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EY Italian Macroeconomic Bulletin

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Index

Executive summary

- The global economy is expected to growth by 3.0% in 2025 and 3.1% in 2026. Emerging markets are driving momentum, while advanced economies continue to expand at a slower pace. Global inflation is declining but remains above pre-pandemic levels.
- Despite some signs of improvement, uncertainty remains elevated. Commodity prices are still above pre-pandemic levels, although they generally follow a downward trajectory. Global trade is affected by the slowdown in advanced economies, while emerging markets are experiencing a more positive trend.
- In the Eurozone, following a 0.9% growth in 2024, a slight acceleration is expected in 2025 (1.0%), followed by more dynamic growth in 2026 (1.2%). The industrial sector continues to face severe challenges, although recent PMI data shows improvement. The services sector depicts a more heterogeneous picture.
- At its September meeting, the ECB maintained its monetary policy rates unchanged (deposit rate at 2.0%), reflecting inflation forecasts that point to price stability (around 2%). Downside risks persist, stemming from geopolitical tensions, industrial sector weaknesses, and elevated public debt levels compared to pre-pandemic benchmarks.
- In July, Italian industry recorded its first year-on-year growth after 29 consecutive months of decline. While this marks a positive development, industrial production remains significantly below 2021 levels, with notable disparities across sectors. In the services sector, revenue growth is largely price-driven, with volume indicators showing limited improvement.
- Inflation remains broadly stable (around 1.6%), supported by persistent core inflation. The labor market is solid, although real wages per hour worked remain below their 2021 levels.
- The labor market is expected to remain particularly robust, with the unemployment rate falling to 6.4% in 2025, followed by a slight increase to 6.8% in 2026. Employment growth is coming mainly from the older age groups, particularly the 55+ who gained around 5 percentage points in the total share of employees between 2018 and 2024. Over the last ten years, with the exception of 2020, there has been a significant decrease in the number of unemployed (-50%) and inactive (-15%) people in the 20-64 age group.
- GDP components show mixed dynamics: private consumption stagnated in Q2 2025, while investment maintained a robust pace (+1.0% quarter-on-quarter). Exports, however, contracted sharply (−1.7%) following a 2.1% increase in Q1.
- EY forecasts a real GDP growth of 0.5% for Italy in 2025 and 0.7% in 2026. Inflation is projected to reach 1.9% in both years. These forecasts are subject to considerable uncertainty, given the conflicting signals occasionally emerging from current data.

Figure 1: Real GDP, Italy – % change

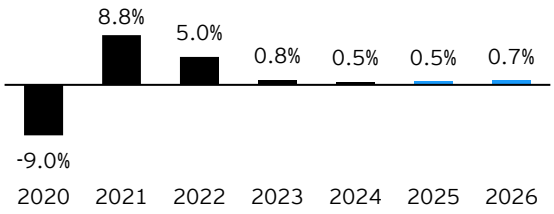
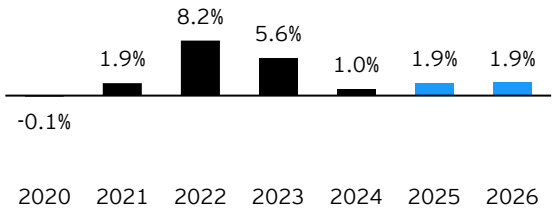


Figure 2: Consumer prices, Italy – % change



The global scenario

The world economy

The global economy continues to be marked by significant uncertainty. Following the downward revisions to global growth published by the International Monetary Fund (IMF) in its April 2025 edition of the World Economic Outlook,[1] the July 2025 update revised growth forecasts upward for 2025 and 2026 across major global economies—underscoring the persistent complexity of the current macroeconomic environment.[2]

Specifically, global GDP is projected to grow by 3.0% in 2025 and 3.1% in 2026, representing upward revisions of 0.2 and 0.1 percentage points respectively compared to the April 2025 estimates.

This improvement reflects more favorable growth prospects in both advanced economies and, more notably, in emerging markets and developing countries. For advanced economies, growth is expected to reach 1.5% in 2025 and 1.6% in 2026 (a revision of +0.1 percentage points in both years). For emerging and developing economies, the revisions are more substantial, with growth forecast at 4.1% and 4.0% respectively (+0.4 and +0.1 percentage points), largely driven by an acceleration in the Chinese economy.

Among advanced economies, the United States is expected to grow by 1.9% in 2025 and 2.0% in 2026, with upward revisions of 0.1 and 0.3 percentage points respectively. This suggests that the impact of economic uncertainty may be less severe for the U.S. economy by 2026. Conversely, the Eurozone is projected to experience more modest growth of 1.0% and 1.2%, with a revision of +0.2 percentage points in 2025 and no change for 2026.

Figure 1: Real GDP – % change

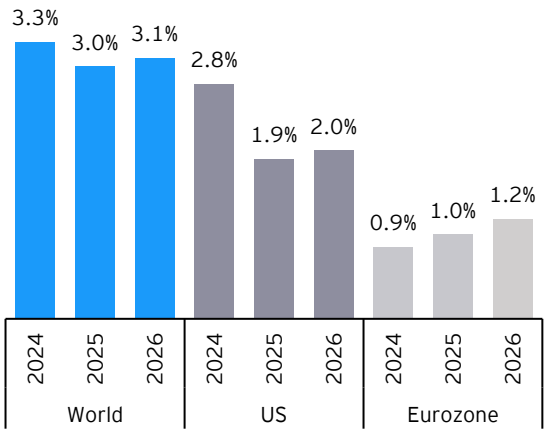
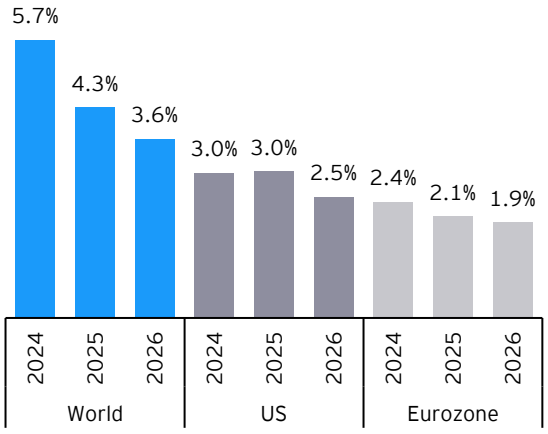


Figure 4: Consumer prices – % change



Source: EY elaborations based on IMF World Economic Outlook data, July 2025 for GDP; IMF World Economic Outlook, April 2025 for consumer prices.

Despite the modest upward revisions, it remains essential to emphasize the role of uncertainty, trade policy decisions, and other structural factors in shaping the economic trajectory of the countries under review.

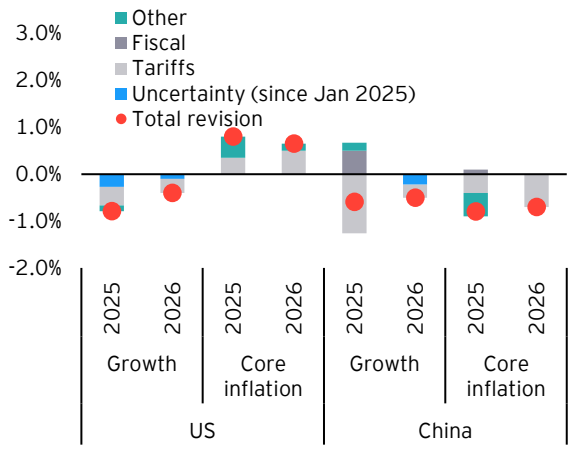
In comparing growth expectations between January and April 2025, the International Monetary Fund (IMF) attributed the downward

[1] International Monetary Fund, World Economic Outlook, April 2025 – A Critical Juncture amid Policy Shifts.

[2] International Monetary Fund, World Economic Outlook Update, July 2025 – Global Economy: Tenuous Resilience amid Persistent Uncertainty.

revisions for countries, such as the United States and China, primarily to the negative impact of new tariffs imposed by the United States. The effects on core inflation—defined as inflation calculated on a basket of goods excluding volatile components such as energy and fresh food—are more nuanced. The IMF estimates that these dynamics will lead to an increase in core inflation in the United States, while in China, a decline in economic activity is expected to result in lower core inflation.[3]

Figure 2: Change in IMF growth and core inflation forecasts between January and April 2025



Source: international Monetary Fund.

Global price growth is gradually returning to levels more consistent with historical trends. Following an inflation rate of 5.7% in 2024, a decline to 4.3% is expected in 2025, and to 3.6% in 2026—representing a reduction of approximately two percentage points compared to 2024. For reference, the average global inflation rate between 2000 and 2019 stood at 3.7%.

