenced financial conditions in key economies.[18,19]

Figure 13: Change in commodity prices, 2019-2025



Source: EY elaborations on World Bank data. Latest observation: May 2025.

It has been estimated that a 10-basis point increase in the US monetary policy benchmark rate leads to a reduction in commodity prices—such as oil, base metals, and food—ranging between 0.5% and 2.5% within 18 to 24 business days. According to several studies, the response of commodity prices to tighter U.S. monetary policy accounts for approximately 47% of the overall effect on US inflation and 57% of its impact on inflation in other countries. The European Central Bank's (ECB) monetary policy exerts similar effects, although to a lesser degree.[20]

Overall, the partial recovery observed in commodity prices is aiding central banks in their mandate to contain inflation, particularly in emerging and developing economies where food and energy constitute significant portions of consumer expenditure.[21] Nevertheless, current developments indicate that risk factors remain present and warrant continued attention.

Growth in the world's major economies: the latest data

The international landscape is characterised by a heterogeneous trend across the main world economies, even when considering the short term.

United States

The United States GDP recorded a contraction of 0.1% in the first quarter of 2025 (equivalent to an annualised growth rate of -0.2%),[22] following a growth of 0.6% in the fourth quarter of the previous year. Specifically, the first quarter of 2025 was marked by weak private consumption growth (0.3%, slowing compared to 1.0% in the previous quarter), largely due to stagnation in goods consumption (0.0%) and an increase in the purchase of services (0.4%). Within goods consumption, durable goods contracted by 1.0%, while non-durable goods consumption grew by 0.5%

Private investments showed a significant rebound with 5.6% growth in the first quarter, after a contraction of 1.4% in the fourth quarter of 2024.

From an accounting perspective, the international trade component was responsible for the GDP contraction in the first quarter of

[17]Alvarez, Jorge, Mehdi Benatiya Andaloussi, Chiara Maggi, Alexandre Sollaci, Martin Stuermer, and Petia Topalova. 2023. "Geoeconomic Fragmentation and Commodity Markets." IMF Working Paper 2023/201.
[18]Barsky, Robert B., and Lutz Kilian. 2004. "Oil and the Macroeconomy Since the 1970s." Journal of Economic Perspectives 18(4): 115-134. 10.1257/0895330042632708.
[19]Jacks, David S, and Martin Stuermer. 2020. "What drives commodity price booms and busts?" Energy Economics 85 104035.
[20]Miranda-Pinto, J., Pescatori, M.A., Prifti, E., & Verduzco-Bustos, G. (2023). *Monetary policy transmission through commodity prices*. IMF Working Paper WP/23/215, 2023 Oct.
[21]Ha, J., M. A. Kose, and F. Ohnsorge, eds. 2019. Inflation in Emerging and Developing Economies: Evolution, Drivers and Policies. Washington, DC: World Bank.
[22]For more information, https://www.bea.gov/help/faq/463 .

2025. Imports increased by 9.3% quarterly, while exports rose by a more moderate 0.6%, resulting in a negative contribution of -1.4 percentage points to GDP growth.[23] Many analysts suggest that, excluding measurement errors, this may reflect a slowdown in domestic economic activity.[24]

Regarding price trends, inflation in the United States has declined in recent months. In April 2025, inflation stood at 2.3%, down from an average of 2.7% over the previous three months. Other price indicators, such as the Personal Consumption Expenditure Price Index, have followed a similar downward trend.[25]

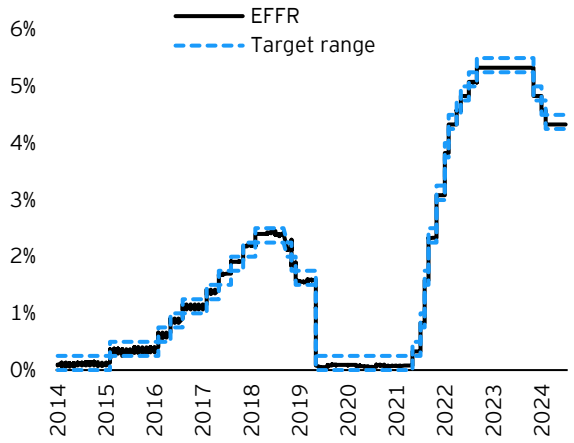
Although inflation has been decreasing, it remains above the central bank's 2% target. Consequently, monetary policy continues to adopt a cautious stance, with interest rates remaining unchanged. At its May 7 meeting, the Federal Reserve decided to maintain the target interest rate range at 4.25%-4.50%.[26] This decision followed the unchanged rates confirmed at the March 19 meeting.[27]

The Federal Reserve's position is supported by an overall dynamic economic trend—particularly over recent quarters—a still elevated inflation rate, and a robust labour market.

Despite the decline in interest rates from their peak in 2023, it is important to note that their relatively high levels may still have adverse effects on emerging economies, as widely documented in the literature.[28]

Extending the analysis, changes in U.S. monetary policy have been a major driver of global economic fluctuations, especially since the 2008-2009 financial crisis. This is mainly due to the Federal Reserve's central role within the global financial system. Emerging economies with strong trade and financial ties to the global economy are the most vulnerable to these fluctuations.

Figure 14: Federal Reserve monetary policy benchmark rates, United States



Source: EY calculations based on Federal Reserve Bank of New York data. EFFR: Effective Federal Funds Rate; the EFFR is calculated as the volume-weighted median of reported overnight transactions. For more information, see https://www.newyorkfed.org/markets/reference-rates/effr .

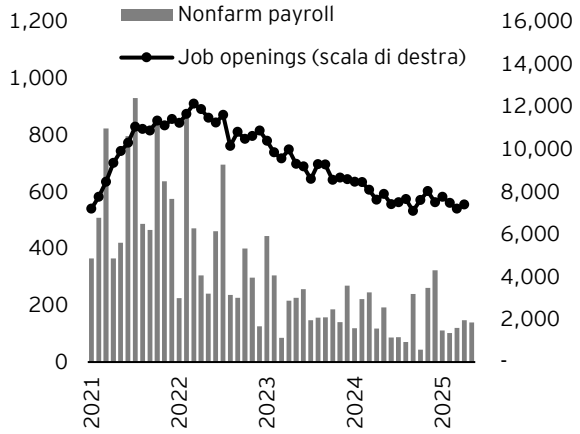
The effects of monetary policy also exhibit significant asymmetries between tightening and easing phases. This asymmetry arises from varying degrees of budget constraints within the banking sector. Restrictive monetary policy periods usually coincide with tighter budget constraints, amplifying the negative impact of liquidity reduction. Conversely, easing periods tend to coincide with looser constraints, resulting in a more moderate effect of monetary expansion. Additionally, emerging market policymakers' aversion to exchange rate volatility exacerbates the negative consequences of US monetary tightening, further amplifying the asymmetric effects of monetary policy shocks.[29]

Regarding recent US economic data, consumer spending in April 2025 declined

[23]Gross Domestic Product (Second Estimate), Corporate Profits (Preliminary Estimate), 1st Quarter 2025, https://www.bea.gov/news/2025/gross-domestic-product-second-estimate-corporate-profits-preliminary-estimate-1st-quarter .
[24]As an example, please refer to the following link https://x.com/vmrconstancio/status/1917930078320693527?s=61&t=p-IKXbBQsz9WWgP7OIeJXw .
[25]For more information, https://www.bea.gov/data/personal-consumption-expenditures-price-index .
[26]Federal Reserve issues FOMC statement, 07 May 2025, https://www.federalreserve.gov/newsevents/pressreleases/monetary20250507a.htm .
[27]Federal Reserve issues FOMC statement, 19 March 2025, https://www.federalreserve.gov/newsevents/pressreleases/monetary20250319a.htm .
[28]In this regard, Georgiadis, G. (2016) can be cited. Determinants of global spillovers from US monetary policy. Journal of International Money and Finance 67 (C), 41–61; Iacoviello, M. and G. Navarro (2019). Foreign effects of higher US interest rates. Journal of International Money and Finance 95, 232–250; Miranda-Agrippino, S. and H. Rey (2020). US Monetary Policy and the Global Financial Cycle. Review of Economic Studies 87 (6), 2754–2776; Ca' Zorzi, M., L. Dedola, G. Georgiadis, M. Jarocinski, L. Stracca, and G. Strasser (2020). Monetary policy and its transmission in a globalized world. International Journal of Central Banking 19 (2); Ahmed, S., O. Akinci, and A. Queralt´o (2021). US Monetary Policy Spillovers to Emerging Markets: Both Shocks and Vulnerabilities Matter. International Finance Discussion Papers 1321, Board of Governors of the Federal Reserve System.
[29]Mistak, J., & Ozkan, G. (2024). Asymmetric monetary policy spillovers: the role of supply chains, credit networks and fear of floating.

modestly by 0.1% compared to the previous month, following stronger growth of 0.7% in March.[30] This contraction was primarily driven by a 0.2% decrease in goods consumption, after gains of 1.5% and 0.2% in March and February, respectively, while services consumption increased by 0.3% in April, following 0.4% and -0.1% changes in March and February. Specifically, durable goods consumption declined by 0.8%, while non-durable goods consumption exhibited weak growth of 0.1%.

Figure 15: Change in nonfarm payrolls and job openings – USA

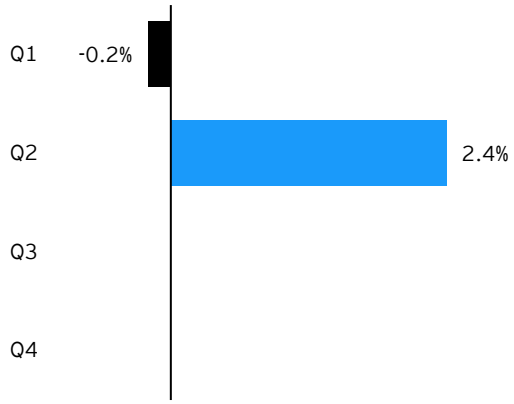


Source: EY calculations based on Bureau of Labor Statistics (BLS) data. *Nonfarm payroll* refers to the number of US workers in the economy excluding business owners, household employees, unpaid volunteers, farm employees, and the unincorporated self-employed. This measure represents about 80% of workers who contribute to gross domestic product (GDP). For more information, https://fred.stlouisfed.org/series/PAYEMS.

Labour market data remain positive. In May, nonfarm payroll increased by 139,000 units, following a gain of 147,000 in April. These figures represent an improvement compared to the average monthly growth of approximately 111,000 during the first quarter of 2025. Job openings have declined from their 2022 peak but remain above 7,000 per month. The unemployment rate remains relatively stable, slightly above 4%.[31]

Industrial and manufacturing activity presents mixed signals. Industrial production registered zero growth (0.0%) in April 2025 relative to March, following a 0.3% contraction in March and 0.9% growth in February. Manufacturing activity contracted by 0.4% in April, after growth of 0.4% and 1.1% in the two previous months. Despite these monthly fluctuations, the trend for both industrial and manufacturing production remains encouraging, with growth of 1.5% and 1.2%, respectively, in April 2025.[32]

Figure 16: GDP 2025 – USA, annualised QoQ % change



Source: EY calculations based on Federal Reserve Bank of New York data, US Bureau of Economic Analysis (BEA). Blue bars represent available forecasts for the next quarters (New York Fed Staff Nowcast). Rates of change are annualised. Last update: May 23, 2025. Forecasts for the third and fourth quarters are not currently available.

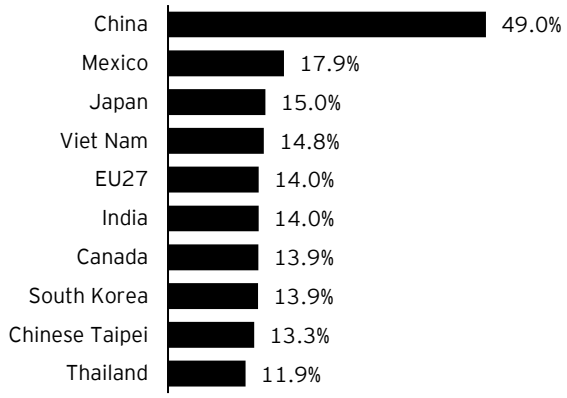
Forecasts for the upcoming quarters, according to the Federal Reserve Bank of New York's May 2025 projections, indicate an average GDP growth rate over the next four quarters ranging between -1.04% and +2.63%, with a median of 0.89%.[33] For the second quarter of 2025, the forecasted annualised growth rate[34] stands at 2.4%.[35]

Political uncertainty following the early November elections, particularly regarding trade policies, adds an additional layer of uncertainty to both the US and global economic outlook.

[30]Personal Income and Outlays, April 2025. For more information, https://www.bea.gov/news/2025/personal-income-and-outlays-april-2025 .
[31]Bureau of Labor Statistics, Employment Situation News Release. For more information, https://www.bls.gov/news/release/empsit.htm .
[32]Industrial Production and Capacity Utilization, April 2025. For more information, https://www.federalreserve.gov/releases/g17/current/default.htm .
[33]Federal Reserve Bank of New York, Outlook-at-Risk: Real GDP Growth, Unemployment, and Inflation, https://www.newyorkfed.org/research/policy/outlook-at-risk#root:growth-at-risk .
[34]For more information, https://www.bea.gov/help/faq/463 .
[35]For more information, https://www.newyorkfed.org/research/policy/nowcast#/overview .

Currently, China faces the highest average tariff rate on exports to the United States at 49%, followed by Mexico (approximately 18%), Japan (15%), and Vietnam (15%). The European Union applies an average tariff rate of 14%. It is important to note that these rates represent weighted averages based on export values for each product. Consequently, some goods may be subject to higher or lower tariffs, resulting in varying impacts on export performance and foreign trade dynamics in these countries.

Figure 17: Average tariff rate applied to exports to the USA



Source: EY calculations on World Trade Organization, International Monetary Fund. Last update: 22 May 2025.

The overall impact on the Eurozone and other major global economies will be explored at the end of Chapter 2 of this report.

United Kingdom

The United Kingdom experienced a GDP growth of 0.7% in the first quarter of 2025, following modest growth of 0.1% in the fourth quarter of 2024 and no growth in the third quarter of 2024. The positive performance in the first quarter of 2025 was primarily driven by an increase in private consumption (0.2%) and investment (2.9%), along with a favourable contribution from foreign demand amounting to 0.4 percentage points.[36]

High-frequency data indicate a modest upward trend in the economy. Following monthly growth rates of 0.1% in January and 0.3% in February, the services sector exhibited stronger growth in March, expanding by 0.4%.[37]

The construction sector also demonstrated signs of expansion, with growth of 0.5% in March, following increases of 0.2% in February and a contraction of 0.3% in January. Meanwhile, the industrial sector experienced a contraction of 0.7% in March compared to the previous month, after a growth of 1.7% in February and a contraction of 0.4% in January.[38,39]

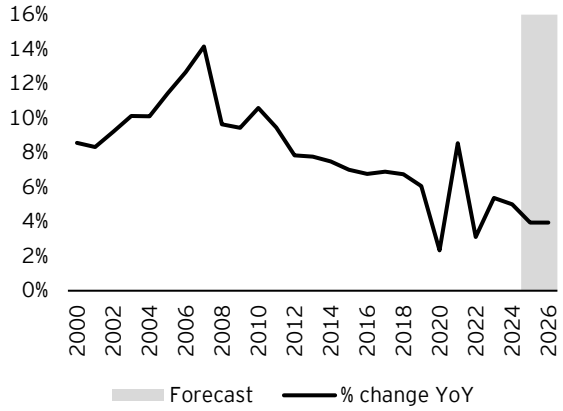
Regarding price developments, April registered a 3.5% increase compared to the same month of the previous year, following a 2.6% rise in March. Core inflation—measured on a basket of goods excluding the most volatile components such as energy and food—also remained elevated, recording a 3.8% increase in April year-on-year, up from 3.4% in March.[40]

China

The Chinese economy is exhibiting signs of deceleration. This trend is not limited to recent GDP growth figures or the forecasts for 2026—in its latest World Economic Outlook, the International Monetary Fund projects China's growth at 4.0% for both 2025 and 2026—but reflects a longer-term pattern that has been ongoing since the period following the 2008 financial crisis.