Inflation is also projected to decline in both the United States and the Eurozone, although the adjustment in the U.S. is expected to be more gradual. In 2025, inflation in the United States is forecast to be 3.0%, broadly in line with the rate observed in 2024, followed by a decline to 2.5% in 2026.

Inflation expectations partly reflect the potential future impact of trade policy decisions implemented by the new U.S. administration, which could lead to upward pressure on prices. Notably, IMF forecasts from October 2024 had projected inflation rates of 1.9% for 2025 and 2.1% for 2026.[4]

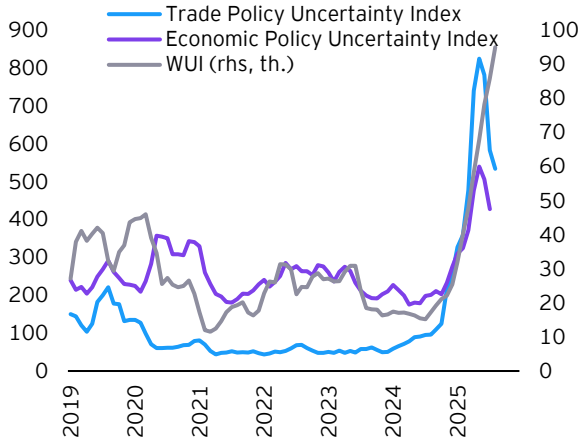
The outlook for the Eurozone differs somewhat, with inflation expected to converge toward the price stability target of 2% over the next two years—broadly in line with the October 2024 projections.

Despite the anticipated moderation in inflation, it is important to recognize that the elevated rates experienced in recent years, combined with inflation that remains partially unanchored in certain countries, continue to pose financial risks—particularly for several advanced and emerging economies. These risks stem from both higher operating costs (e.g., labour and service expenses) and the volatility of costs and revenues linked to monetary policy interest rate movements. In this regard, a recent IMF study found that approximately 3% of banks in advanced economies and 6% of banks in emerging markets currently exhibit exposure to inflation and interest rate risks comparable to that of Silicon Valley Bank in the period immediately preceding its collapse.[5,6]

More broadly, the prevailing climate of uncertainty is well illustrated by several key indicators. Notably, economic policy uncertainty and overall global uncertainty are now close to—or have exceeded—the levels observed during the pandemic in 2020. At the same time, trade-related uncertainty is significantly higher than during the pandemic period, despite some easing in recent months.

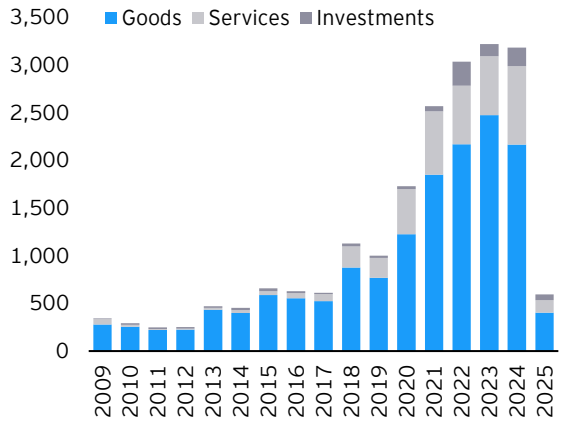
[3] IMF Blog (2025), The Global Economy Enters a New Era. For more information, https://www.imf.org/en/Blogs/Articles/2025/04/22/the-global-economy-enters-a-new-era.
[4] IMF World Economic Outlook, October 2024.
[5] Bergant, K., Kirti, M. D., Hakamada, M. M., & Mano, R. (2025). *Inflation and Bank Profits: Monetary Policy Trade-offs* (No. 2025/001). International Monetary Fund, Staff Discussion Notes No. 2025/001, https://doi.org/10.5089/9798400294723.006.
[6] IMF Blog (2025), Rising Rates May Trigger Financial Instability, Complicating Fight Against Inflation. For more information, https://www.imf.org/en/Blogs/Articles/2025/02/13/rising-rates-may-trigger-financial-instability-complicating-fight-against-inflation.

Figure 3: Uncertainty indices, World - quarterly averages



Source: EY elaborations on ISTAT, Caldara et al. (2019),[7] Economic Policy Uncertainty database. WUI: World Uncertainty Index. Latest data available: August 2025.

Figure 4: Number of restrictive measures, World



Source: IMF World Economic Outlook, april 2025.

Trade-related uncertainty is also driven by the growing number of protectionist measures implemented in recent years. In the first quarter of 2025 alone, the number of newly announced trade-distorting measures increased by 16% compared to December 2024, with a marked intensification of actions beginning on April 2. From a historical perspective, the volume of such measures in 2024 was approximately 200% higher than in 2019, and nearly 400% higher than in 2015.

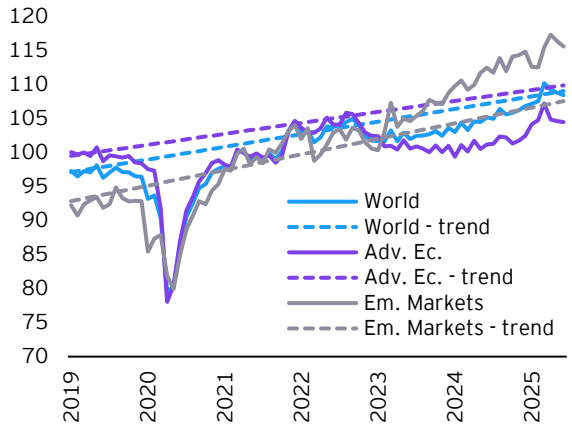
While these measures have primarily targeted goods trade, an increasing number of restrictive actions have been directed toward services and, more recently, investment flows.

The impact of new trade policies and potential retaliatory measures by affected countries could lead to a further slowdown in global goods trade. An analysis of recent trade performance, compared with trends observed between 2010 and 2019 (the pre-pandemic period), reveals that over the past two years, trade volumes have consistently remained below their linear trend—despite a partial recovery in early 2025.

When disaggregating this data by the two main global economic blocs—advanced economies and emerging (and developing) economies—it becomes evident that the recent recovery has been largely driven by trade growth in emerging markets. In contrast, advanced economies continue to exhibit weaker dynamics relative to the trend established during the 2010-2019 period.

[7] 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.

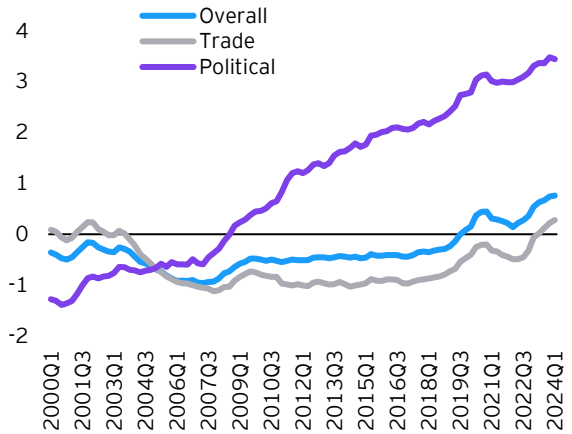
Figure 8: Trade in goods by volume and linear trend (2010-2019), World – index, 2021=100



Source: EY elaborations based on data from CPB Netherlands Bureau for Economic Policy Analysis. Refers to trade in goods. Latest data available: June 2025.

The ongoing fragmentation of global trade is accompanied by a broader geopolitical fragmentation—a phenomenon that has been unfolding since the aftermath of the 2007-2008 financial crisis.

Figure 9: Geopolitical fragmentation index

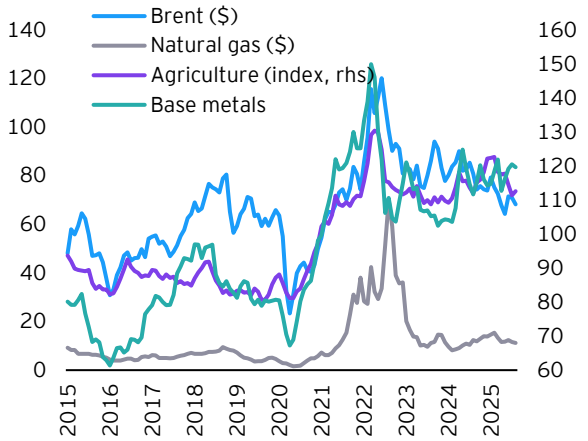


Source: World Bank. The geopolitical fragmentation index extracts the common factor between various indicators related to trade, finance, people mobility, geopolitical instability and misalignment, as in Fernández-Villaverde, J., T. Mineyama, D. Song. 2025. "Are We Fragmented Yet? Measuring Geopolitical Fragmentation and Its Causal Effects." NBER Working Paper 32638, National Bureau of Economic Research, Cambridge, MA. A higher value implies greater fragmentation. Latest observation: 2024-Q1.

Overall fragmentation and the uncertainty it generates represent negative forces for the global economy. These dynamics may lead to a decline in aggregate demand due to reduced confidence and potentially lower consumer income in the medium term. Uncertainty also poses risks of slower investment and global trade,[8,9] as well as potential effects on commodity price trends.

In this context, the average Brent crude oil price in August 2025 was 68.2 $/barrel,[10] down from 71.0$/barrel in July. After hitting a low of 64.2$/barrel in May 2025, oil prices rose in June and July, driven by heightened tensions between Iran and the United States, broader Middle East instability, and a general climate of uncertainty.

Figure 5: Energy Commodity Prices ($) and Agricultural & Base Metal Price Index (2010=100)



Source: EY elaborations based on World Bank data. Brent and natural gas prices are expressed in USD per barrel and USD per mmbtu, respectively. The natural gas price refers to the Title Transfer Facility (TTF) benchmark. The agricultural price index includes a range of global agricultural commodities and derivatives (e.g., wheat). Latest data available: August 2025.

Recent tensions between Iran and the United States have brought renewed attention to energy commodity prices—particularly oil—and more broadly, to the vulnerability of global supply chains.

For example, the Strait of Hormuz, located in Iranian territory, is a critical chokepoint through which approximately 20% of global oil volumes transit. Any disruption, even partial, of these

[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.

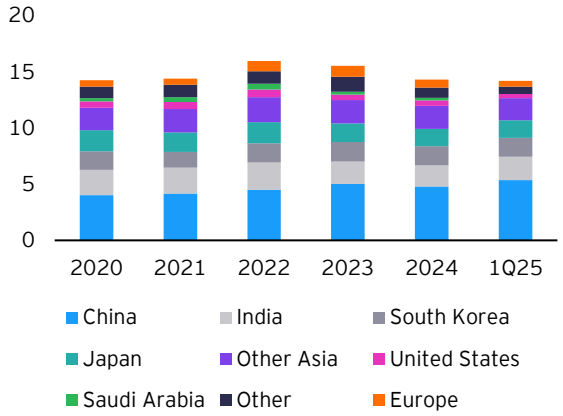
[9] Caldara, Dario, Matteo Iacoviello, Patrick Molligo, Andrea Prestipino, and Andrea Raffo. 2020. "The Economic Effects of Trade Policy Uncertainty." Journal of Monetary Economics 109: 38-59.

[10] Dollars per barrel of oil. One barrel is equivalent to approximately 159 litres.

flows due to escalating tensions would likely result in a significant increase in crude oil prices.[11]

In addition to oil, the Strait of Hormuz is also a key transit route for natural gas, accounting for roughly 20% of global LNG flows.[12]

Figure 6: Volume of Crude Oil Transported Through the Strait of Hormuz by Destination Country (Million b/d)



Source: EY elaborations based on U.S. Energy Information Administration (EIA) data.

As for natural gas traded on the European market, prices stabilized in August at around 11.1 USD/mmbtu[13], consistent with levels observed in previous months, despite a temporary increase in June (12.4 USD/mmbtu). Overall, prices continue to follow a downward trajectory after rising between late 2024 and early 2025.

Agricultural commodity prices, after accelerating in late 2024 and early 2025, are now trending downward, showing a decline compared to earlier in the year.

Base metal prices, on the other hand, have increased by approximately 7% year-on-year. This rise reflects higher prices for key components of the index—such as aluminum, copper, lead, tin, and zinc—with the exception of nickel. These price dynamics are particularly relevant given the role of metals in shaping core inflation (i.e., inflation excluding volatile components such as energy and unprocessed food.

Price shocks in metals can have significant and lasting effects, especially in economies where production systems rely heavily on metals as intermediate inputs. This distinguishes them from supply shocks in energy commodities like oil, which primarily affect headline inflation.

The global economy's shift toward production models with higher metal intensity—driven largely by the energy transition—may cause metal price shocks to increasingly influence core inflation. As a result, such shocks may become less immediately visible but more persistent over time. Furthermore, reduced reliance on fossil fuels and increased use of metals in energy systems could make the global economy less dependent on oil and more dependent on metals.[14]

Recent geopolitical tensions may also contribute to greater volatility in metal prices, particularly in light of the trade-distorting and restrictive measures introduced since the onset of the war in Ukraine.[15] Given that metal production is often geographically concentrated and not easily substitutable, trade tensions typically lead to sharp price fluctuations, with increasingly negative repercussions for the global economy.[16]

In summary, the geopolitical and economic landscape remains complex, characterized by high uncertainty regarding the future configuration of global systems. Growth forecasts are affected by potential trade distortions, while commodity prices—despite some moderation—remain elevated compared to pre-pandemic levels.

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

The international macroeconomic landscape continues to exhibit divergent short-term dynamics across key advanced economies.

[11] US EIA (2025). Amid regional conflict, the Strait of Hormuz remains critical oil chokepoint, https://www.eia.gov/todayinenergy/detail.php?id=65504.
[12] US EIA (2025). About one-fifth of global liquefied natural gas trade flows through the Strait of Hormuz, https://www.eia.gov/todayinenergy/detail.php?id=65584.
[13] Dollars per million British thermal units, which is a measure of the amount of gas.

[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] Gopinath, Gita, Pierre-Olivier Gourinchas, Andrea Presbitero, and Petia B Topalova. 2024. "Changing Global Linkages: A New Cold War?" IMF Working Paper 2024/076.
[16] 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.

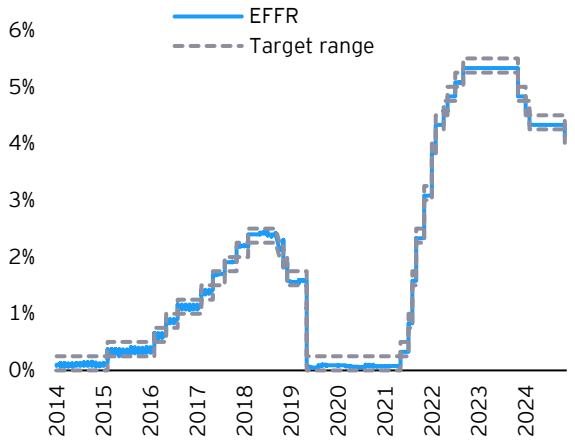
United States

In the second quarter of 2025, U.S. gross domestic product (GDP) expanded by 0.8% on a quarterly basis, equivalent to an annualized growth rate[17] of 3.3%. This marks a rebound from the slight contraction of 0.1% recorded in the first quarter.

The acceleration in economic activity was primarily supported by a substantial positive contribution from net exports (+1.4 percentage points) and a moderate increase in private consumption (+0.4% q/q, contributing +0.3 percentage points). The improvement in net exports was largely attributable to a sharp decline in imports (−8.5%), while exports registered a marginal contraction (−0.3%).

Conversely, private investment declined by 3.6% compared to the previous quarter, exerting a negative impact on overall growth by −0.7 percentage points.[18]

Figure 7: Federal Reserve Policy Rates, United States



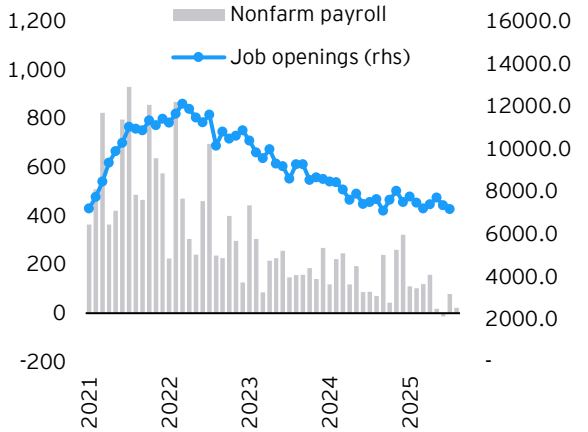
Source: EY elaborations based on data from the Federal Reserve Bank of New York. EFFR: Effective Federal Funds Rate, calculated as the volume-weighted median of overnight reported transactions. For more information: New York Fed Reference Rates, https://www.newyorkfed.org/markets/reference-rates/effr.