[36]GDP first quarterly estimate, UK: January to March 2025, https://www.ons.gov.uk/economy/grossdomesticproductgdp/bulletins/gdpfirstquarterlyestimateuk/januarytomarch2025 .
[37]Office for National Statistics, Index of Services, UK: March 2025, https://www.ons.gov.uk/economy/economicoutputandproductivity/output/bulletins/indexofservices/march2025 .
[38]Office for National Statistics, Construction output in Great Britain: March 2025, https://www.ons.gov.uk/businessindustryandtrade/constructionindustry/bulletins/constructionoutputingreatbritain/january2025 .
[39]Office for National Statistics, Index of Production, UK: March 2025, https://www.ons.gov.uk/economy/economicoutputandproductivity/output/bulletins/indexofproduction/january2025 .
[40]Office for National Statistics, Consumer price inflation, UK: April 2025, https://www.ons.gov.uk/economy/inflationandpriceindexes/bulletins/consumerpriceinflation/april2025 .

Figure 18: GDP, China – var. %



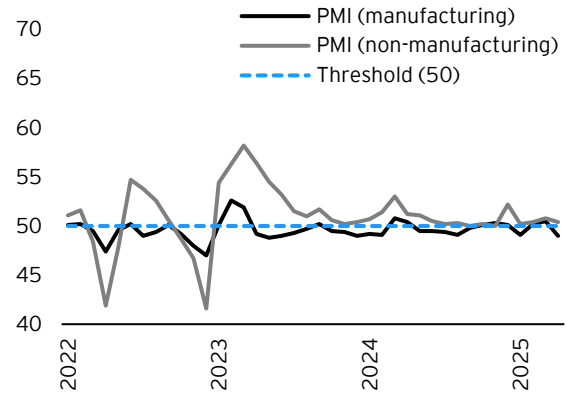
Source: EY elaborations on International Monetary Fund data and forecasts.

According to the latest data, the Chinese economy grew by 5.4% in the first quarter of 2025 compared to the same quarter of the previous year, following growth rates of 5.4% and 4.6% in the fourth and third quarters of 2024, respectively. On a cyclical basis, quarter-on-quarter growth for the first quarter of 2025 was 1.2%, after increases of 1.6% and 1.4% in the fourth and third quarters of 2024.[41]

Regarding the industrial sector, value added increased by 6.1% in April compared to the same month of the previous year, following a notable growth of 7.7% recorded in March. This marks an acceleration relative to the trends observed in the final months of 2024. This performance is partly attributable to the growth in value added in the manufacture of railway, ship, aerospace and other transport equipment, which rose by 17.6% annually, and in the manufacture of electrical machinery and apparatus, which increased by 13.4%.[42]

Regarding the expectations of operators in both the manufacturing and non-manufacturing sectors, the Purchasing Managers' Index (PMI) published by the National Bureau of Statistics of China indicates a trend close to the expansion threshold of 50, despite having recorded a decline in recent months.[43]

Figure 19: Purchasing Managers Index (PMI), manufacturing and non-manufacturing activities, China



Source: EY elaborations on National Bureau of Statistics of China data. Latest observation: April 2025.

The real estate sector remains in crisis, with investments contracting by 10.3% between January and April 2025 compared to the same period in the previous year, indicating significant difficulties within the sector.[44]

Expanding the scope of analysis to overall investments, cumulative growth between January and April 2025,compared to the same period in the previous year, reached 4.0%. This increase was primarily driven by significant growth in the manufacture of railway, ship, aerospace and other transport equipment (29.6%), production and supply of electricity, heat power, gas and water (25.5%);and the manufacture of automobiles (23.6%).[45]

Regarding retail sales, April 2025 saw an annual increase of 5.1% compared to the same month in the previous year. This growth was lower than the rate recorded in March (5.9%), but remained higher than the monthly growth rates observed in the latter part of 2024—for instance, annual growth rates of 3.0% and 3.7% were recorded in November and December 2024, respectively.[46]

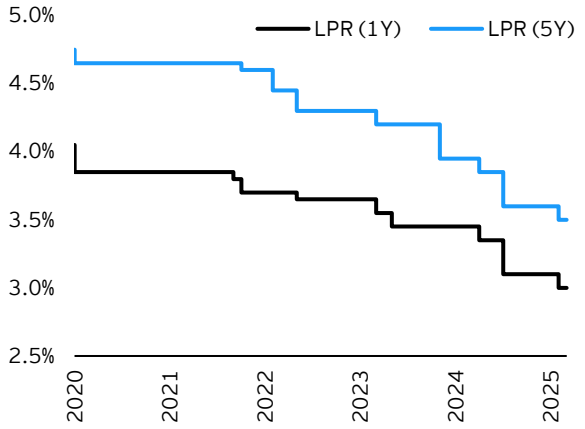
[41]Preliminary Accounting Results of GDP for the First Quarter of 2025, https://www.stats.gov.cn/english/PressRelease/202504/t20250421_1959377.html.
[42]Industrial Production Operation in April 2025, https://www.stats.gov.cn/english/PressRelease/202505/t20250526_1959952.html.
[43]Purchasing Managers' Index for April 2025, https://www.stats.gov.cn/english/PressRelease/202505/t20250507_1959690.html.
[44]Investment in Real Estate Development from January to April 2025, https://www.stats.gov.cn/english/PressRelease/202505/t20250526_1959953.html.
[45]Investment in Fixed Assets from January to April 2025, https://www.stats.gov.cn/english/PressRelease/202505/t20250526_1959951.html.
[46]Total Retail Sales of Consumer Goods in April 2025, https://www.stats.gov.cn/english/PressRelease/202505/t20250526_1959954.html.

From a foreign trade perspective, exports in April 2025 grew by 9.3% year-on-year, while imports increased by 0.8%.[47] The trajectory of exports in the upcoming months remains a critical factor to monitor, especially in light of prevailing trade uncertainties stemming from the implementation of new trade-distorting measures.

Based on the information presented, it can be affirmed that the Chinese economy is undergoing a slowdown in growth, which the country is actively addressing through targeted fiscal[48] and monetary measures.

From a monetary perspective, it is important to note that interest rates have continued to decline, even as major central banks worldwide were adopting restrictive monetary policies to address rising price levels.

Figure 20: 1- and 5-year Loan Prime Rate (LPR), China



Source: EY elaborations on People Bank of China data. Latest observation: May 2025.

Specifically, in May 2025, the one- and five-year Loan Prime Rates (LPR)—which serve as benchmarks for commercial banks in setting lending costs for customers with the highest credit ratings—stood at 3.00% and 3.50%, respectively. Meanwhile, the Medium-Term Lending Facility (MLF) rate, representing the rate at which commercial banks and other financial institutions, such as the China Development Bank, borrow from the central bank over the medium term, remained steady at 2.00%.[49]

From a fiscal policy perspective, a recent study has demonstrated that such measures can serve as effective tools to promote export growth. Specifically, certain subsidies have contributed to increasing export volumes and reducing export prices, particularly within sectors such as metallurgical industries and furniture manufacturing.[50]

The slowdown in China's economy is expected to persist, underscoring the urgent need to reform its growth model. Key challenges to address include demographic shifts—particularly an aging population that will reduce the workforce,[51] slowing productivity growth as the country transitions to advanced economy status,[52] and diminishing returns on investment. Notably, record-high savings are increasingly being channeled into less productive sectors, such as state-owned enterprises and real estate.

These factors indicate the necessity to rebalance China's growth model, shifting towards one increasingly propelled by private consumption. Without reforms, potential growth is projected to slow to approximately 3.8% on average between 2025-2030 and further decline to around 2.8% on average between 2031 and 2040. Conversely, under a hypothetical reform scenario, potential growth could be sustained at about 4.7% between 2023 and 2038.[53]

While the overall international scenario indicates a general recovery, it remains marked by numerous uncertainties and vulnerabilities. These stem from a still complex geopolitical landscape, more moderate growth in certain economies compared to the pre-pandemic period, uncertainty arising from implemented or threatened trade-distorting measures and the consequent slowdown in trade, as well as

[47]For more information, see http://english.customs.gov.cn/statics/report/preliminary.html . The annual growth of exports stands at 8.1% when considering exports expressed in dollars, while that of imports stands at -0.2%.
[48]The State Council Information Office of the People's Republic of China, "China vows 'highly proactive' fiscal policy to shore up economy." For more information, http://english.scio.gov.cn/pressroom/2025-01/11/content_117658569.html .
[49]For more information, http://www.pbc.gov.cn/en/3688229/3688335/3883798/index.html .
[50]Rotunno, L., & Ruta, M. (2024). Trade Implications of China's Subsidies. IMF Working Paper WP/24/180, 2024 Aug.
[51]International Monetary Fund (IMF). 2017. "Asia: At Risk of Growing Old before Becoming Rich?" Chapter 2 in Asia and Pacific Regional Economic Outlook: Preparing for Choppy Seas. May 2017: Washington, DC.
[52]Madsen, Jakob B., Md. Rabiul Islam, and James B. Ang. 2010. "Catching Up to the Technology Frontier: The Dichotomy Between Innovation and Imitation." Canadian Journal of Economics 43(4): 389-1411.
[53]Muir, D., Novta, N., & Oeking, A. (2024). China's Path to Sustainable and Balanced Growth. IMF Working Paper WP/24/238, 2024 Nov.

commodity prices that remain elevated relative to pre-pandemic levels.

The European framework

The Eurozone economy and main indicators

In the first quarter of 2025, the Eurozone recorded a quarterly growth rate of 0.4% compared to the previous quarter, following a contraction of 0.2% in the fourth quarter of 2024 and modest growth of 0.1% in the third quarter. This positive performance in the first quarter was primarily driven by Spain, which continued to experience sustained growth of 0.6%, building on growth rates of 0.7% recorded in both the third and fourth quarters of 2024. Italy and Germany showed more moderate growth of 0.3% and 0.4%, respectively, while France's growth was weaker at 0.1%.

When considering the year-on-year trend, Spain led the region with a GDP increase of 2.8% in the first quarter, slightly down from 3.3% growth in the previous two quarters of 2024. France and Italy also exhibited positive but more moderate growth rates of 0.6% and 0.7%, respectively. For Germany, the first quarter of 2025 marked the end of a period of GDP contraction that began in the third quarter of 2023, although growth remained flat at 0.0%. Overall, the Eurozone experienced a trend growth rate of 1.2% in the first quarter of 2025.

Figure 21: GDP and contributions by country, Eurozone – % change YoY

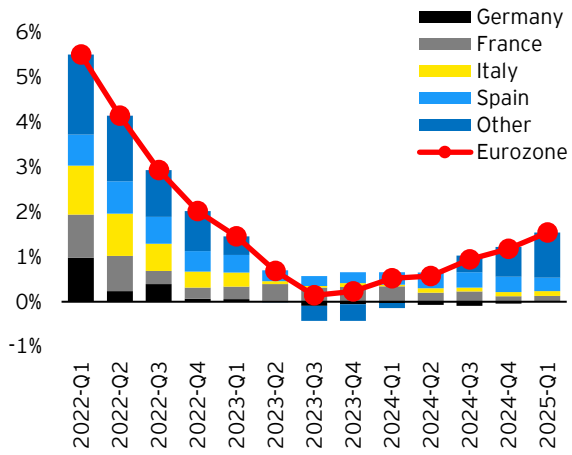
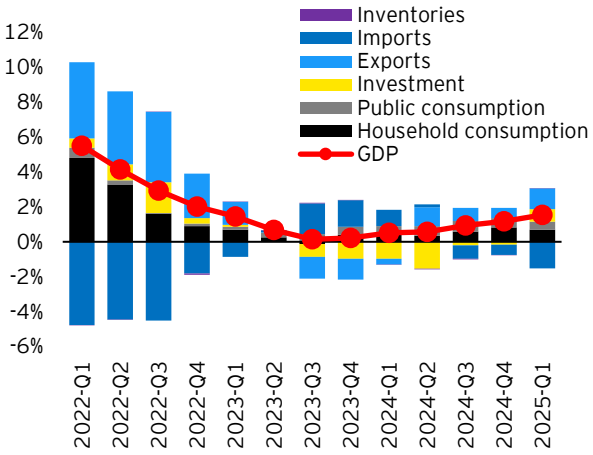


Figure 22: GDP and contributions by component, Eurozone – % change YoY



Source: EY elaborations on Eurostat data.

From the perspective of GDP components, the primary drivers of trend growth in the first quarter of 2025 were private consumption and investments, each contributing positively by 0.7 percentage points. Public consumption also supported growth, adding 0.5 percentage points. In contrast, foreign demand exerted a negative impact due to imports growing faster than exports, with respective trend growth rates of 3.3% and 2.3%.

Expanding the analysis, it is noteworthy that among the four main Eurozone economies, only Italy has realigned itself with the growth trajectory observed between 2015 and 2019. Meanwhile, Germany, France, and Spain continue to remain significantly below the levels seen during that period.

Figure 23: Quarterly GDP and linear trend, Germany, France – index, 2019 = 100

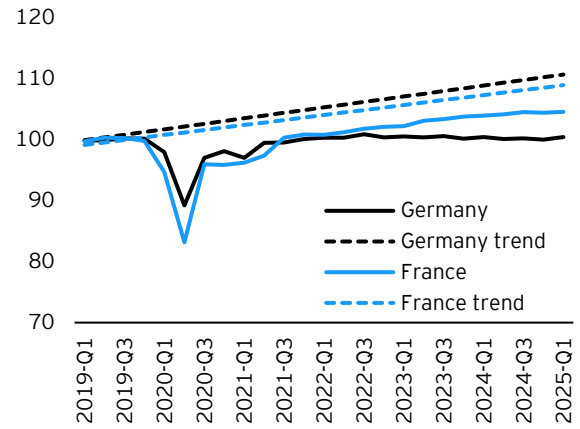
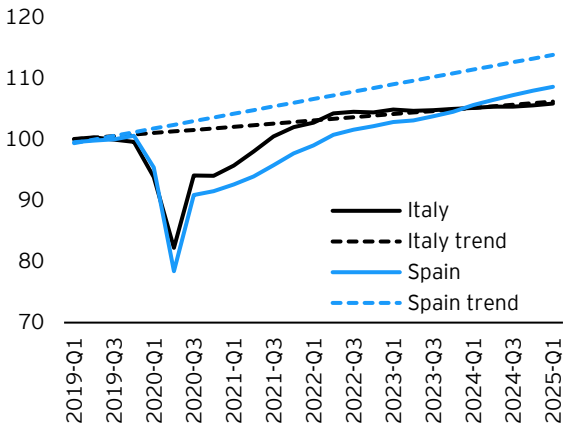


Figure 24: Quarterly GDP and linear trend, Italy, Spain – index, 2019 = 100



Source: EY elaborations on Eurostat data.

In accurately interpreting this data, it is important to highlight that the average trend growth between 2015 and 2019 varied among the four countries analysed, with Italy exhibiting a lower growth rate compared to the others (average annual growth of 1.0% for Italy, 1.8% for Germany, 1.5% for France, and 2.8% for Spain). Therefore, Italy's ability to realign with pre-pandemic levels should be considered in the context of its relatively weak growth in the years preceding the pandemic.

Regarding Eurozone industrial production, March 2025 showed a recovery both in trend and cyclical terms. Compared to the same month of the previous year, the industrial production index increased by 3.9%, following a 0.9% growth in February, after twenty-one consecutive months of negative trend growth. From a cyclical perspective, industrial production rose by 2.6% in March, building on gains of 0.8% and 1.1% recorded in January and February, respectively. These developments brought the industrial production index back to levels consistent with the average for 2021.

Figure 25: Industrial production by main countries, Eurozone – index, 2021=100

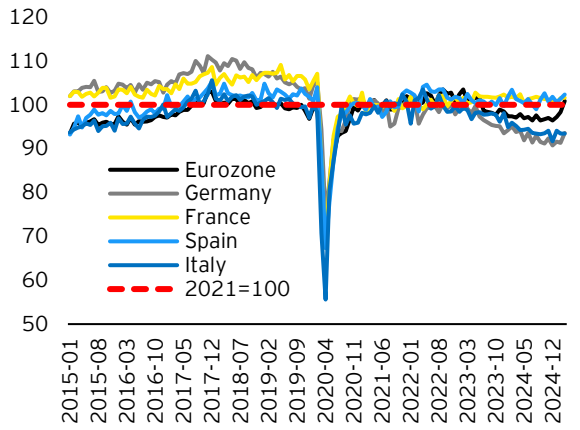
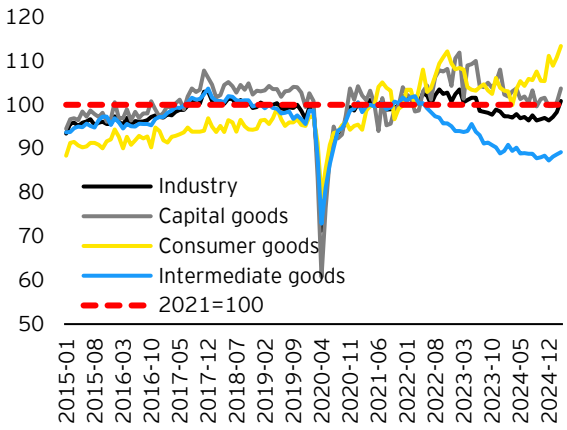


Figure 26: Industrial production by type of good, Eurozone – index, 2021=100



Source: EY elaborations on Eurostat data. For industrial production, reference is made to NACE Rev. 2 BD codes (*Mining* and *quarrying; manufacturing; electricity, gas, steam and air conditioning supply*). Latest observation: March 2025.

While the overall recent performance appears notably positive at an aggregate level, it is important to recognise that the manufacturing sectors in the two main Eurozone economies—Germany and Italy—continue to exhibit significant weaknesses. Additionally, the Eurozone's aggregate performance does not fully align with the industrial production trends observed in these four principal countries. This discrepancy is largely attributable to the strong growth recorded in Irish industry, which saw an average increase of approximately

32% between January and March 2025. This exceptional growth, coupled with the general volatility of Ireland's industrial production figures, can be largely explained by Ireland's central role as a hub for numerous multinational corporations.

Analysing the main macro-categories of industrial goods, the production of intermediate goods remains the most critical sector. March marked the thirty-fourth consecutive month of year-on-year decline, with a contraction of 0.3%, following a 2.4% reduction in December. However, from a cyclical perspective, March saw a growth of 0.6%, consistent with the gains recorded in the previous months (0.6% in February and 1.0% in January). Conversely, the production of capital goods and consumer goods is on the rise, with monthly increases of 3.2% and 2.3%, respectively, corresponding to year-on-year growth rates of 0.6% and 13.5%.

The analysis of PMI indicators[54] for the manufacturing and services sectors provides valuable and timely insights into the performance of key economic areas. Recent manufacturing PMI readings indicate a generally subdued sentiment, although with some signs of improvement. In April 2025, the four largest Eurozone countries recorded PMI values below the expansion threshold of 50, albeit with varying trends. Spain, for instance, has experienced a decline in manufacturing business confidence since the latter months of the previous year, reaching levels just below the expansion threshold. In contrast, France, Italy, and Germany have maintained PMI values below 50 for nearly two years, with only occasional deviations, despite some recovery observed in recent months.

The situation in the services sector is similarly complex. Spain and Italy both report PMI values above the expansion threshold, although Spain exhibits a downward trend while Italy shows signs of improvement. Meanwhile, France continues to remain below the expansion threshold, and Germany has experienced a decline in sector confidence since the beginning of 2025.

Figure 27: Purchasing Managers Index (PMI), manufacturing

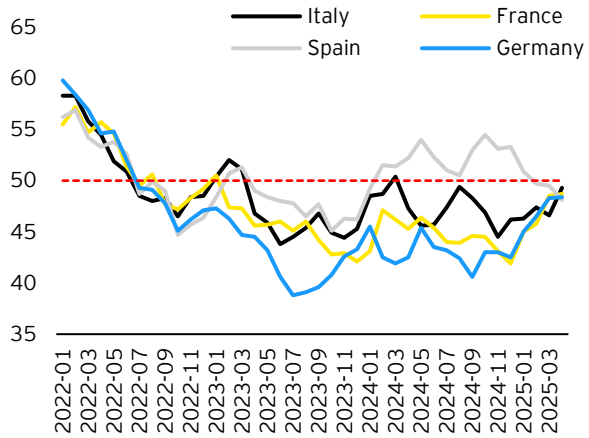
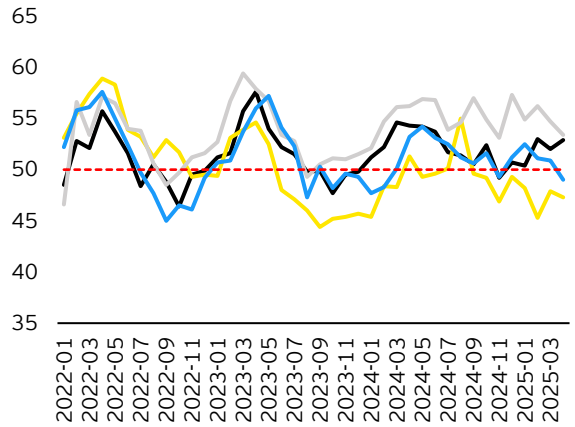


Figure 28: Purchasing Managers Index (PMI), services



Source: EY elaborations on S&P Global data. Latest observation: April 2025.

Monetary Policy and Prices in the Eurozone

On 5 June 2025, the European Central Bank decided to implement a further reduction in its key monetary policy interest rates.[55] This decision is supported by the anticipated inflation trajectory and its underlying dynamics.

According to the latest Eurosystem staff macroeconomic projections, headline inflation is expected to average 2.0% in 2025, 1.6% in 2026, and 2.0% in 2027.[56] The downward revisions compared to the March

[54]The PMI (Purchasing Managers' Index) is one of the most popular economic indices, i.e. an index of the prevailing direction of economic trends in the manufacturing, construction and services sectors, obtained thanks to timely surveys conducted on the most representative companies in the reference sectors. Values above 50 indicate a growth trend in economic activity, values below 50 a decrease.
[55]ECB, Monetary policy decisions, 5 June 2025. For more information, https://www.ecb.europa.eu/press/pr/date/2025/html/ecb.mp250605~3b5f67d007.en.html .
[56]Eurosystem staff Macroeconomic projections for the euro area, June 2025. For more information, https://www.ecb.europa.eu/pub/pdf/other/ecb.projections202506_eurosystemstaff~16a68fbaf4.en.pdf .

projections - amounting to 0.3 percentage points for both 2025 and 2026 - primarily reflect lower energy price assumptions and an appreciation of the exchange rate. Regarding core inflation, average values are expected to range between 2.4% in 2025 and 1.9% in 2026 and 2027, remaining largely unchanged from the March projections.[57]

These projections are also justified by the prevailing context of high uncertainty, where adverse trade policies could exacerbate trade tensions in the coming months, potentially resulting in lower-than-expected economic growth and price levels.

Consequently, the interest rates for the main refinancing operations, the marginal lending facility, and the deposit facility[58] have been set at 2.15%, 2.40%, and 2.00%, respectively.

Figure 29: Reference interest rates of the European Central Bank's monetary policy

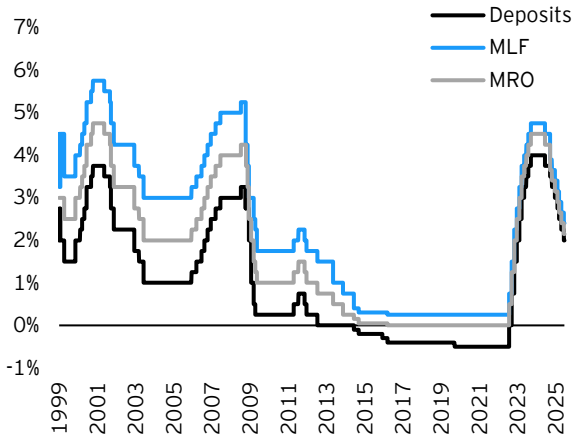
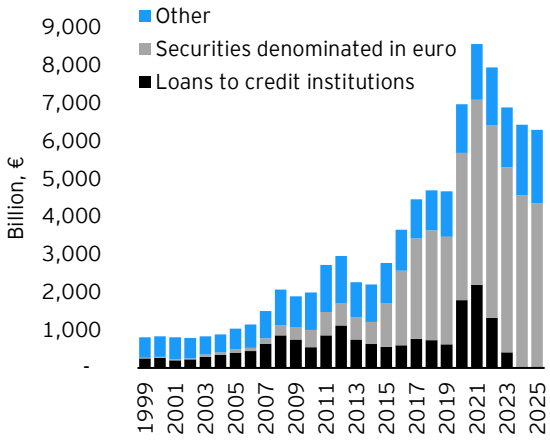


Figure 30: Main balance sheet items of the European Central Bank (€, billion)



Source: EY elaborations on European Central Bank (ECB) data. MLF = marginal lending facility; MRO = main refinancing operation. The deposit rate refers to deposits at the central bank. Balance sheet items - loans to credit institutions: it refers to loans to Eurozone credit institutions related to monetary policy operations denominated in euro (the different items include main refinancing operations and LTROs); securities denominated in euro: it refers to Eurozone residents' securities denominated in euro (the different items include assets acquired for monetary policy purposes); other: the different items include gold and claims denominated in foreign currency on Eurozone residents and non- Eurozone residents. The Latest observation for 2024 refers to the *weekly financial statement* dated May 23, 2025.

Focusing on the effects of the restrictive monetary policy adopted in recent years, it has not only contributed to bringing inflation closer to the price stability target but has also had notable repercussions on the emerging economies of Europe. Research indicates that monetary tightening by the ECB results in more than proportional increases in government bond yields in "emerging Europe"—a group that includes Albania, Belarus, Bosnia and Herzegovina, Bulgaria, Croatia, Hungary, Kosovo, North Macedonia, Moldova, Montenegro, Poland, Romania, Serbia, and Turkey (excluding Russia and Ukraine due to the ongoing conflict). These effects are accompanied by significant widening of government bond spreads, depreciation of local currencies, and a substantial decline in economic output.[59] This phenomenon pertains both to "conventional" monetary policy—primarily implemented through interest rate hikes—and to balance sheet reductions by the Central Bank. The impact tends to be moderate when tightening measures are implemented predictably but can become significant if the pace of tightening accelerates. Moreover, the adverse effects are generally more pronounced under a fixed exchange rate regime compared to an inflation-targeting regime with a freely floating currency.

[57]Eurosystem staff Macroeconomic projections for the euro area, March 2025. For more information, https://www.ecb.europa.eu/press/projections/html/ecb.projections202503_ecbstaff~106050a4fa.en.html .
[58]The deposit facility rate is one of three key interest rates that the ECB sets every six weeks as part of its monetary policy decisions. This rate defines the interest that banks earn on their overnight (one working day) deposits with the central bank. The other two key interest rates are the main refinancing operations (MRO) rate and the marginal lending facility (MRO) rate. The MRO rate defines the cost at which banks can obtain credit from the central bank with a maturity of one week. If banks need overnight liquidity, they can use the marginal lending facility at a higher rate. For more information, see https://www.ecb.europa.eu/stats/policy_and_exchange_rates/key_ecb_interest_rates/html/index.en.html .
[59]Engler, P., Ferrucci, G., Zabczyk, P., & Zheng, T. (2024). ECB Spillovers to Emerging Europe: The Past and Current Experience. IMF Working Paper WP/24/170, 2024 Aug.

In this context, it is important to emphasise that the rise in interest rates coincides with a broader normalisation of monetary policy, which also entails a reduction in the European Central Bank's balance sheet. Considering the net asset purchases made between July 2022—the month when the first increase in monetary policy interest rates occurred—and the most recent data available (May 2025), a ranking can be established regarding the extent of the reduction in public debt purchases by the ECB through its two main programs (PSPP and PEPP) across Eurozone countries. Specifically, Germany, Austria, and Italy rank highest in terms of the volume of public debt securities sold by the ECB as a percentage of GDP, amounting to approximately 4.6%, 4.8%, and 6.1% respectively. Conversely, Estonia continues to benefit from the public debt purchase program, recording positive net purchases below 1% of GDP, while Malta, Slovenia and Luxembourg have experienced slightly negative overall net purchases.

Figure 31: Net purchases of public debt from July 2022 to May 2025 (% of sum of last four quarters of GDP)

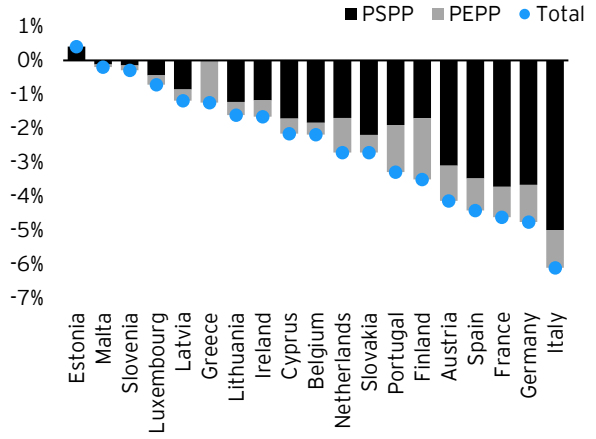
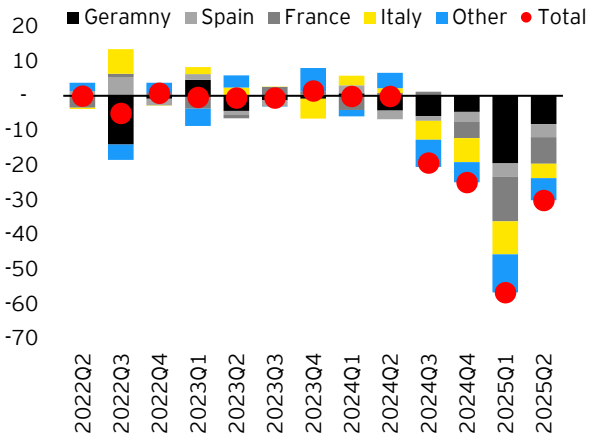


Figure 32: Net purchases of government debt securities through PEPP from 2022-Q2 to 2025-Q2 (billion, €)



Source: EY elaborations on Eurostat data, European Central Bank. Latest observation: May 2025; the second quarter of 2025 shows partial data (up to May 2025).

The restrictive monetary policy cycle implemented since mid-2023, combined with a varying degree of easing in certain external factors—such as the trend in raw material prices—has effectively contributed to bringing inflation back within target levels.