On the inflation front, price pressures have shown a modest upward trend in recent months. In July 2025, headline inflation stood at 2.7%, unchanged from June and above the average of 2.4% observed between March and May. Similar patterns are evident in other price indicators, including the Personal Consumption Expenditures (PCE) Price Index.[19]

Despite inflation remaining above the Federal Reserve's 2% target, the central bank opted, at its most recent policy meeting, to reduce the federal funds rate range to 4.00%-4.25%. This decision reflects growing concerns over an increasingly uncertain economic outlook and signs of moderation in labour market conditions.

It is important to recall that the Federal Reserve operates under a dual mandate: to foster maximum employment and maintain price stability.

Figure 8: Figure 13: Change in Nonfarm Payrolls and Job Openings, USA



Source: EY elaborations based on data from the Bureau of Labor Statistics (BLS). Nonfarm payrolls refer to U.S. workers excluding business owners, household employees, unpaid volunteers, agricultural workers, and self-employed individuals not incorporated. This measure accounts for approximately 80% of the labor force contributing to GDP. For more information: https://fred.stlouisfed.org/series/PAYEMS.

Recent labor market indicators suggest a deceleration in employment dynamics. In August, nonfarm payrolls increased by only 22,000 jobs, a notable decline from the 79,000 jobs added in July.[20] Job openings have remained broadly stable since mid-2024, following a peak in 2022, with monthly figures consistently exceeding 7 million. Meanwhile, the unemployment rate has remained relatively steady, hovering slightly

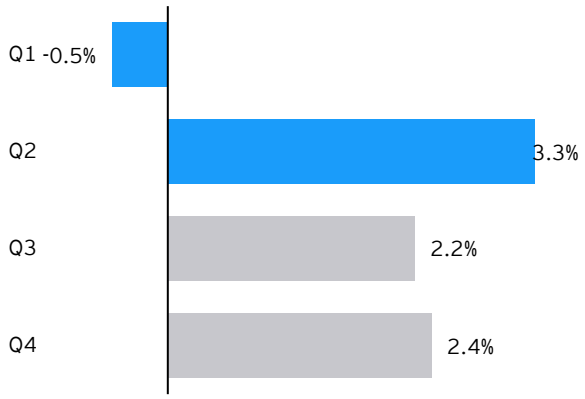
[17] For more information, https://www.bea.gov/help/faq/463.
[18] Gross Domestic Product, 2nd Quarter 2025 (Second Estimate) and Corporate Profits (Preliminary), https://www.bea.gov/news/2025/gross-domestic-product-2nd-quarter-2025-second-estimate-and-corporate-profits-preliminary.
[19] For more information, https://www.bea.gov/data/personal-consumption-expenditures-price-index.
[20] Federal Reserve issues FOMC statement, 17 September 2025, https://www.federalreserve.gov/newsevents/pressreleases/monetary20250917a.htm.

above 4%, indicating a gradual softening in labor market momentum.[21]

Consumer spending in the United States continued to expand in July 2025, rising by 0.3% following a more subdued increase of 0.1% in June.[22] This acceleration was primarily driven by a rebound in goods consumption, which rose by 0.9% in July after contracting by 0.1% in June and 0.7% in May. In contrast, spending on services increased by a modest 0.1%, in line with the trend observed in previous months.

Industrial and manufacturing activity remains uncertain. In July 2025, industrial production declined slightly (−0.1%) after rising by 0.4% in June and 0.1% in May. Manufacturing output was flat in July, following increases of 0.3% and 0.2% in June and May, respectively. On a year-over-year basis, both industrial and manufacturing production posted encouraging growth of 1.4%. [23]

Figure 9: U.S. GDP 2025 – QoQ Annualized % Chang

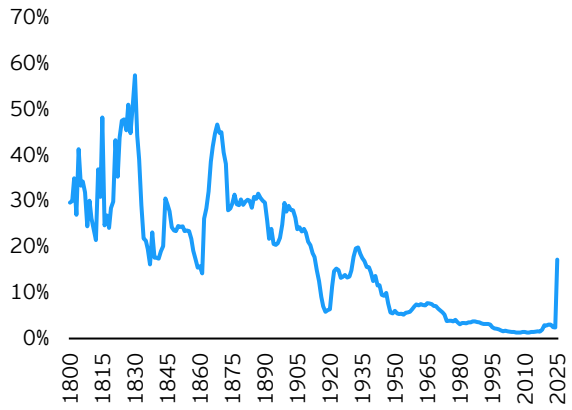


Source: EY elaborations based on data from the Federal Reserve Bank of New York and the U.S. Bureau of Economic Analysis (BEA). Gray bars represent available forecasts for upcoming quarters (New York Fed Staff Nowcast). Growth rates are annualized. Last update: August 20, 2025

Looking ahead, the Federal Reserve Bank of New York's August 2025 projections suggest that GDP growth over the next four quarters could range from −0.56% to +3.04%, with a median estimate of 1.34%. These figures reflect a dynamic but uncertain economic outlook. Specifically, short-term forecasts point to annualized growth rates of 2.2% and 2.4% for the third and fourth quarters of 2025, respectively.[24]

When assessing the outlook for the U.S. economy, it is essential to consider recent developments in trade policy, which have introduced additional uncertainty both domestically and globally. The effective tariff rate currently applied by the United States to imports from the rest of the world stands at approximately 17%—a level not observed since the early 20th century. This elevated rate poses potential risks to both global growth and inflation.

Figure 10: Average effective tariff rate, USA



Source: EY elaborations based on World Trade Organisation and International Monetary Fund data. Last update: August 2025.

In this context, the World Bank has conducted a scenario analysis to assess the potential macroeconomic implications of U.S. trade policy. Two scenarios were considered.[25]

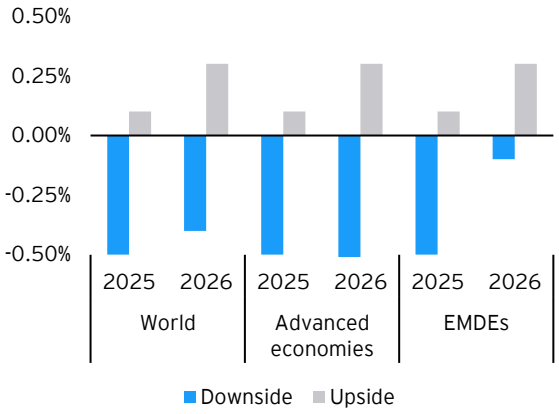
This assumes a weighted average increase in tariffs of approximately 10 percentage points relative to the baseline scenario projected in May 2025, triggering retaliatory measures from trading partners. The escalation in trade tensions is expected to heighten uncertainty and increase financial market volatility. Under this scenario, global GDP growth would be reduced by 0.5 percentage points in 2025 and 0.4 percentage points in 2026. The impact would be broadly similar across advanced and developing economies, driven by weaker global demand and

[21] Bureau of Labor Statistics, Employment Situation News Release. For more information, https://www.bls.gov/news.release/empsit.htm.
[22] Personal Income and Outlays, July 2025. Per maggiori informazioni, https://www.bea.gov/news/2025/personal-income-and-outlays-july-2025.
[23] Industrial Production and Capacity Utilization, July 2025. For more information, https://www.federalreserve.gov/releases/g17/current/default.htm.
[24] For more information, https://www.newyorkfed.org/research/policy/nowcast#/overview.
[25] World Bank, Global Economic Perspective, June 2025.

declining energy prices. These factors are projected to lower global inflation by 0.4 percentage points in 2025. However, inflationary pressures stemming from higher tariffs are expected to materialize fully in 2026, pushing inflation 0.5 percentage points above the baseline. In such an environment, central banks in both advanced and emerging economies may face constraints in implementing accommodative monetary policies.

In the second scenario (upside), this envisions a reduction in the effective U.S. tariff rate to roughly half of the baseline level, alongside the removal of retaliatory trade measures. Such an outcome could result from successful negotiations between the United States and its key trading partners, leading to bilateral agreements and a general easing of trade tensions. The improved trade environment and enhanced confidence are expected to support global growth, with increases of 0.1 and 0.3 percentage points in 2025 and 2026, respectively, relative to the baseline. The positive impact would be broadly distributed across economies.

Figure 11: Change in global growth under different scenarios – percentage points



Source: World Bank.