Figure 33: Inflation rate, Eurozone – % change YoY

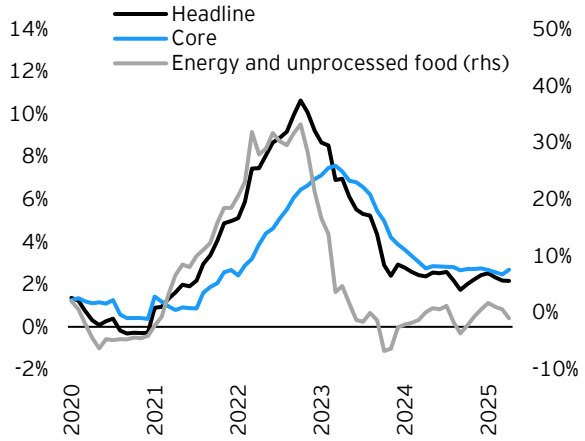
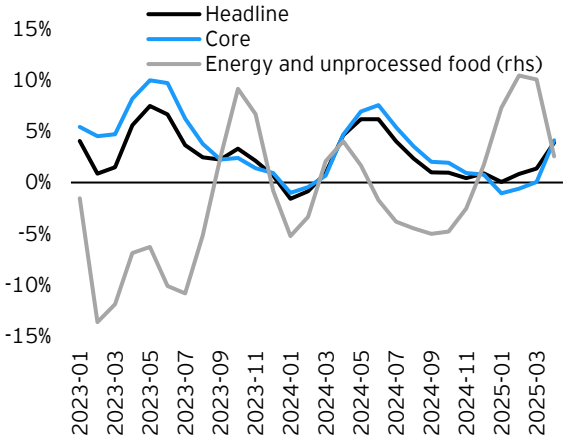


Figure 34: Inflation rate, Eurozone – 3-month on 3-month annualised % change



Source: EY elaborations on Eurostat data. The *headline measure* considers all goods in the basket used to calculate the price change; the *core measure considers the goods in the headline* basket excluding energy and fresh food. The rates refer to the harmonised rates. Latest observation: April 2025.

Headline inflation in the Eurozone, which accounts for all goods in the consumer basket used to monitor price trends, stood at 2.2%. Although this figure is lower than the 2.5% recorded in January, it is important to note that inflation experienced a sustained increase from September 2024 (1.7%) through early 2025.

Core inflation, which excludes the most volatile components such as energy and fresh food,[60] remains higher and persistent, reaching 2.7% in April compared to 2.5% in March. A similar pattern was observed during the pandemic crisis when energy prices fell sharply due to the slowdown in global economic activity; in such cases, a core inflation rate exceeding headline inflation indicates that the underlying inflation components are rising faster than energy and fresh food prices.

These inflation dynamics described are further corroborated by the quarterly analysis of the consumer price index, which has shown a deceleration in its rate of decline in recent months. When calculating the annualised rate of change[61] of the quarterly average consumer price index compared to the previous quarter, it is clear that, while the energy and unprocessed food components have decreased following significant increases towards the end of 2024, the core component has been rising. This upward trend in the core component is also reflected in the overall consumer price index.

Overall, it can be affirmed that the European Central Bank's monetary policy has played a significant role in curbing the growth of the price level, especially considering that approximately 33% of the components comprising the core inflation basket are directly influenced by monetary policy decisions (for instance, goods commonly purchased through financing or credit).[62]

Trends in consumer prices are also partly attributable to the positive developments in the Eurozone labour market. Although the labour market remains robust, it has shown signs of slight cooling. One useful tool for analysing these dynamics is the Beveridge curve, which examines the relationship between the unemployment rate and the job vacancy rate,[63] thereby offering insights into the overall health of the economy and the labour market's characteristics.

The relationship between the two variables under analysis is generally inverse: a higher unemployment rate is typically associated with a lower job vacancy rate, and vice versa. By examining the dynamics of the Beveridge curve across three key periods over the past 15 years—namely, 2010 to 2014 (following the financial crisis and including the sovereign debt crisis), 2015 to 2020 (encompassing the pandemic), and 2021 to 2025 (post-pandemic period marked by increased uncertainty due to adverse geopolitical events)—valuable insights can be gained.

The segment of the Beveridge curve for the period 2021–2025 was initially characterised by a steeper slope compared to the previous two periods, indicating a labour market where companies faced greater difficulty in finding the necessary workforce to carry out their activities. This situation enhanced workers' bargaining power, potentially leading to higher wage increases during negotiations. In recent quarters, however, a decline in the vacancy rate has been observed, signaling a partial cooling of the labour market, which nonetheless remains marked by historically low unemployment levels (approximately 6% at the end of 2024). This labour market trend in the Eurozone exerts a dual effect on the inflation rate. On one hand, the reduction in the vacancy rate lessens upward pressure on wages, thereby decreasing their capacity to support consumption and consequent price increases. On the other hand, the decline in inflation enhances households' real income, which may positively influence consumption and, as a result, contribute to rising prices.

[60] Reference is made to the ISTAT definition of core inflation, which considers the consumer price index net of variations in energy products and fresh food products.
[61] The annualised rate of change is used to reflect the amount of change in a variable over a year if it had continued to grow at the specified rate. For more information, see https://www.dallasfed.org/research/basics/annualizing .
[62] Allayioti, A., G ó rnicka, L., Holton, S., & Hernández, C. M. (2024). Monetary policy pass-through to consumer prices: evidence from granular price data. European Central Bank, Working Paper Series No 3003.
[63] The job vacancy rate is defined as the ratio of the number of vacancies to the sum of the number of occupied posts and the number of vacancies. A vacancy is defined as a paid post that is newly created, unfilled or about to become vacant (i) for which the employer is taking active steps and is prepared to take further steps to find a suitable candidate outside the undertaking concerned; and (ii) which the employer intends to fill immediately or within a specific period of time. For more information, see https://ec.europa.eu/eurostat/statistics-explained/index.php?title=Glossary:Job_vacancy_rate_(JVR) .

Figure 35: Beveridge Curve, Eurozone

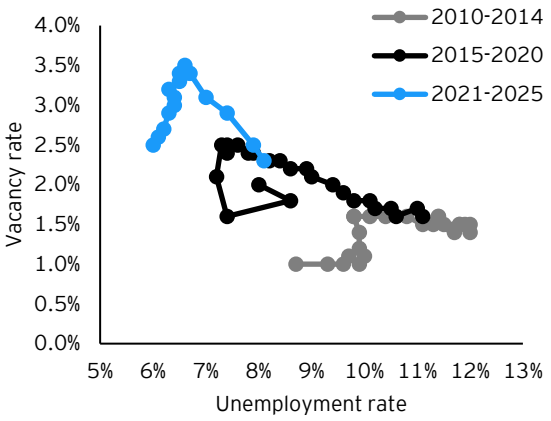
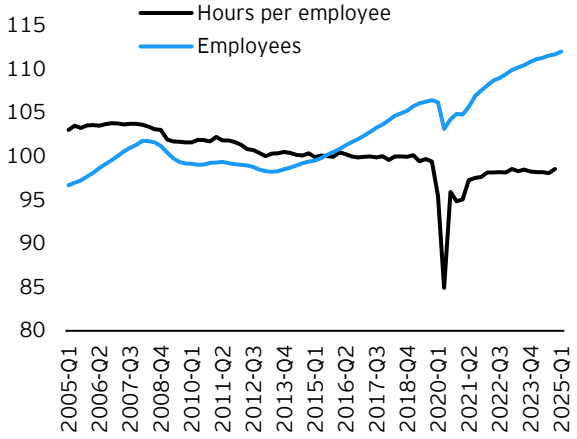


Figure 36: Hours per employee and number of employees, Eurozone – index, 2015=100



Source: EY elaborations on Eurostat data.

Regarding the labour market, the number of employees continues to increase, reaching historic highs not seen since 1995, with approximately 172 million people employed in the first quarter of 2025.[64] However, it is noteworthy that despite this increase in employment, the average number of hours worked per employed person is declining, suggesting a structural transformation within the labour market.

This phenomenon is not limited to recent quarters but reflects a long-term structural trend, as illustrated in Figure 36.[65] Moreover, it is not exclusive to the Eurozone economies: average working hours in developed countries have been declining over an extended period. For instance, in Germany, average working hours halved between 1870 and 2000.[66] More broadly, average working hours in OECD countries decreased by approximately 0.5% annually from 1870 through the early 2000s, with the post-war United States as a notable exception.[67] This structural reduction in working hours has been examined in several OECD reports,[68,69] which identify both the expansion of workers' rights and technological advancements as key factors contributing to the sustained decline in average working hours over the past two centuries.[70]

Due to the decline in inflation and the persistence of relatively high - though decreasing - monetary policy interest rates, real interest rates have returned to positive territory since the end of 2023.

[64]Both employed and self-employed persons are considered. For more information, https://ec.europa.eu/eurostat/cache/metadata/en/namq_10_esms.htm .
[65]Astinova, D., Duval, R., Hansen, N. J., Park, B., Shibata, I., Toscani, F. (2024). Dissecting the Decline in Average Hours Worked in Europe. International Monetary Fund, Working Paper, WP/24/2, January 2024.
[66]Messenger, J.C., Sangheon, L., McCann, D., (2007). Working Time Around the World: Trends in Working Hours, Laws, and Policies in a Global Comparative Perspective, International Labor Organization, Routledge, May 2007.
[67]Boppart, T., Krusell, P., (2020). Labor Supply in the Past, Present, and Future: A Balanced-Growth Perspective. The University of Chicago Press, January 2020, 128 (1), 118-157.
[68]OECD, "Working Hours: Latest Trends and Policy Initiatives," in "OECD Employment Outlook 1998: June" OECD Employment Outlook, Paris: Organization for Economic Co-operation and Development, 1998, pp. 153-188.
[69]OECD, "Working Time and Its Regulation in OECD Countries: How Much Do We Work and How?," in "OECD Employment Outlook 2021: Navigating the COVID-19 Crisis and Recovery" OECD Employment Outlook, Paris: Organization for Economic Co-operation and Development, July 2021.
[70]Greenwood, J., Vandenbroucke, G., (2005). Hours Worked: Long-Run Trends. NBER, Working Paper 11629.

Figure 37: Real interest rate, Eurozone – Households (house purchase)

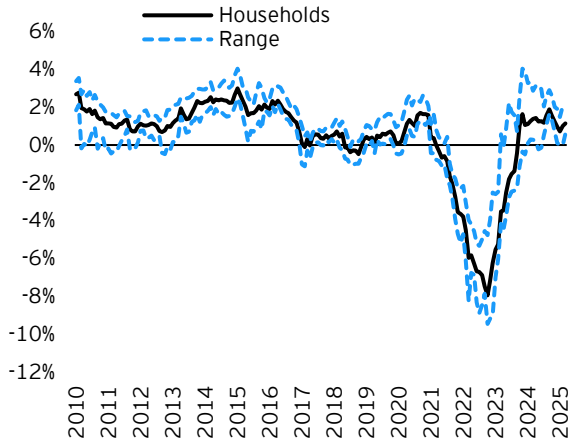
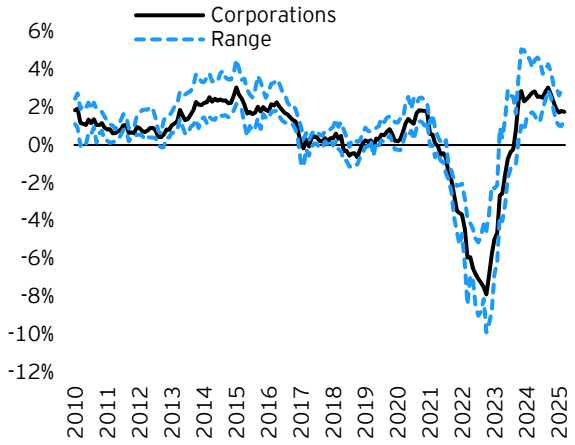


Figure 38: Real interest rate, Eurozone – Corporations



Source: EY elaborations on Eurostat, ECB data. Latest observation: March 2025.

Closely related to the issue of interest rates is the matter of bank lending and economic growth in the Eurozone. A recent study has demonstrated that the increases in the European Central Bank's key interest rates between July 2022 and September 2023 have significantly dampened GDP growth and inflation, partly due to their impact on the supply of bank credit.[71] In this context, the latest edition of the Eurozone Bank Lending Survey[72] provides valuable insights into this subject.[73]

In the first quarter of 2025, Eurozone banks reported a slight net tightening of credit supply conditions for businesses, with a net rate of 3%. This continued the tightening trend seen in the fourth quarter of 2024 but at a lower intensity than the 10% expected in the previous survey. Specifically, the tightening was milder than anticipated in Germany and France, while in Italy, lending conditions remained largely unchanged, contrary to expectations of easing.

This tightening was primarily driven by German banks, whereas France, Italy, and Spain saw largely stable credit conditions. The overall net tightening rate of 3% is below the long-term historical average of 9% since 2003.

The main factors behind this further tightening are an increased perception of risk, related to both the general economic outlook and the specific situations of individual companies. This aligns with trends in asset quality indicators, such as the ratio of non-performing loans (NPL) to total loans, and lending criteria. Additionally, some banks have reported heightened caution when assessing companies more vulnerable to macroeconomic uncertainties and economic policies, particularly those heavily reliant on exports to the United States.

Banks' risk tolerance had a broadly neutral effect this quarter, after having contributed to tightening previously. The cost of raising funds, balance sheet constraints, and competition among banks also had neutral impacts, consistent with recent quarters. German, French, and Italian banks reported increased risk perceptions.

[71] Conti, A. M., Neri, S., & Notarpietro, A. (2024). *Credit strikes back: the macroeconomic impact of the 2022-23 ECB monetary tightening and the role of lending rates* (No. 884). Bank of Italy, Economic and Financial Issues (Occasional Papers).
[72] The Bank Lending Survey (BLS) has been conducted since January 2003 by the national central banks of the countries that have adopted the single currency in collaboration with the European Central Bank. It is addressed to credit policy makers of the main banks in the area (about 150). The survey allows to highlight in a distinct manner, on the one hand, the factors that influence the supply of credit as well as the terms and conditions practiced to customers and, on the other, the trend of the demand for credit with the related determinants.
[73] The euro area bank lending survey - First quarter of 2025.

Figure 39: Conditions of supply of bank loans to businesses, Eurozone – net percentage of respondents

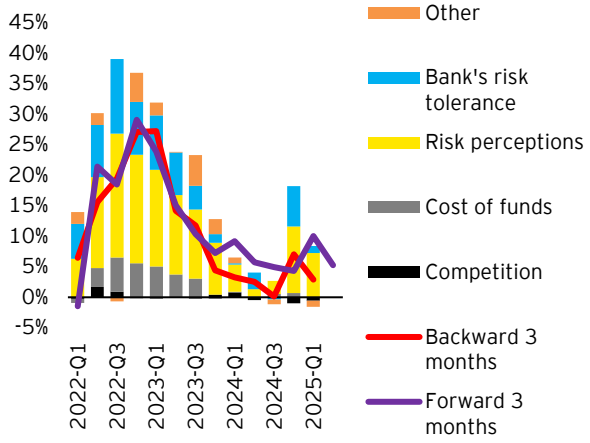
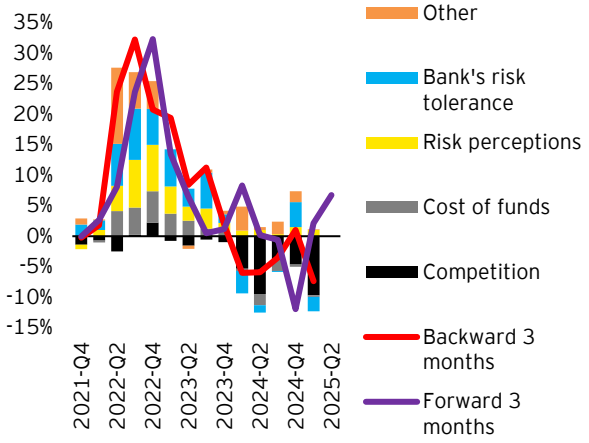


Figure 40: Conditions of supply of bank loans to households, Eurozone – net percentage of respondents



Source: EY elaborations based on European Central Bank data (Bank Lending Survey). For households, this refers to the supply conditions for home loans. Net percentages are defined as the difference between the sum of the percentages of banks responding, "significantly tightened" and "slightly tightened" and the sum of the percentages of banks responding 'slightly loosened' and "significantly loosened" in reference to the change in credit conditions. Net percentages for responses to questions on contributing factors are defined as the difference between the percentage of banks reporting that a particular factor contributed to tightening and the percentage of banks reporting that it contributed to loosening.