United Kingdom

The United Kingdom registered GDP growth of 0.3% in the second quarter of 2025, following a more robust expansion of 0.7% in the first quarter and a modest increase of 0.1% in the final quarter of 2024. The performance in Q1 2025 was shaped by subdued growth in private consumption (+0.1%), strong public sector consumption (+1.2%), a marginal contribution from net exports, and a contraction in gross fixed capital formation (−1.1%).[26]

Recent monthly indicators suggest a slight improvement in economic momentum. In May and June, GDP grew by 0.1% and 0.3%, respectively, while in July, the services sector posted a modest expansion of 0.1%, indicating a return to slower growth.[27]

The construction sector also showed signs of resilience, expanding by 0.2% in July, following growth of 0.3% in June and a contraction of 0.5% in May.[28] In contrast, industrial activity remained volatile: output declined by 0.9% in July, after increasing by 0.7% in June and contracting by 1.3% in May.[29]

On the inflation front, consumer price growth continues to accelerate. In August, headline inflation remained stable at 3.8%, unchanged from July, but up from 3.6% in June and 3.4% in

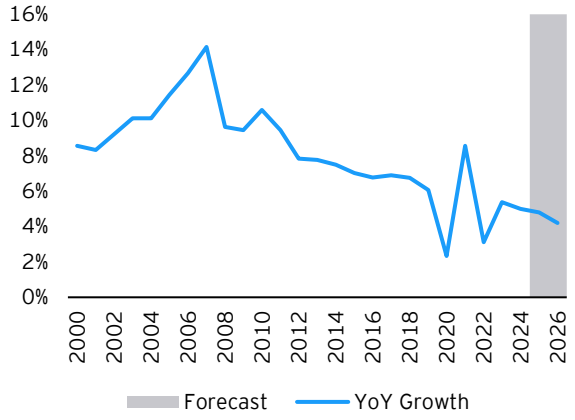
[26] GDP first quarterly estimate, UK: April to June 2025, https://www.ons.gov.uk/economy/grossdomesticproductgdp/bulletins/gdpfirstquarterlyestimateuk/aprilto june2025.
[27] Office for National Statistics, Index of Services, UK: July 2025, https://www.ons.gov.uk/economy/economicoutputandproductivity/output/bulletins/indexofservices/july2025.
[28] Office for National Statistics, Construction output in Great Britain: July 2025, https://www.ons.gov.uk/businessindustryandtrade/constructionindustry/bulletins/constructionoutputingreatbritain/july2025.
[29] Office for National Statistics, Index of Production, UK: July 2025, https://www.ons.gov.uk/economy/economicoutputandproductivity/output/bulletins/indexofproduction/july2025.

May. This upward trajectory is notable, considering that inflation stood at 2.5% at the end of 2024. Core inflation also remains elevated and broadly stable, registering 3.6% in August, 3.8% in July, and 3.7% in June.[30]

China

The Chinese economy continues to exhibit signs of a structural slowdown. This trend extends beyond recent GDP figures or medium-term forecasts—such as the International Monetary Fund's projection of 4.8% growth in 2025 and 4.2% in 2026—and reflects a broader deceleration that has been underway since the post-global financial crisis period.

Figure 12: PIL, GDP, China – % change

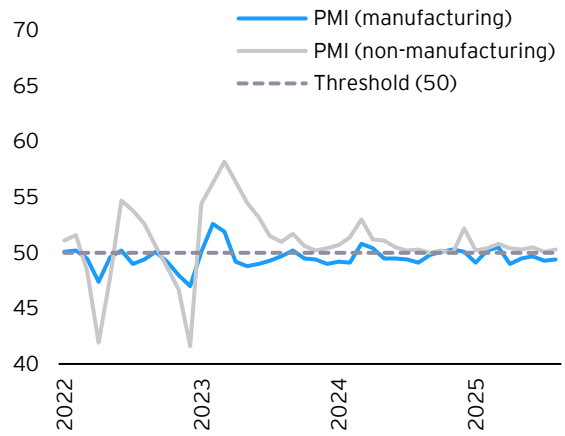


Source: EY elaborations based on International Monetary Fund data and forecasts.

According to the latest data, GDP grew by 5.2% year-on-year in the second quarter of 2025, following growth of 5.4% in the previous two quarters. On a quarter-on-quarter basis, GDP expanded by 1.1% in Q2, after increases of 1.2% in Q1 and 1.6% in Q4 2024.[31]

Industrial activity has begun to moderate. In July, industrial value added rose by 5.7% year-on-year, down from 6.8% in June. Growth in July was supported by strong performance in specific segments, including transport equipment manufacturing (+13.7%) and electrical machinery and equipment (+10.2%).[32]

Figure 13: Purchasing Managers Index (PMI), manufacturing and non-manufacturing activities, China



Source: EY elaborations based on data from the National Bureau of Statistics of China. Latest data available: August 2025.

Business sentiment, as measured by the Purchasing Managers' Index (PMI), remains close to the expansion threshold of 50, indicating subdued optimism across both manufacturing and non-manufacturing sectors.[33]

Investment in Real Estate are declining by 12% between January and July 2025 compared to the same period in 2024. This reflects deep-rooted challenges in the sector.[34]

Broadening the scope of analysis to total investment, cumulative investment growth between January and July 2025 compared to the same period of the previous year stands at 1.6%, with a significantly weaker trend since May 2025 (cumulative growth from January to April was 4.0%, followed by cumulative growth from January to May and January to June of 3.7% and 2.8% respectively).[35]

[30] Office for National Statistics, Consumer price inflation, UK: August 2025, https://www.ons.gov.uk/economy/inflationandpriceindices/bulletins/consumerpriceinflation/august2025.
[31] Preliminary Accounting Results of GDP for the Second Quarter and First Half of 2025, https://www.stats.gov.cn/english/PressRelease/202507/t20250728_1960507.html.
[32] Industrial Production Operation in April 2025, https://www.stats.gov.cn/english/PressRelease/202505/t20250526_1959952.html.
[33] Purchasing Managers' Index for August 2025, https://www.stats.gov.cn/english/PressRelease/202508/t20250807_1960606.html.
[34] Investment in Real Estate Development from January to July 2025, https://www.stats.gov.cn/english/PressRelease/202508/t20250821_1960856.html.
[35] Investment in Fixed Assets from January to July 2025, https://www.stats.gov.cn/english/PressRelease/202508/t20250821_1960855.html.

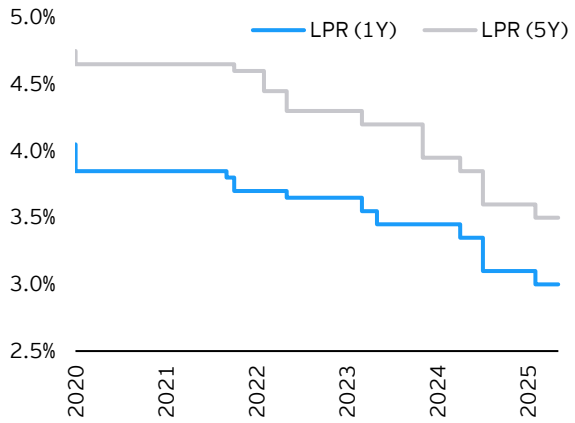
With regard to retail sales, July 2025 saw annual growth (compared to the same month of the previous year) of 3.7%, lower than that recorded in June (4.8%) and May (6.4%). Among the various categories of goods, household appliances and furniture recorded the highest growth rates (28.7% and 20.6% respectively).[36]

From a trade perspective, exports rose by 8.0% year-on-year in July 2025, while imports increased by 4.8%.[37] Despite elevated global trade uncertainty—primarily stemming from U.S. trade policy decisions—recent figures do not yet indicate a significant deterioration in China's external sector.

Overall, the Chinese economy is undergoing a phase of decelerating growth, which authorities are addressing through targeted fiscal and monetary policy measures.

On the monetary front, interest rates remain low relative to previous years—a strategic choice maintained even during periods when major central banks adopted restrictive stances to combat inflation. In August 2025, the one-year and five-year Loan Prime Rates (LPR)—used by commercial banks as benchmarks for lending to prime borrowers—stood at 3.00% and 3.50%, respectively. The Medium-Term Lending Facility (MLF) rate, which governs medium-term borrowing from the central bank, remained unchanged at 2.00%.[38]

Figure 14: 1-year and 5-year Loan Prime Rate (LPR), China



Source: EY elaborations based on People's Bank of China data. Latest data available: August 2025.

From a fiscal policy standpoint, recent research highlights its role in supporting export growth. In particular, targeted subsidies have contributed to increased export volumes and reduced prices, especially in sectors such as metallurgy and furniture manufacturing.[39]

The slowdown in the Chinese economy is expected to continue, however, highlighting the need to reform the growth model. The main challenges to be considered include demographic issues (the ageing population will reduce the labour force),[40] the slowdown in productivity growth (given its transition to advanced economy status),[41] and the declining returns on investment which - fuelled by savings (now at historic highs) - are being directed towards less productive sectors such as real estate.

These dynamics point to the necessity of rebalancing the growth model toward greater reliance on private consumption. Absent reform, potential growth could decline to an average of 3.8% between 2025 and 2030, and further to 2.8% between 2031 and 2040. In contrast, under a reform-oriented scenario, potential growth

[36] Total Retail Sales of Consumer Goods in July 2025, https://www.stats.gov.cn/english/PressRelease/202508/t20250821_1960854.html.
[37] For more information, http://english.customs.gov.cn/statics/report/preliminary.html. Annual export growth stands at 8.1% when exports are expressed in dollars, while import growth stands at -0.2%.
[38] For more information, http://www.pbc.gov.cn/en/3688229/3688335/3883798/index.html.

[39] Rotunno, L., & Ruta, M. (2024). Trade Implications of China's Subsidies. IMF Working Paper WP/24/180, 2024 Aug.
[40] 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.
[41] 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.

could be sustained at approximately 4.7% through 2038.[42]

While the global economy is broadly recovering, significant uncertainty and fragility remain. These stem from ongoing geopolitical tensions, slower growth in several economies relative to pre-pandemic levels, the impact of trade-distorting measures, and commodity prices that remain elevated compared to historical norms.

[42] Muir, D., Novta, N., & Oeking, A. (2024). China's Path to Sustainable and Balanced Growth. IMF Working Paper WP/24/238, 2024 Nov.

The European framework

The Eurozone economy and main indicators

Following GDP growth of 0.6% in the first quarter of 2025, the Eurozone recorded a more modest expansion of 0.1% in the second quarter. This aggregate figure reflects divergent national performances: Spain posted robust growth of 0.7%, France expanded by 0.3%, while Germany and Italy experienced contractions of −0.3% and −0.1%, respectively.

On a year-on-year basis, GDP in the Eurozone grew by 1.5% in the second quarter of 2025, broadly in line with the 1.6% recorded in the first quarter. This result was driven by strong growth in Spain (+2.8%) and more moderate increases in Germany (+0.2%), France (+0.8%), and Italy (+0.4%).

Figure 15: GDP and contributions by country, Eurozone – % change YoY

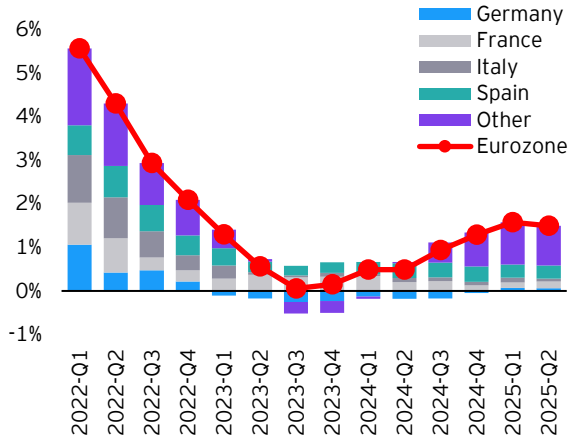
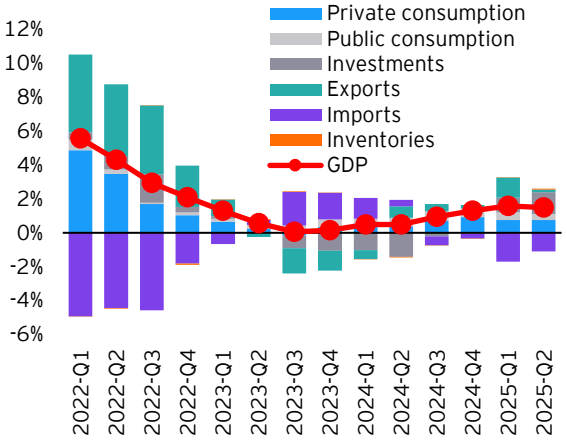


Figure 16: GDP and contributions by component, Eurozone – % change YoY



Source: EY elaborations based on Eurostat data.

From a demand-side perspective, second-quarter growth was primarily supported by private consumption and investment, which contributed +0.7 and +1.3 percentage points, respectively. Public consumption added a further +0.4 percentage points. In contrast, net external demand exerted a negative drag on growth, as imports outpaced exports.

Industrial production in the Eurozone showed a modest year-on-year recovery in June 2025, supported in part by strong performances in March (+3.8%) and May (+2.9%). The industrial production index rose by 0.5% year-on-year in June, marking the fifth consecutive month of positive annual growth. However, from a cyclical perspective, the index contracted by −1.3% in June, following growth of +1.1% in May and a decline of −2.5% in April. Overall, the index remains slightly below its 2021 average, underscoring persistent fragilities in the industrial sector.

Among the largest economies in the monetary union, industrial activity in Germany and Italy continues to underperform, with levels well below 2021 averages and a largely stagnant trend.

Figure 17: Industrial production by main countries, Eurozone – index, 2021=100

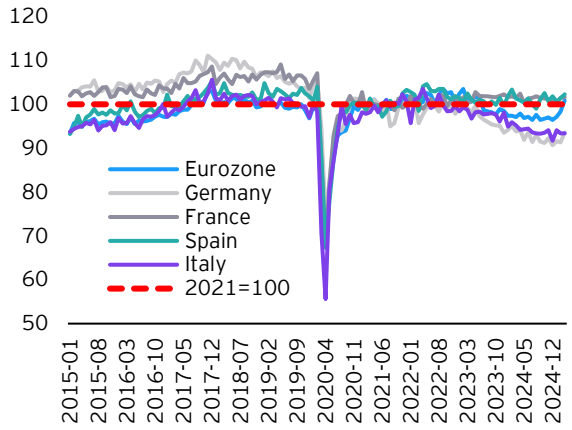
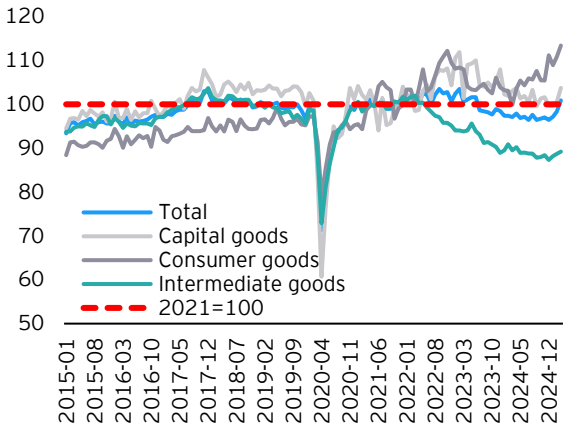


Figure 18: Industrial production by type of goods, Eurozone – index, 2021=100



Source: EY elaborations based on Eurostat data. For industrial production, reference is made to NACE Rev. 2 codes B-D (Mining and quarrying; manufacturing; electricity, gas, steam and air conditioning supply). Latest data available: June 2025.

Among the main industrial goods categories, intermediate goods production remains the most critical area. June marked the 37th consecutive month of year-on-year contraction (with the sole exception of a slight increase in March 2025), with a decline of −1.9%, following a −1.7% drop in May. On a month-on-month basis, intermediate goods production fell by −0.2% in June, after contractions of −1.7% and −0.9% in the previous two months. Conversely, consumer goods production is on a generally upward trajectory, despite recent volatility—including a −4.3% monthly contraction in June, following a +6.8% increase in May.

These figures highlight the complex and fragile state of European industry. In response, Eurozone countries are pursuing industrial policy initiatives aimed at addressing rising geopolitical fragmentation, enhancing productivity, and accelerating the green transition —such as the European Green Deal and Important Projects of Common European Interest (IPCEI). While well-designed policies can address market failures, improve efficiency, and leverage economies of scale, unilateral approaches risk generating negative externalities, including overcapacity, deteriorating terms of trade, and reduced comparative advantages. Greater cross-country coordination would help optimize outcomes, prevent inefficient relocations, and foster mutual incentives for more effective policy implementation.[43]

Turning to sectoral sentiment, Purchasing Managers' Index (PMI) data for manufacturing and services provide timely insights into economic dynamics. In the manufacturing sector, sentiment is improving across the four largest Eurozone economies. Germany, France, and Italy have all shown upward trends in recent months, approaching the expansion threshold of 50. Spain stands out with PMI readings well above this level, indicating a broadly positive outlook among manufacturers.