Regarding household lending in the first quarter of 2025, Eurozone banks reported a moderate easing of credit standards for house purchase loans, with a net rate of 7%. This marked a return to easing after a projected slight tightening of 2%, following largely unchanged standards in the previous quarter.

There was notable variation among the main Eurozone countries: in France, banks continued to ease credit standards for the fifth consecutive quarter; Germany recorded its first easing since the start of interest rate cuts; Spain saw no change in standards for home purchases; while Italy experienced further tightening for the second consecutive quarter.

The primary driver of this easing in mortgage lending conditions was increased competition among banks, with a smaller contribution from improved risk tolerance. Looking ahead to the second quarter of 2025, Eurozone banks expect credit standards for house purchase loans to tighten again, with an expected net balance of 7%. This anticipated tightening is mainly linked to banks in France and Germany, whereas banks in Italy and Spain foresee standards to remain broadly stable.

Talking about consumer price index growth, it is noteworthy that inflation dynamics are influenced by the size of public debt. A recent ECB study examined the interaction between fiscal policy and inflation in the Eurozone, revealing that the level of public debt plays a key role in this relationship. Specifically, high public debt levels tend to amplify inflation's response to fiscal expansions or contractions, meaning that fiscal policy's impact on prices is stronger when debt is high.[74]

Overall, public debt-to-GDP ratios across Eurozone countries have risen significantly due to fiscal responses to the pandemic and energy shocks. These ratios remain elevated compared to the pre-pandemic period, reflecting the sustained fiscal efforts to support economies amid these crises.

[74]With reference to the relationship between public debt and inflation, according to the so-called fiscal theory of prices, an expansionary fiscal policy not accompanied by higher expected future primary surpluses leads to the perception of economic agents of greater real wealth, leading to an increase in consumption and, consequently, in prices. More generally, if the present value of future primary surpluses is lower than the amount of nominal debt, the equilibrium price level is expected to increase (reducing the real value of the debt) to ensure its solvency. For more information, Checherita-Westphal, CD, & Pesso, T. (2024). Fiscal policy and inflation: accounting for non-linearities in government debt. ECB Working Paper Series No 2996.

Figure 41: Changes in the public debt-to-GDP ratio, 2019-Q4-2024-Q4

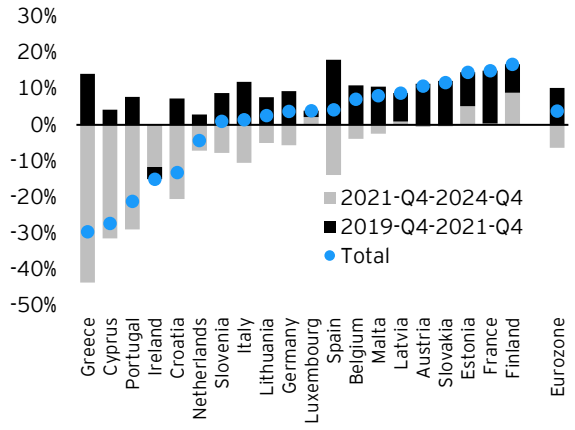
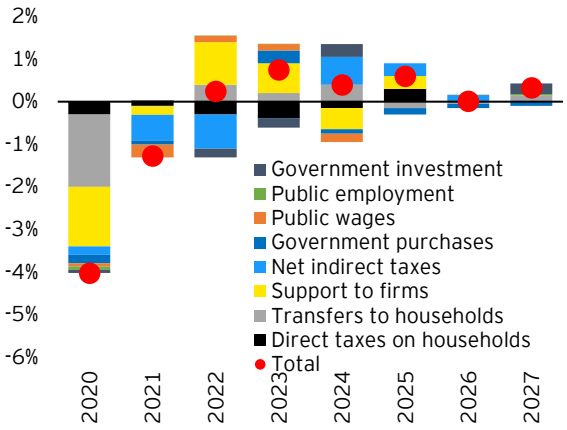


Figure 42: Fiscal policy measures by type of intervention, Eurozone - % of GDP



Source: EY elaborations on European Central Bank data.

It is important to note, however, that fiscal policy measures adopted since 2020 have had significant macroeconomic effects, particularly in supporting real GDP growth between 2020 and 2022. In the subsequent years, their impact on growth has been more limited or essentially negligible. Regarding inflation, specific measures introduced in 2022 helped mitigate the adverse effects of the energy shock.[75] However, from 2023 onwards, the gradual withdrawal of these measures, combined with lingering pressures from prior fiscal stimulus, has contributed to upward pressure on prices.[76]

Figure 43: Effect of fiscal policy measures on real GDP growth

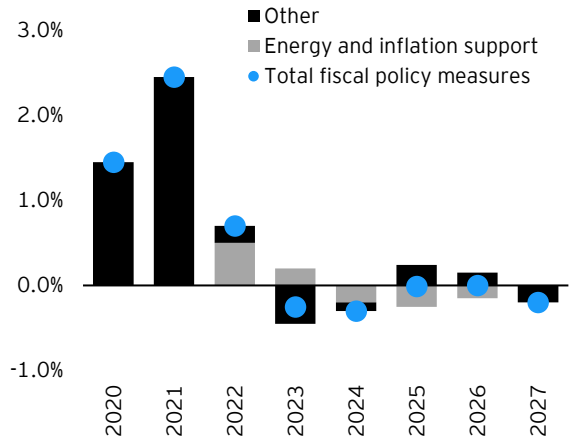
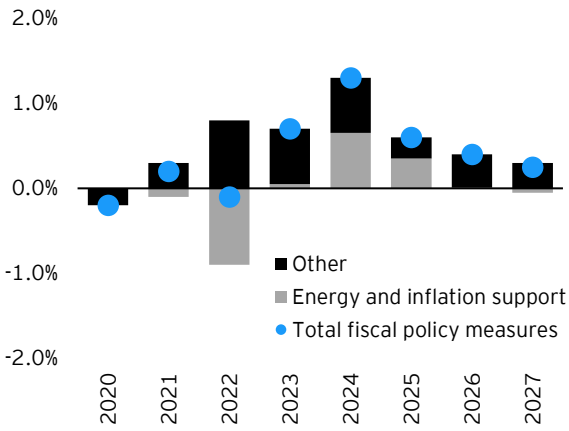


Figure 44: Effect of fiscal policy measures on inflation growth



Source: EY elaborations on European Central Bank data.

There are also potential medium- and long-term spending pressures arising from increased defense expenditures, the climate transition, and population aging. This situation raises the risk that the public debt-to-GDP ratio may not stabilise in the medium term. In the Eurozone, the ECB's bond purchase programs have helped member countries maintain a long-term issuance profile, thereby easing short-term financing pressures.[77]

[75]Checherita-Westphal, C., & Dorrucci, E. (2023). Update on euro area fiscal policy responses to the energy crisis and high inflation. *Economic Bulletin Boxes*, *2*.
[76]Angelini, E., Bańkowski, K., Checherita-Westphal, C., Muggenthaler-Gerathewohl, P., & Zimic, S. (2025). The macroeconomic impact of euro area discretionary fiscal policy measures since the start of the pandemic. *Economic Bulletin Boxes* , *3* .
[77]Armendariz, S., Cabezon, E., Cui, M.L.Q., Domit, S., Iancu, A., Magistretti, G., ... & Wong, Y.C. (2024). *Taming Public Debt in Europe: Outlook, Challenges, and Policy Response* (No. 2024/181). International Monetary Fund. IMF Working Paper WP/24/181, 2024 Aug.

Overall, the Eurozone's situation remains complex. Economic activity is relatively weak, with the industrial sector still facing challenges. While restrictive monetary policy has been important in curbing inflation, the pace of price level reduction has slowed recently, partly due to strong labour market dynamics and wage growth.

Added to this are uncertainties stemming from the effects of trade-distorting policies—such as tariff barriers on imports—implemented by the new U.S. administration, alongside potential retaliatory measures from affected countries. In this context, a recent EY study has estimated the potential economic impact of these measures on both the European Union and the Eurozone.[78]

Specifically, the EY Economic Advisory team estimates that by 2027, the peak impact of additional tariffs will reduce GDP by 0.7 percentage points for both the European Union and the Eurozone compared to a scenario without these measures. Spain is expected to experience the smallest impact (-0.4 percentage points), while Ireland faces the largest contraction (-1.2 percentage points). Italy's GDP is projected to contract by about 0.7 percentage points, similar to the overall Eurozone impact, and slightly less than Germany's expected contraction of 0.8 percentage points.

Figure 45: Percentage deviation from GDP in the year of maximum effect of additional duties imposed – percentage points

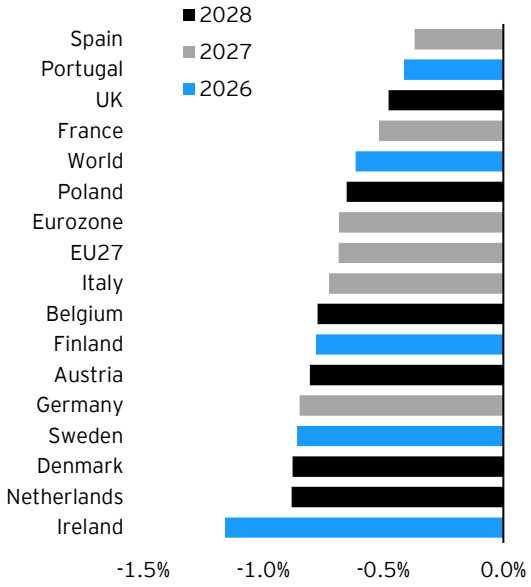
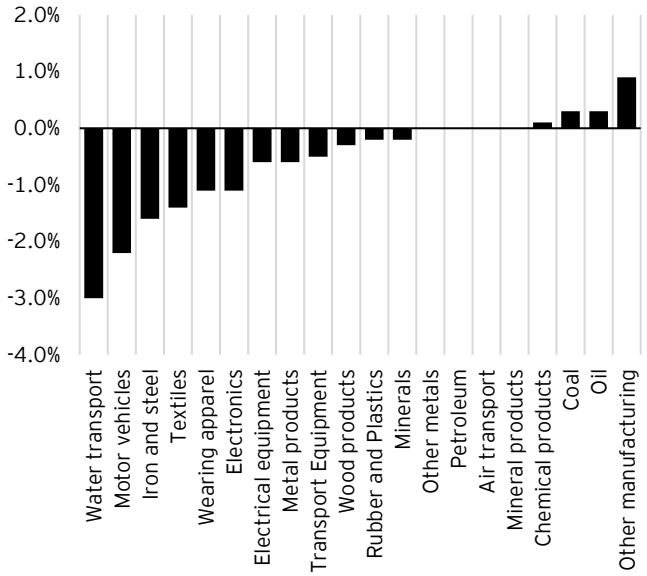


Figure 46: Percentage deviation from value added in the long run (10 years) following additional tariffs imposed and trade retaliation – percentage points



Source: EY Economic Advisory team elaborations.

The EY Economic Advisory team's GDP impact estimates align with those from the ECB, which projects that trade distortions will reduce GDP growth rates in 2025, 2026, and 2027 from 0.9%, 1.1%, and 1.3% respectively, down to 0.5%, 0.7%, and 1.1%. This results in a cumulative GDP reduction of 1 percentage point by 2027 compared to a scenario without new trade restrictions. These projections correspond to the "severe scenario" outlined in the ECB's latest Eurosystem staff macroeconomic projections for the Eurozone.[79]

Over the long term (10 years), the Eurozone sectors projected to face the largest negative impacts from additional tariffs are maritime transport (-3.0 percentage points), motor vehicles and related parts production (-2.2 percentage points), and iron and steel production (-1.6 percentage points). Conversely, the oil and gas extraction, coal mining, and chemicals sectors are expected to see modestly higher growth

[78]EY - European Economic Outlook: What Will Tariffs Bring?. For more information, https://www.ey.com/en_pl/insights/economic-analysis-team/ey-european-economic-outlook-may-2025.
[79]Eurosystem staff Macroeconomic projections for the euro area, June 2025. The "severe" scenario envisages a further broad-based increase in US tariffs (in line with the announcement of so-called "reciprocal" tariffs in the US), symmetric retaliation by the EU and continued heightened trade policy uncertainty. For more information, see https://www.ecb.europa.eu/pub/pdf/other/ecb.projections202506_eurosystemstaff~16a68fbaf4.en.pdf.

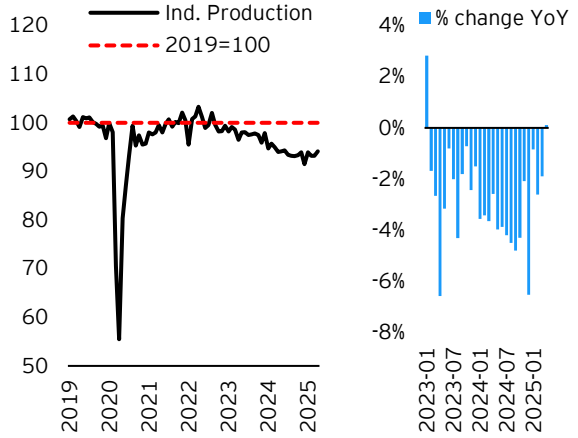
compared to a no-tariff scenario, with deviations from the baseline of +0.3, +0.3, and +0.1 percentage points respectively.

The Italian economy

The real economy

Italian industrial production still shows an overall negative trend, despite recording a year-over-year growth in April (0.3% on calendar-adjusted data and 0.1% on seasonally adjusted data). This April figure marks the first positive year-over-year growth after twenty-six consecutive months of decline.

Figure 47: Industrial production index (average 2019=100) and % YoY change, Italy



Source: EY elaborations on ISTAT data. The indices refer to the seasonally adjusted indices. Latest observation: April 2025.

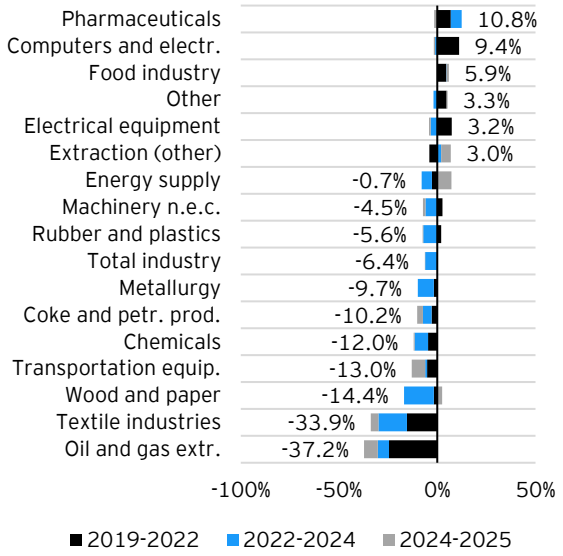
This data comes after negative trend growths of -1.9% in March and -2.6% in February.