The services sector presents a more nuanced picture. In France and Germany, PMI readings are near or below the expansion threshold—declining in Germany and rising in France. In contrast, Spain and Italy remain above the 50-point mark, though their trends have been relatively stable.

[43] Andrew Hodge, Roberto Piazza, Fuad Hasanov, Xun Li, Maryam Vaziri, Atticus Weller, and Yu Ching Wong. "Industrial Policy in Europe: A Single Market Perspective", *IMF Working Papers* 2024, 249 (2024), accessed July 18, 2025, https://doi.org/10.5089/9798400295690.001.

Figure 19: Purchasing Managers Index (PMI), manufacturing

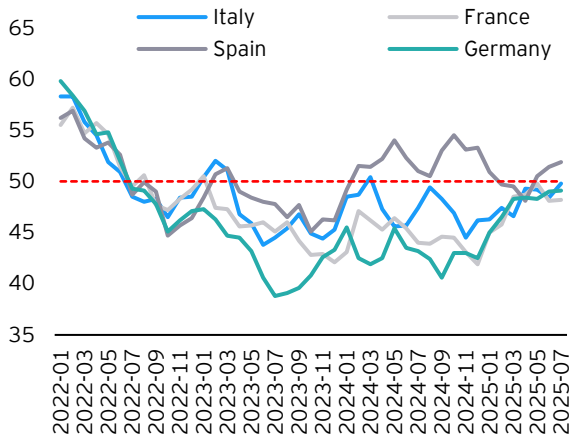
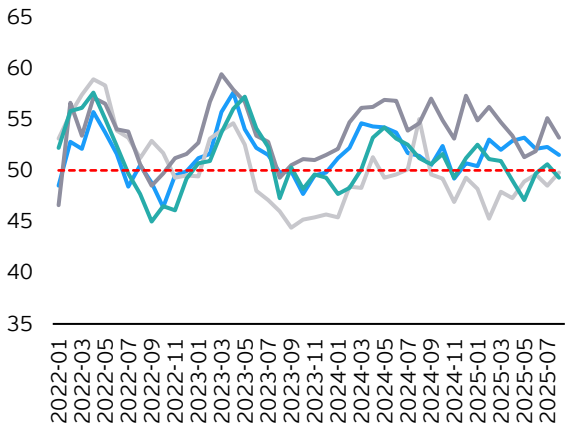


Figure 20: Purchasing Managers Index (PMI), services



Source: EY elaborations based on S&P Global data. Latest data available: August 2025.

Monetary Policy and Prices in the Eurozone

On 11 September 2025, the European Central Bank decided to keep its key monetary policy interest rates unchanged,[44] taking into account the current and expected inflation rate (around 2%) as well as the general economic situation and possible developments that could lead to a rise in the price index.

The ECB's Survey of Professional Forecasters for the third quarter of 2025[45] confirms the institution's inflation expectations. Forecasts indicate inflation at 2.0% in 2025, 1.8% in 2026, and 2.0% in 2027. These figures represent downward revisions of 0.2 percentage points for both 2025 and 2026, consistent with the ECB staff projections published in September 2025.[46] Respondents cited declining energy prices—particularly for oil and natural gas—and the appreciation of the euro, which exerts a disinflationary effect by reducing the relative cost of dollar-denominated imports, as key drivers of the downward revision. However, some forecasters noted the potential persistence of inflation in food prices, driven by supply-side constraints and adverse climatic conditions.

As for the latest decision, the interest rates on the main refinancing operations, the marginal lending facility, and the deposit facility stand at 2.15%, 2.40%, and 2.00%, respectively.

[44] ECB, Monetary policy decisions, 11 September 2025. For more information, https://www.ecb.europa.eu/press/pr/date/2025/html/ecb.mp250911~6afb7a9490.en.html.
[45] The ECB Survey of Professional Forecasters, Third quarter of 2025, July 2025. For more information, https://www.ecb.europa.eu/stats/ecb_surveys/survey_of_professional_forecasters/pdf/ecb.spf2025q3.en.pdf.
[46] ECB staff macroeconomic projections for the euro area, September 2025. For more information, https://www.ecb.europa.eu/pub/pdf/other/ecb.projections202509_ecbstaff~c0da697d54.en.pdf.

Figure 26: European Central Bank monetary policy reference interest rates

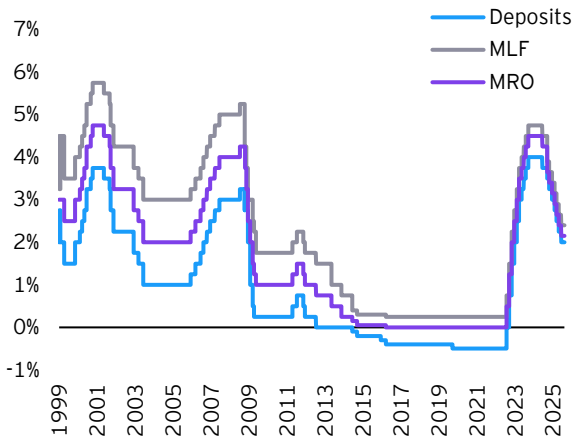
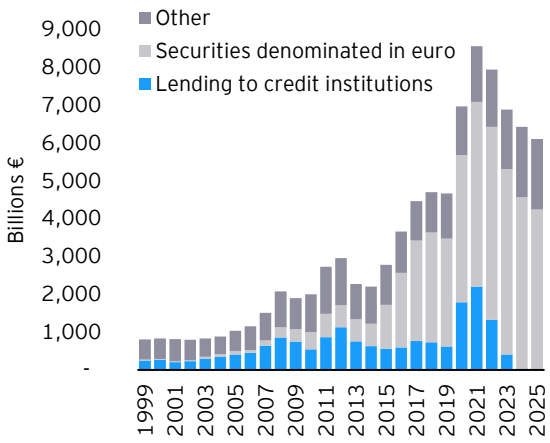


Figure 27: Main items in the European Central Bank's balance sheet (€ billion)



Source: EY elaborations based on European Central Bank (ECB) data. MLF = marginal lending facility; MRO = main refinancing operation. The deposit rate refers to deposits with the central bank. Balance sheet items – loans to credit institutions: these are loans to credit institutions in the Eurozone related to monetary policy operations denominated in euro (the various items include main refinancing operations and LTROs); euro-denominated securities: these are securities denominated in euro held by Eurozone residents (these items include assets acquired for monetary policy purposes); other: these items include gold and foreign currency-denominated claims on Eurozone residents and non-residents. The latest data available for 2025 refers to the weekly financial statement of 1 August 2025.

Focusing on the effects of the restrictive monetary policy implemented in previous years, this not only allowed inflation to return to levels aligned with the price stability objective, but also had an impact on Europe's emerging economies. In fact, studies have shown that the ECB's monetary tightening leads to more than proportional increases in government bond yields in "emerging Europe",[47] together with significant increases in government bond spreads, depreciation of local currencies and a significant reduction in production.[48] This phenomenon refers both to "conventional" monetary policy, achieved mainly through interest rate increases, and to a reduction in the central bank's balance sheet, whereby the effects are moderate when tightening is carried out in a predictable manner, but can become significant if the pace of tightening is unexpectedly accelerated. Finally, the negative effects tend to be more pronounced under a fixed exchange rate regime than under an inflation targeting regime with a flexible exchange rate.

The restrictive monetary policy cycle in place since mid-2023, together with a more or less significant reversal of certain external factors (such as commodity price trends), has been effective in bringing inflation back to target levels.

[47] The countries considered are Albania, Belrus, Bosnia-Erzegovina, Bulgaria, Croatia, Hungary, Kosovo, Macedonia, Moldavia, Montenegro, Poland, Romania, Serbia e Turkey, excluding Russia and Ukraine due to the the ongoing war.
[48] 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.