Despite the slight recovery in April, industrial production remains , on average, about 6% below the 2021 levels. It is also important to note that there is significant variation across different sectors

In the manufacturing sector, April 2025 saw notable divergences in performance across industries. The pharmaceutical industry experienced the largest year-on-year decline, contracting by 10.5%. This was followed by the manufacturing of means of transport, which fell by 9.7%, and the production of coke and petroleum refining products, which decreased by 5.0%. Conversely, the wood and paper industry and the food industry posted the most significant growth, increasing by 3.8% and 2.5%, respectively.

Taking a longer-term perspective, additional insights into Italy's industrial performance can be observed. Compared to 2019, the pharmaceutical industry, the manufacturing of computers and electronic products, and the food industry stand out as the top three sectors with the strongest growth, registering increases of 10.8%, 9.4%, and 5.9%, respectively, in production.

Figure 48: Industrial production index by industrial sector, Italy – % change compared to 2019 and contributions for years analysed

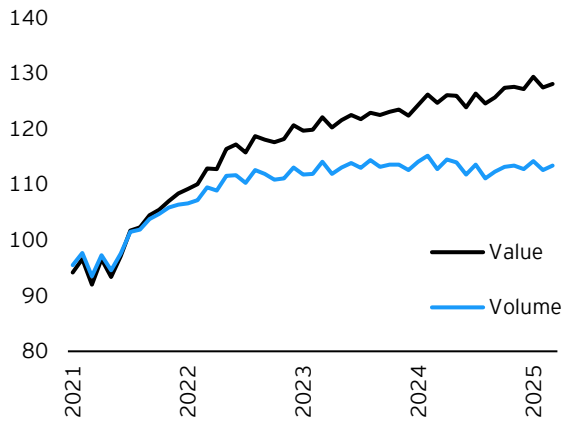


Source: EY elaborations on ISTAT data. Machinery nca: Manufacture of machinery and equipment not classified elsewhere.

Conversely, certain sectors remain significantly below their pre-crisis production levels. In particular, the crude oil and natural gas extraction sector, the textile industry, the wood and paper products industry, and the transport industry have registered declines of 37.2%, 33.9%, 14.4%, and 13.0%, respectively.

Regarding the services sector, which accounts for over 70% of Italy's total added value, the trend appears mixed. While the sector shows relatively better dynamics compared to industry, its performance remains subdued. Specifically, nominal turnover in services has increased substantially—by nearly 30% since 2021. However, this growth largely reflects price level increases since 2022; in real terms, growth has been more moderate, around 13%, and has essentially stagnated since 2023.

Figure 49: Index of value and volume of turnover of services, Italy – index, 2021=100

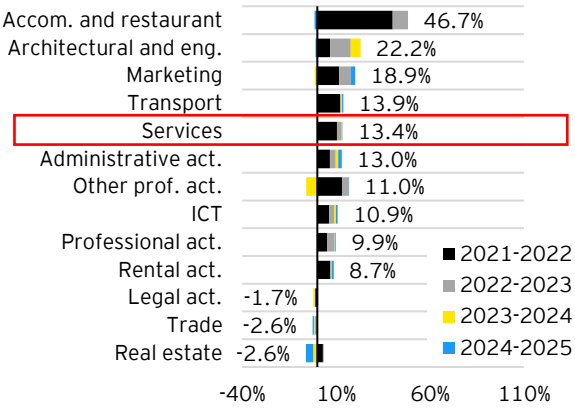


Source: EY elaborations on ISTAT data. Latest observation: March 2025.

An analysis of the data across different service sectors reveals notable heterogeneity in growth patterns. The most substantial contribution to growth occurred between 2021 and 2022, largely driven by the recovery following the pandemic crisis. However, growth has slowed in subsequent years, resulting in an overall deceleration in the real turnover of services.

Among the various sectors, accommodation and food services have been the most dynamic, with an overall growth of approximately 47%, primarily reflecting the post-pandemic rebound. This is followed by other service activities, including architecture and engineering firms, advertising and market research, transport and warehousing services, and management consultancy, all of which recorded positive growth.

Figure 50: Index of turnover volume of services, Italy – % change 2021-2025



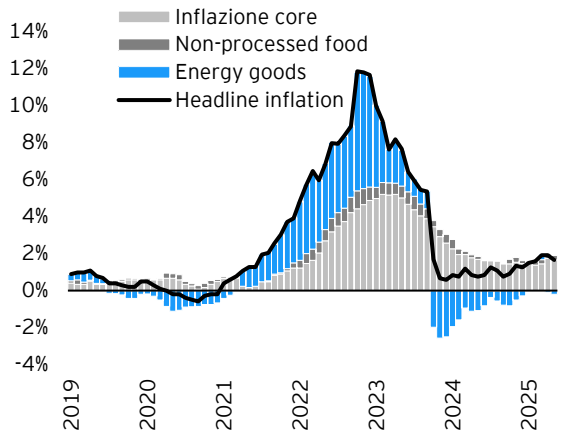
Source: EY elaborations on ISTAT data. Accommodation and food services: Accommodation and food services activities; Transport and storage: Transport and storage; Professional activities: Professional, scientific and technical activities required by the STS regulation; ICT.: Information and communication services; Rental and other: Rental, travel agencies, business support services; Real estate activities: Real estate activities; Trade: Wholesale and retail trade, repair of motor vehicles and motorcycles.

On the other hand, legal activities, wholesale and retail trade and real estate activities show overall negative growth compared to 2021 (-1.7%, -2.6% and -2.6% respectively).

Price trends and the labour market in Italy

Compared to the final months of 2024, the inflation rate has risen, reaching 1.7% in May 2025, up from an average rate of 1.2% between October and December 2024. This increase is primarily attributable to a reduction in the negative contribution from the energy component, alongside a largely stable trend in core inflation—defined as the inflation rate excluding unprocessed food and energy products.

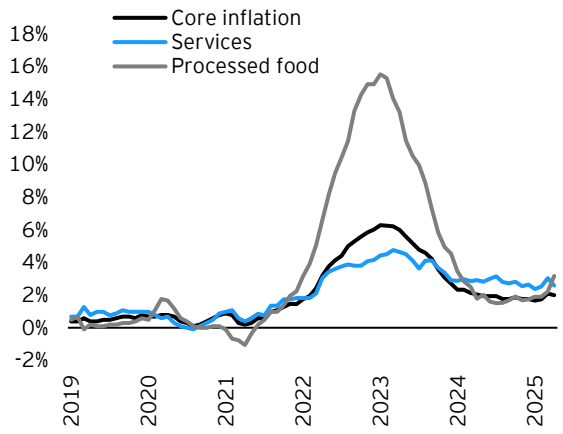
Figure 51: Inflation and components, Italy – % change YoY and percentage points



Source: EY elaborations on ISTAT data. Latest observation: May 2025.

Core inflation stood at 2.0% in May 2025, slightly down from 2.1% in April, yet still elevated compared to the first quarter of the year, when it fluctuated between 1.7% and 1.8%. This indicates a persistent upward trend in underlying inflation. A key driver of this persistence is the services sector, which recorded an inflation rate of 2.6% in May, following values ranging between 2.5% and 3.0% over the previous two months. Meanwhile, inflation in the processed food category accelerated notably, rising to 3.2% in May from 2.2% in April.

Figure 52: Core inflation and components, Italy – % change YoY and percentage points

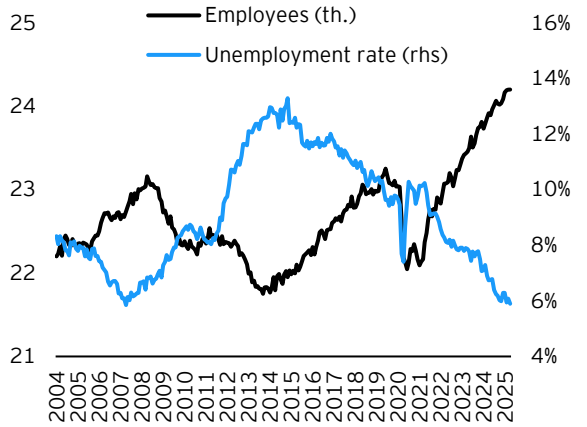


Source: EY elaborations on ISTAT data. Latest observation: May 2025.

The inflation trend is also partially influenced by labour market dynamics. Notably, total employment remains at historic highs, with approximately 24.2 million people employed. Concurrently, the unemployment rate has returned to levels last seen prior to the 2007-2008 global financial crisis, standing at around 6%.

A positive trend is also observed in real gross domestic wages, which continue to increase, recovering losses experienced in previous years. Specifically, wages grew by approximately 4.7% in the first quarter of 2025 compared to the average level recorded in 2021.

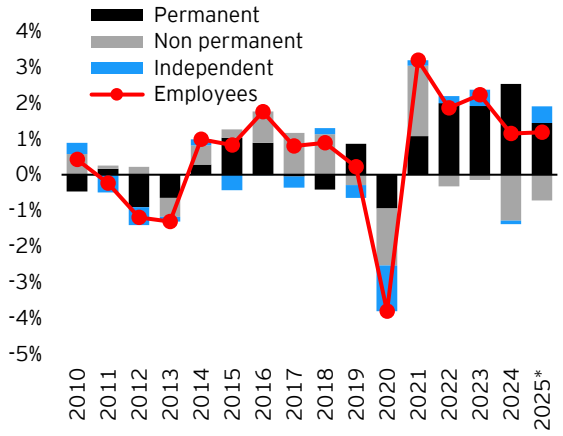
Figure 53: Employment (thousands) and unemployment rate, Italy



Source: EY elaborations on ISTAT data. Latest observation: April 2025.

Still focusing on labour market trends, it is important to highlight that the recent and sustained increase in employment has been driven primarily by growth in permanent positions, thereby contributing to greater employment stability and potentially supporting a more robust consumption trend.

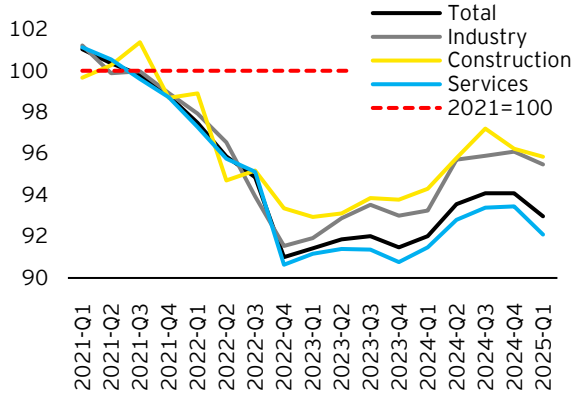
Figure 54: Employed by type of contract, Italy – % change and percentage points



Source: EY elaborations on ISTAT data. The variation to 2025 is given by the ratio between the value of April to 2025 on the value of April to 2024.

However, the overall positive trend in total incomes conceals a less favorable, albeit gradually improving, development in real wages per hour worked, which currently remain approximately 7 percentage points below their 2021 levels.

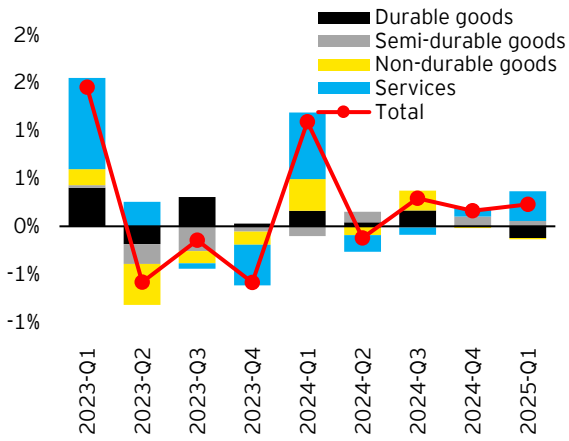
Figure 55: Real wages per hour worked in the macro-sectors of the economy, Italy – index, 2021=100



Source: EY elaborations on ISTAT data.

The positive momentum in the labour market is mirrored in consumption patterns, which registered a quarterly growth of 0.2% in the first quarter of 2025, following comparable increases of 0.2% and 0.3% in the fourth and third quarters of 2024, respectively. This growth was primarily driven by an expansion in services consumption, while spending on durable goods contracted by 1.3%.

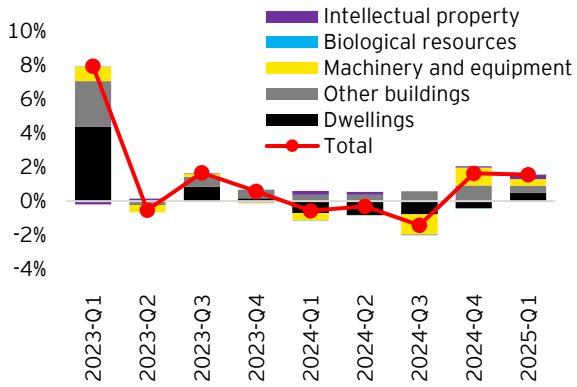
Figure 56: Final consumption expenditure of households by item of expenditure, Italy – % change QoQ and percentage points



Source: EY elaborations on ISTAT data.

Regarding other components of GDP, investment continued its positive trajectory following the last quarter of 2024, with a quarter-on-quarter growth of 1.6%, comparable to the previous quarter's performance. This expansion was partly driven by a recovery in dwellings, which grew by 1.7%, alongside increases in investment in other buildings (non-residential) and in machinery and equipment, which recorded growth rates of 1.8% and 1.2%, respectively.

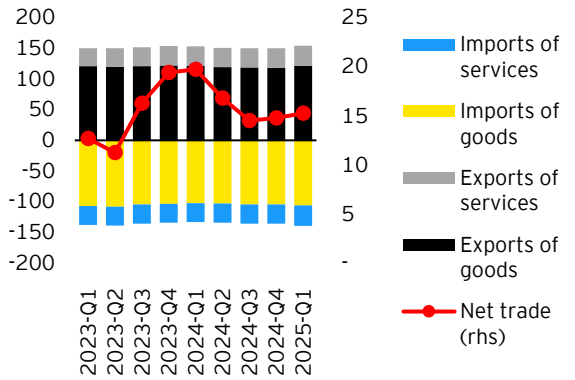
Figure 57: Investments, Italy – QoQ var. and contributions to growth



Source: EY elaborations on ISTAT data.

Finally, regarding foreign trade, Italy recorded a trade surplus of €15 billion in the first quarter of 2025, primarily driven by goods exports, which amounted to €121 billion.

Figure 58: Exports and imports, Italy – billions, €



Source: EY elaborations on ISTAT data.

Trade remains a key risk factor to be closely monitored, given the potential shifts in the geopolitical landscape and the trade policy decisions that are either threatened or already in place, contributing to heightened overall uncertainty.

The Italian economy continues to be marked by notable weaknesses, primarily due to elevated interest rates and persistent difficulties in the industrial sector, whereas the service sector displays relatively greater dynamism. Conversely, encouraging signals emerge from the labour market, with employment reaching historic highs and consumption showing signs of recovery. Inflation is exhibiting signs of acceleration, although it remains at moderate levels at present.

Focus: Italy's integration within GVCs and the risks from international trade

Main messages:

1. *In the current international and geopolitical context, it is essential to analyse the characteristics of Italian exports—both at the national and regional levels—to better understand the potential risks associated with them.*
2. *Between 2010 and 2022, the growth in the value of Italian goods exports was primarily driven by an increase in exports integrated into global value chains (GVCs). This trend was widespread across all types of goods.*
3. *Europe remains the primary market for Italian goods, accounting for approximately €392 billion in exports by 2024. However, it is important to note that the United States is the second largest destination for Italian exports, with around €65 billion, closely following Germany at approximately €71 billion. Beyond direct trade exposure, Italy also faces significant indirect exposure to the U.S. market through its participation in global value chains.*
4. *Italy's high level of integration into global value chains presents both strengths and vulnerabilities. On the one hand, it supports greater resilience to shocks in domestic demand or disruptions in traditional trade flows, owing to the broad and geographically diversified nature of its export markets. On the other hand, this deep integration heightens exposure to external shocks, which can reverberate across a wide range of domestic sectors and industries.*

In discussing international trade—and Italian exports in particular—within a geopolitical and economic landscape characterised by heightened uncertainty, it is essential to evaluate both the extent of Italy's export exposure to specific countries and its level of integration within global supply chains.

Figure 59: Exports of manufactured goods, Italy - % of "traditional" trade and GVC trade by destination, 2010

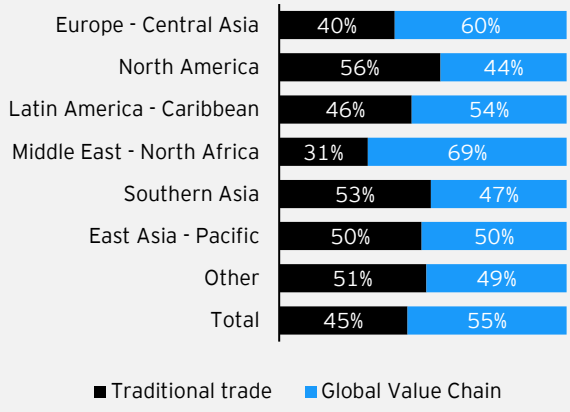
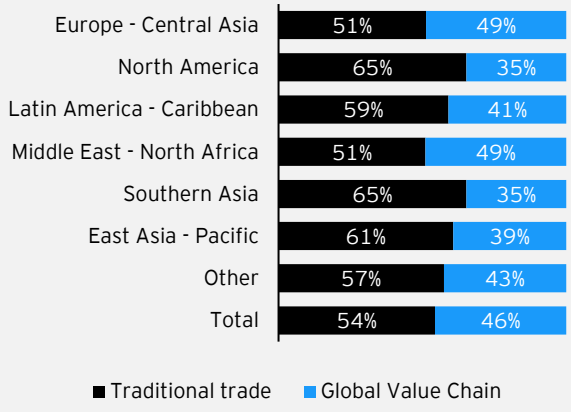


Figure 60: Exports of manufactured goods, Italy - % of "traditional" trade and GVC trade by destination, 2022



Source: EY elaborations on World Bank data (WITS). Traditional trade: goods and/or services that cross only one border; Global Value Chains: goods and/or services that cross more than one border.

Between 2010 and 2022, Italian goods exports integrated within global value chains (GVCs) increased significantly, irrespective of their geographical destination. In 2010, approximately 46% of Italian goods exports were part of GVCs—meaning the goods crossed multiple borders—while 54% followed a more

traditional trade pattern, crossing only a single border. By 2022, these proportions had effectively reversed, with 55% of exports occurring within global value chains and 45% being conducted through traditional trade.

The increasing significance of exports integrated within global value chains (GVCs) is further evidenced by the growth of total exports categorised by export channel. Between 2010 and 2022, the overall expansion in exports—approximately €325 billion—was predominantly driven by the increase in exports within GVCs, which accounted for around €210 billion of this growth. Trade within GVCs can be further classified based on the origin of inputs and the destination of the exported goods. Specifically, it is possible to distinguish between "Backward" GVC trade, referring to exports of goods that incorporate intermediate inputs imported from other countries; "Forward" GVC trade, which consists of exports of goods that serve as intermediate inputs in countries other than the final destination of the export; and "Mix" GVC trade, where exported goods combine characteristics of both backward and forward trade, involving imported intermediate goods that are further processed and consumed in countries other than the final destination. Among these categories, the "forward" component represents the largest share of Italian exports within global value chains, underlining Italy's significant role as a supplier of intermediate goods to other countries.

Figure 61: Exports of manufactured goods by destination, Italy – difference 2010-2022, €, billion

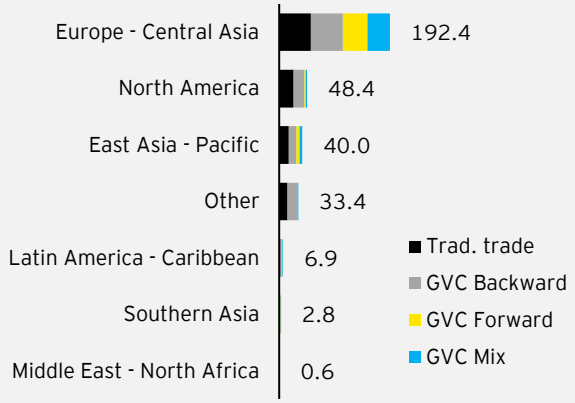
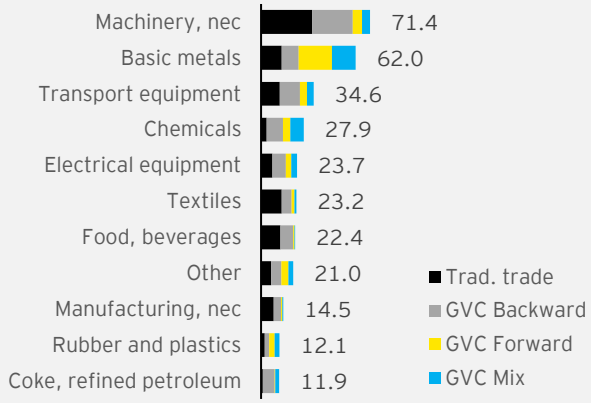


Figure 62: Exports of manufactured goods by product, Italy – difference 2010-2022, € billion



Source: EY elaborations on World Bank data (WITS), see Borin et al. (2021). Traditional trade: goods that cross only one border; Global Value Chains: goods that cross more than one border; GVC Backward: imported goods that are subsequently exported; GVC Forward: exported goods that are then exported again; GVC Mix: imported goods that are then exported to be exported again.

Global value chain (GVC) integration represents a critical factor to consider when evaluating Italy's commercial strengths and vulnerabilities. Equally important is the analysis of export destinations. From a broad macro-regional perspective, Europe remains the primary market for Italian goods, with exports valued at approximately €392 billion in 2024, followed by Asia with around €99 billion, and the Americas with €92 billion. Notably, the United States ranks as the second-largest individual country market for Italian exports, with a value of about €65 billion, just behind Germany, which accounts for approximately €71 billion.

Figure 63: Exports of manufactured goods by destination macro-regions, Italy – 2024, €, billion

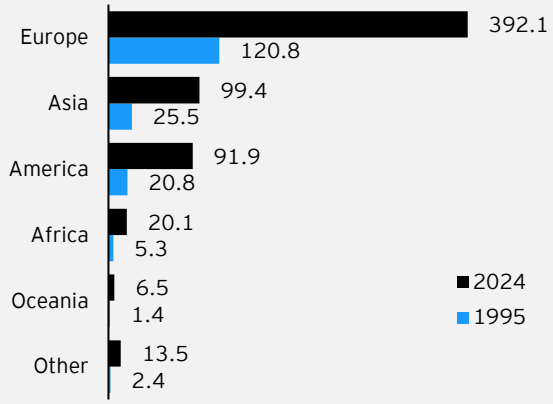
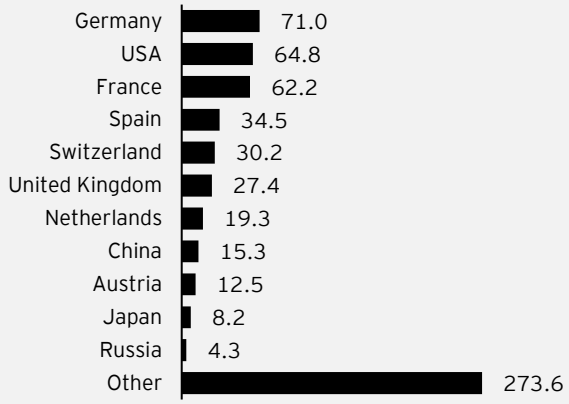


Figure 64: Exports of manufactured goods by destination country, Italy – 2024, €, billion



Source: EY elaborations on UN Comtrade data.

Italy's exposure to the United States is significant yet remains lower compared to its exposure to other key countries or macro-regions, with notable variations across different sectors. Beyond examining the absolute export values to the U.S., it is also important to consider the relative importance of the U.S. market for each product category. For instance, the United States holds strategic significance for specific goods, accounting for 23% of total exports in beverages and alcoholic products, 19% in pharmaceutical products, and approximately 15% in optical and medical instruments in 2024.

Figure 65: Exports of manufactured goods by destination, Italy – 2024, €, billion

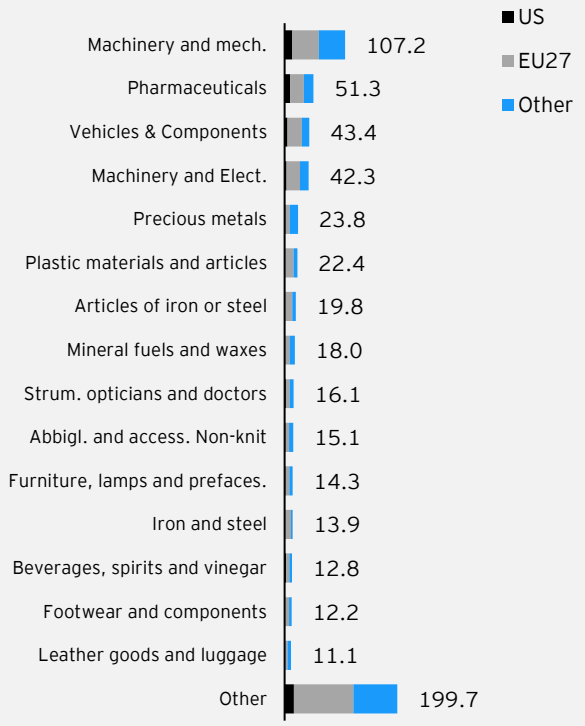
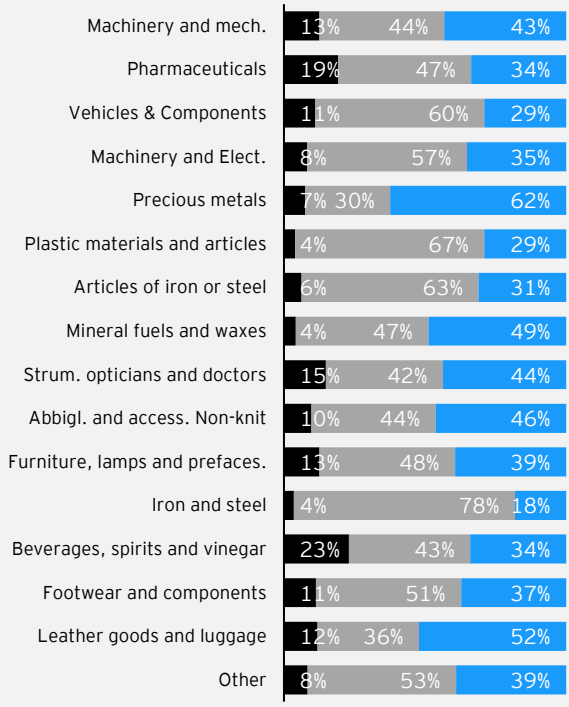


Figure 66: Exports of manufactured goods by destination, Italy – 2024, % by product



Source: EY elaborations on UN Comtrade data.

This heterogeneity also results in varying overall impacts from potential protectionist and trade-distorting measures imposed by the United States, depending on the type of goods and the specific manufacturing sectors involved. Assessing the risks of trade policy solely on direct exposure observed in international trade

data can be misleading. Italy, like other countries, is also indirectly exposed to the US market through the export of intermediate and semi-finished goods to third countries, which then use these inputs to produce goods ultimately exported to the United States. Although challenging to quantify, this indirect exposure constitutes an additional risk factor for Italian exports and trade.

Overall, Italy's significant integration within global value chains represents both a strength and a source of increased vulnerability to shifts in the trade policies of other countries. On the positive side, this integration enhances resilience to potential shocks in domestic demand or traditional trade, given the broad and diversified nature of Italy's international markets. However, strong participation in global value chains also implies heightened exposure to external shocks, which can have ripple effects across various domestic sectors and industries.

The impact of a potential shock depends on several factors, including: (i) the nature of the shock itself; (ii) the country's and firms' positions within global value chains—whether they operate upstream or downstream, as upstream actors tend to amplify demand shocks originating downstream, and vice versa; and (iii) the quality of labour involved, since shocks predominantly affect low-skilled and subordinate suppliers, while firms engaged in "relational GVCs"—characterised by skilled labour and active decision-making roles—tend to be more resilient to such negative impacts.[80]

It is also important to recognise that a significant share of exchanges within global value chains occurs as intra-group transactions, which tend to be less sensitive to price fluctuations of intermediate goods. Consequently, vertical integration can mitigate the negative effects of temporary disruptions in global value chains.[81] Additionally, a high degree of product specialization enables the provision of goods that are difficult to substitute, further reducing the potential adverse impacts arising from specific shocks.

Finally, it is essential to recognise that dependence on strategic inputs entails significant risks. Upstream sectors, which supply inputs accounting for a substantial share of GDP, face systemic vulnerabilities, whereas sectors focused on final outputs do not pose systemic risks.[82] For instance, it is estimated that approximately 15% of Italian companies are exposed to China through the sourcing of critical inputs, which represent around 25% of value added and employment within the manufacturing sector.[83] Addressing these risks requires coordinated action at the European Union level, including initiatives such as raw materials partnerships and multilateral or bilateral agreements.[84]

[80] Acemoglu, D., Akcigit, U., & Kerr, W. (2016). Networks and the macroeconomy: An empirical exploration. *Nber macroeconomics annual , 30* (1), 273-335.; Barrot, J. N., & Sauvagnat, J. (2016). Input specificity and the propagation of idiosyncratic shocks in production networks. *The Quarterly Journal of Economics , 131* (3), 1543-1592.; Borin, A., Mancini, M., & Taglioni, D. (2021). *Measuring exposure to risk in global value chains* (pp. 1-43). Washington, DC: World Bank.; Brancati, E., Brancati, R., & Maresca, A. (2017). Global value chains, innovation and performance: firm-level evidence from the Great Recession. *Journal of Economic Geography , 17* (5), 1039-1073.; Carvalho, V. M., & Tahbaz-Salehi, A. (2019). Production networks: A primer. *Annual Review of Economics , 11* (1), 635-663.

[81] *European Commission (2024). Global trade outlook and the resilience of Global Value Chains.*

[82] *Dew -Becker, I. (2023). Tail risk in production networks. Econometrics, 91(6), 2089-2123.*

[83] *Borin, A., Cariola, G., Gentili, E., Linarello, A., Mancini, M., Padellini, T., & Sette, E. (2023). Inputs in Geopolitical Distress: A Risk Assessment Based on Micro Data Author-Name: Alessandro Borin. Bank of Italy Occasional Paper, (819).*

[84] *Amighini, A., Maurer, A., Garnizova, E., Hagemejer, J., Stoll, P. T., Dietrich, M., & Tentori, D. (2023). Global value chains: Potential synergies between external trade policy and internal economic initiatives to address the strategic dependencies of the EU. European Commission.*

The Italian Economy: GDP and EY Forecasts

In the first quarter of 2025, Italy's GDP grew by 0.3% compared to the previous quarter. This increase was primarily driven by domestic demand, particularly investments, which rose by 1.6%, matching the growth rate recorded in the previous quarter. Private consumption showed modest growth of 0.2%. On the external front, both imports and exports expanded significantly, by 2.6% and 2.8% respectively, with net foreign demand contributing approximately 0.1 percentage points to GDP growth. Conversely, changes in inventories exerted a downward effect, subtracting 0.2 percentage points from quarterly growth.

Looking at the year-on-year trend, GDP increased by 0.7%, mainly supported by private consumption, which grew by 0.6% and contributed 0.3 percentage points to overall growth, and investments, which rose by 1.4%, also contributing 0.3 percentage points. The foreign sector had a notable negative impact, subtracting 0.9 percentage points from growth due to a strong 4.3% increase in imports.

Figure 67: GDP components, Italy – contributions to growth, percentage points

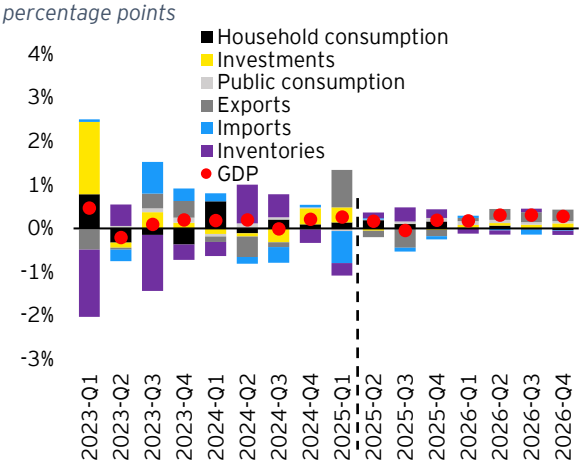
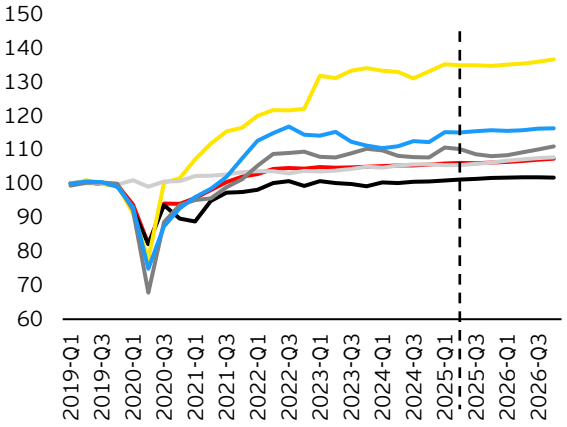


Figure 68: GDP components, Italy – index, quarterly average 2019 = 100



Source: EY elaborations on Eurostat data and EY forecasts. The dotted line represents the forecast horizon. EY forecasts start from the second quarter of 2025. The item "Investments" refers to public and private investments, and includes gross fixed investments, acquisitions less disposals of valuables and depreciation.

Based on the information provided in the preceding sections and the latest available data, it is possible to outline EY's outlook for the Italian economy. Following a quarterly growth of 0.3% in the first quarter, a weaker expansion is expected in the second quarter (0.2%), primarily driven by private consumption (growing by 0.3%, corresponding to a positive contribution of 0.2 percentage points to overall growth). Foreign trade is projected to contribute negatively to growth (-0.1 percentage points), similarly to investment (-0.1 percentage points). The third and fourth quarters are expected to show a trend in private consumption broadly consistent with that of the second quarter. However, foreign trade will exert a more pronounced negative impact on growth, particularly in the third quarter, during which GDP is anticipated to remain essentially stable.

Overall, GDP growth for 2025 is projected at 0.6%, supported by both consumption and investment, while foreign demand is expected to make a negative contribution (-0.7 percentage points). In contrast, 2026 is anticipated to experience slightly more dynamic growth (0.8%), primarily driven by household consumption (contributing 0.3 percentage points to growth) and a potential recovery in production.

Table 1: Forecasts on the Italian economy

	2021	2022	2023	2024	2025	2026
GDP, % change	8.8%	5.0%	0.8%	0.5%	0.6%	0.8%
Household consumption, % change	5.8%	5.3%	0.4%	0.4%	0.9%	0.5%
Investments, % change	21.5%	7.7%	9.2%	0.0%	1.8%	0.6%
Exports, % change	14.2%	10.6%	0.5%	-0.3%	1.0%	0.3%
Imports, % change	16.0%	13.6%	-1.3%	-1.5%	3.4%	0.5%
Unemployment rate	9.5%	8.1%	7.7%	6.6%	6.5%	6.8%
Consumer price index, % change	1.9%	8.2%	5.6%	1.0%	1.7%	1.9%
Deficit, % of GDP	-8.9%	-8.1%	-7.2%	-3.5%	-3.4%	-3.1%
Public debt, % of GDP	146.1%	138.4%	134.6%	135.5%	135.4%	133.9%

Source: forecasts from the EY Italy Macroeconometric Model, "HEY-MoM". The grey area represents the forecast horizon. The changes in GDP and its components are calculated on values in real terms. The item "Investments" refers to public and private investments, and includes gross fixed investments, acquisitions less disposals of valuables and depreciation. Historical growth rates may not coincide with ISTAT communications; this is due to statistical effects of aggregation of quarterly data (used in the HEY-MoM model) which led to possible discrepancies with annual values.

With regard to investment trends, it is important to highlight that growth in 2025 will be largely supported by public investment, which is expected to increase by 7.7%, while private investment will remain considerably less dynamic, growing by only 0.6%. This divergence is expected to persist in 2026, when private investment is projected to decline slightly (-0.2%), whereas public investment will continue to sustain growth, with an increase of 4.4%.

A more detailed breakdown of investment components reveals that the weakness in private investment is primarily linked to a contraction in residential construction (-2.8% in 2025 and -2.9% in 2026), largely due to the phasing out of government incentives (e.g., the "Superbonus 110%").

Other investment categories, by contrast, are expected to expand. In the aggregate of public and private investment, non-residential construction is forecast to grow by 5.5% in 2025 and 0.2% in 2026; investment in machinery is expected to increase by 2.8% and 3.3%, respectively; and investment in intangible assets is set to continue its upward trajectory, with growth rates of 3.3% and 2.1%.

As for the labour market, the unemployment rate is projected at 6.5% in 2025, followed by a modest increase to 6.8% in 2026. Inflation is expected to remain close to the 2% threshold in both 2025 and 2026 (at 1.7% and 1.9%, respectively), in line with the European Central Bank's price stability target.

The public deficit is forecast at 3.4% of GDP in 2025 and 3.1% in 2026, while the public debt-to-GDP ratio is anticipated to decline, reaching approximately 133.9% in 2026. These projections remain subject to a high degree of uncertainty and are therefore exposed to significant risks, both to the downside and the upside, mainly stemming from the broader global macroeconomic context.

Assumptions to forecasts

Forecasts and analyses are based on data available as of June 13, 2025.

The projections outlined above rest on a set of assumptions that define the reference scenario. Specifically, the following hypotheses have been considered:

- **Foreign demand for Italian goods:** overall growth of approximately 1.8% is expected in 2025, followed by more dynamic growth exceeding 2% in 2026;
- **Natural gas prices:** the price of natural gas (based on the Dutch Title Transfer Facility) is assumed to average around $12.4/mmbtu in 2025 and $11.0/mmbtu in 2026;
- **Oil prices:** the average price of oil is expected to be approximately $67.8 per barrel in 2025, declining to around $62.5 per barrel by the fourth quarter of 2025, and further decreasing to an average of $60.4 per barrel in 2026;
- **Exchange rate:** the euro/dollar exchange rate is assumed to remain stable at 1.10;
- **Public spending:** assumptions are based on the UPB Report on budget policy of June 2025, alongside the latest public sector data from ISTAT national accounts;[85]
- **Monetary policy and interest rates:** A reduction in interest rates of 25 basis points is assumed by the end of 2025, in line with expectations reflected in the Bloomberg Survey of Economists conducted between May 23 and 28. Interest rates are expected to remain stable throughout 2026. Additionally, the long-term interest rate (10-year) is projected to display a progressively widening spread relative to the short-term rate.

Given the prevailing high level of uncertainty in the global economic environment, the following downside and upside risks are outlined to provide a more comprehensive understanding of potential future developments.

Upside risks

- Geopolitical tensions: A potential reduction in geopolitical tensions—particularly those linked to the ongoing Russian-Ukrainian and Israeli-Palestinian conflicts, as well as recent developments involving Israel and Iran—could materialise in the short to medium term. Such a de-escalation would likely ease instability in the global macroeconomic environment, with positive effects on energy prices, especially oil, and other commodity markets;
- Trade: A gradual easing of trade tensions may occur over time, facilitating a recovery in trade flows. This would provide support to the Italian economy as well as to its key trading partners;
- Labour market: reduced wage-driven inflationary pressures could lower the risk of sustained inflationary persistence;
- Monetary policy: an accelerated easing of monetary policy by the European Central Bank could alleviate pressures on domestic demand;
- Readjustment of supply chains: a more rapid realignment of value chains at both the European and global levels could reduce supply pressures, enhancing supply security and facilitating smoother global trade;

[85] UPB Report on Fiscal Policy – June 2025. For more information, https://www.upbilancio.it/rapporto-dellupb-sulla-politica-di-bilancio-giugno-2025/ .

- Acceleration of foreign demand: stronger economic growth among key trading partners—including China, Germany, and the United States—would lead to an increased contribution of foreign trade to Italy's economic growth;
- New European legislature: policy decisions by the new European Parliament and Commission could foster growth across EU member states through targeted initiatives, such as support for the defense sector and the implementation of the proposed Rearm EU plan.

Downside risks

- Geopolitical tensions: the Russia-Ukraine conflict may remain unresolved in the short to medium term, sustaining geopolitical instability. This situation could be further exacerbated by a deterioration of the Israeli-Palestinian conflict and heightened tensions between Israel and Iran.[86] Should other countries become involved, the humanitarian and economic consequences could intensify significantly, potentially driving up the prices of energy commodities (primarily oil) and other raw materials;
- Trade: Trade conflicts could escalate, potentially leading to the implementation of more severe trade-distorting measures;
- Monetary policy: In response to persistent or renewed inflationary pressures, the ECB and other major central banks may adopt a tighter monetary policy stance. This could increase the risk of prolonged low growth, as higher interest rates may dampen consumption and investment;
- Stress in the financial system: Elevated interest rates could increase stress on financial institutions, potentially impacting savers and leading to tighter credit conditions in both the United States and the Eurozone;
- High public debt: The post-pandemic rise in public debt, coupled with elevated interest rates, presents increased challenges to debt sustainability in Eurozone economies—particularly in highly indebted countries like Italy. This situation may ultimately heighten the risk of financial market stress;
- PNRR: Incomplete or partial implementation of the National Recovery and Resilience Plan (PNRR) could slow the growth of investments, thereby dampening overall economic growth. Such setbacks may also negatively impact potential GDP, affecting Italy's medium- to long-term growth prospects;
- Monetary policy transmission channels: Structural factors—such as a high proportion of households with fixed-rate debt and the predominance of the service sector in the economy—can weaken the effectiveness of monetary policy transmission, potentially delaying its impact;[87]
- Greater distress in the real estate sector: Prolonged high interest rates could increase pressure on the real estate market, potentially discouraging home and property purchases;
- Lower growth in China, Germany, and the United States: A slowdown in economic growth in these key trading partners could lead to a reduction in foreign demand for Italian goods, negatively impacting Italy's export-driven sectors;
- New European legislature: The new European legislature could face challenges in advancing its political agenda, which may result in slower or less effective policy implementation, potentially dampening economic growth across EU member states.

[86]For an analysis of the potential implications for businesses of a worsening conflict between Israel and Iran, see EY (2024) How potential Middle East conflict scenarios could affect businesses, https://www.ey.com/en_us/insights/strategy/how-potential-middle-east-conflict-scenarios-could-affect-businesses .
[87]ECB, the risks of a stubborn inflation, June 2023, https://www.ecb.europa.eu/press/key/date/2023/html/ecb.sp230619_1~2c0bdf2422.en.html .

Technical Appendix

HEY-MOM: Hybrid EY MOdel for the Macroeconomy[88]

The construction of a new macro-econometric model required the optimisation of an inevitable trade-off between building a model that emphasises the information of the data (such as the ARIMA and VAR models, which do not make any use of economic theory) or a model that pays attention only to the foundations on which its relationships are based (in the extreme case, the calibrated RBC-DSGE models that do not pay attention to the data of their variables). [89]This trade-off has been underlined several times in the literature, see for example the reflections in Granger (1999) and Pagan (2003).

In building HEY-MOM, we tried not to neglect either of the two ingredients mentioned above (economic theory and data), in an attempt to produce a hybrid model with a careful balance in the specification of relationships (a) based on micro-founded economic behaviors and at the same time (b) careful in the application of rigorous techniques for evaluating statistical information. An example of a hybrid model is MARTIN, the model currently in use at the Australian Central Bank (see Cusbert and Kendall, 2018).

In a nutshell, the role of HEY-MOM is to unify the analytical structure of macroeconomics in EY. To do this, the model refers to the main aggregates of the Italian economy, based on empirical data, of a non-monetary nature, with explicit long-term relationships between the variables it studies, and mainly oriented to the definition of short-term forecasts (over a two-year horizon).

The economic foundations

Rigidity in the movement of prices and wages implies a rigidity in the speed with which macroeconomic systems adjust to unexpected shocks. Thus, on the one hand in the model, market demand drives short-run fluctuations, as outlined by Keynesian theories, while in the long run, supply determinants drive the state of the economy.

Long-run output (the economy's potential) depends on the combined effect of trends in total factor productivity, labour supply and hours, and capital stock. These factors are combined by a "Cobb-Douglas" technology with constant returns to scale. The demand for inputs is that which minimises cost given a planned level of output in the context of an oligopolistic competitive economy, where firms are free to set prices based on a markup over labour costs and, at those prices, are collectively willing to meet any level of market demand. Wages are set on a "Phillips curve" driven by the inertia of the inflation rate, labour productivity, and the gap between the actual and natural unemployment rates (defined by the long-run state of the labour market). Actual output is composed of the following items of domestic and foreign demand: private (household) and public consumption; private and public investments by type of asset (residential and non-residential buildings, machinery and equipment, and research and development expenditure); imports and exports.

In each period, the gap between actual and potential output feeds back into prices (through changes in margins) which, in turn, interact with the demand components. In this way, equilibrium between supply and demand is achieved.

[88]The model was created in collaboration with the Department of Economics of the University of Bologna.
[89]"ARIMA" stands for "Autoregressive integrated moving average", "VAR" for "Vector autoregression", "RBC-DSGE" for "Real Business Cycle - Dynamic. Stochastic General Equilibrium".

Data evaluation techniques

The speed with which the economic dynamics outlined above evolve over time is estimated with econometric methods based on the actual time series of the variables of interest in the model.

To this end, the model uses a combination of the approaches of the London School of Economics and Fair's (2004) revision of the Yale Cowles Commission approach. The synthesis realised in HEY-MOM uses cointegration methods (Engle and Granger, 1987, and Johansen, 1995) to estimate long-run relationships between non-stationary variables (Dickey and Fuller, 1979), interpretable in the light of economic theory and identified by state relations whose parameters are estimated on the basis of error correction models (Hendry et al., 1984, and Pesaran et al., 2001). In the absence of exogeneity of some explanatory variables of the model, the relationships are first inspected following the instrumental variables estimation approach, and then definitively estimated in three stages (Hsiao, 1997).

The overall result is a model composed of 74 equations, of which 29 stochastic and 45 accounting identities. The forecasts and analyses carried out are conditional on the delineation of scenarios for 65 exogenous variables classifiable as: fiscal and monetary policy instruments, foreign bloc, and cyclical indicators.

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