Figure 28: Inflation rate, Eurozone – % change YoY

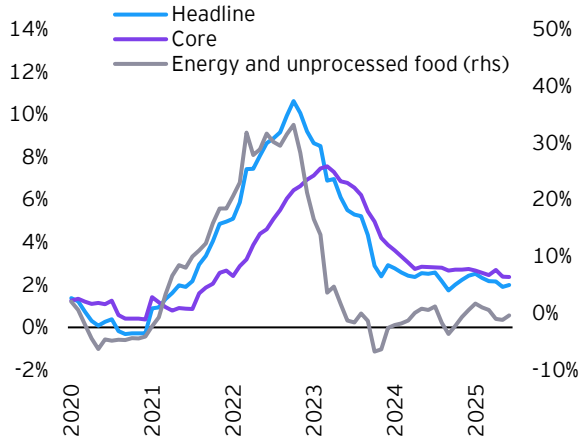
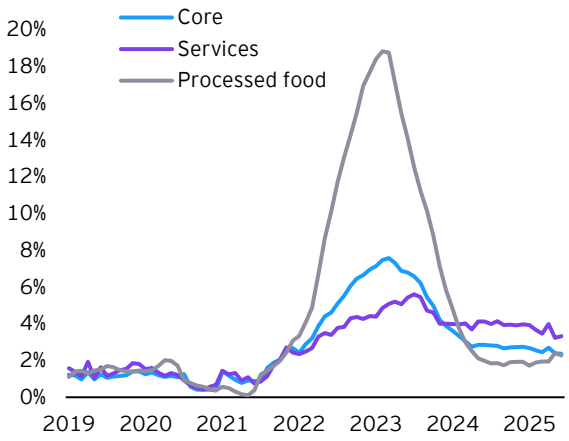


Figure 29: Inflation rate, Eurozone – % change 3 months on 3 months annualised



Source: EY elaborations based on Eurostat data. The headline measure considers all goods in the basket used to calculate price changes; the core measure considers the goods in the headline basket net of energy and fresh food. The rates refer to harmonised rates. Latest data available: July 2025.

In July, headline inflation (inflation that considers all goods in the basket used to monitor price trends) stood at 2.0% in the Eurozone. This figure is in line with the ECB's target, despite the continuing sources of risk for possible increases in inflation (e.g., geopolitical tensions). Core inflation (i.e., the underlying component)[49] continues to show higher and persistent values (2.4% in July, similar to the figure recorded in the previous two months). A similar phenomenon occurred during the pandemic crisis, when energy prices fell significantly due to the slowdown in global economic activity: a core inflation rate higher than the headline inflation rate indicates a rate of change in the underlying component that is higher than that of energy and unprocessed food.

Overall, however, it can be said that the European Central Bank's monetary policy has played an important role in reducing price growth, considering that around 33% of the items in the basket of goods used to calculate core inflation are directly affected by monetary policy decisions (e.g. goods that are often purchased through financing or credit).[50]

The analysis of consumer price trends, and in particular the energy component, is also important from an employment perspective. A study by the European Central Bank has shown that a persistent 10% increase in energy prices (specifically, electricity) can lead to a reduction of up to 2% in employment in the most energy-intensive sectors,[51] with possible further negative consequences (e.g., a reduction in employment in the manufacture of high-tech products corresponds to a further greater reduction in the number of people employed in related service sectors).[52] These effects are expected to be even more significant in areas where energy-intensive manufacturing companies are concentrated, including southern Germany, the Ruhr, northern Italy and, to a lesser extent, northern Belgium.

Another study by the European Central Bank has highlighted how the increase in interest rates needed to manage a rise in inflation rates (e.g. due to an energy price shock) has negative effects on employment.[53] Specifically, a study conducted on Latvia, Estonia and Lithuania shows that a restrictive monetary policy leads to a persistent decline in job openings, while expansionary policies stimulate an increase. On average,

[49] Reference is made to ISTAT's definition of core inflation, which considers the consumer price index net of changes in energy and unprocessed food prices.
[50] Allayioti, A., Górnicka, 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.
[51] How enduring high energy prices could affect jobs. The ECB Blog, May 2025. For more information, https://www.ecb.europa.eu/press/blog/date/2025/html/ecb.blog20250505~86c88d726c.en.html.
[52] Bijnens, G. et al. (2021), "The interplay between green policy, electricity prices, financial constraints and jobs: firm-level evidence", *Working Paper Series*, No 2537, ECB.
[53] Cevik, S., Fan, A., & Naik, S. (2025). Monetary Shocks and Labor Markets: Evidence from Online Job Vacancy Postings. IMF Working Papers, 2025(058). Retrieved Jul 18, 2025, from https://doi.org/10.5089/9798229004251.001.

an unexpected 1 percentage point increase in short-term rates reduces job openings by 2% over a period of about 15 days in the countries analysed.

In this regard, it is worth noting that the increase in energy prices does not necessarily lead to a direct and linear increase in inflation: the effect on consumer price trends depends on specific sectoral characteristics (e.g., price elasticity as energy costs vary), as well as on the presence of non-linear transmission factors between energy prices and consumer prices.[54,55]

As mentioned above, core inflation remains high. This also depends on the trend in the services component within the basket considered for the inflation analysis: wage growth in the services sector plays a crucial role in the trend in services prices, with possible persistent effects on the general price level.[56]

Figure 30: Real wages in the services sector, Eurozone – index, 2015=100

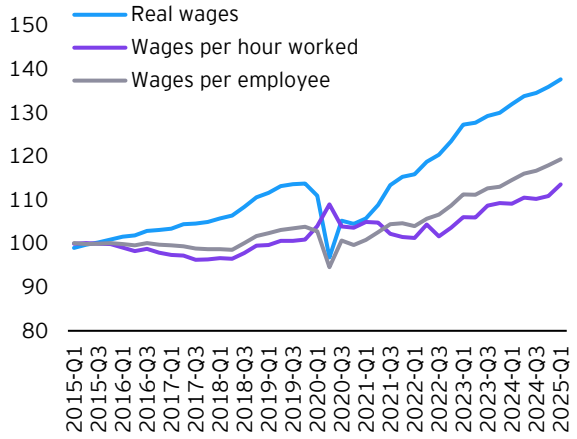
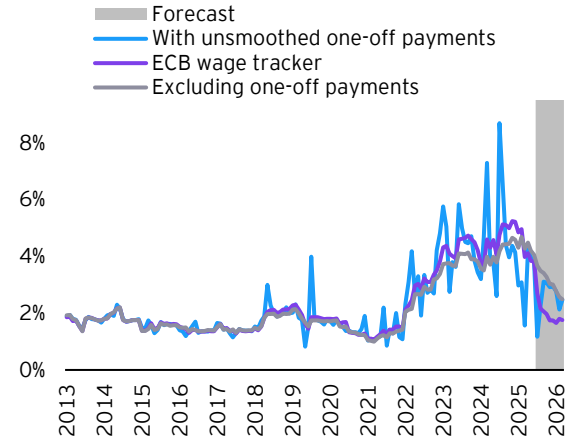


Figure 31: ECB wage tracker, Eurozone – negotiated wage growth



Source: EY elaborations based on Eurostat data, European Central Bank.

Therefore, while the dynamics of the services component in the price index basket are playing an important role in the persistence of inflation in the Eurozone, it is important to note that these pressures have been easing in recent months. The ECB wage tracker provides some interesting insights in this regard. This indicator draws on a broad and detailed database of collective labor agreements, collecting and aggregating information on wage growth from agreements between trade unions and employers' associations.[57] One of the advantages of the indicator is that it provides timely information on agreements that have recently come into force.[58]

Although the ECB wage tracker is not a forecasting tool, this indicator can provide us with more frequent information, potentially anticipating the structured data that will be derived from national accounts or other sources. The data shown, which takes into account agreements signed up to June 2025, points to a reduction in wage pressures during 2025 and 2026. This phenomenon seems even more pronounced for the series that does not take into account "one-off payments"[59] made in 2024 to meet specific needs (e.g. bonuses) and which will no longer be made in 2025.[60]

[54] Alvarez, J. A., & Kroen, T. (2025). The Energy Origins of the Global Inflation Surge. IMF Working Papers, 2025(091). Retrieved Jul 18, 2025, from https://doi.org/10.5089/9798229008310.001.
[55] Bobeica, E., Holton, S., Huber, F., & Hernández, C. M. (2025). Beware of large shocks! A non-parametric structural inflation model. ECB Working Paper Series No 3052.
[56] Chen, S., & Igan, D. (2024). Inflation and Labor Markets: A Bottom-Up View October 2024. IMF Working Paper WP/24/220, 2024 Oct.
[57] The headline "ECB wage tracker" aims to track the annual growth of employees' salaries at any point in time and includes one-off payments smoothed over the twelve months that follow each payment. As one-off payments can make series very volatile, smoothing them renders the series easier to interpret and more aligned to their economic intent (that they cover a period of time even if they are disbursed in one payment). The ECB wage tracker also publishes an indicator with unsmoothed one-off payments.
[58] Lane, P. (2024), "Underlying inflation: an update", Speech at the Inflation: Drivers and Dynamics Conference 2024 organised by the Federal Reserve Bank of Cleveland and the ECB; Bing, M., S. Holton, G. Koester, and M. Roca I Llevadot (2024): "Tracking euro area wages in exceptional times", ECB Blog post, 23 May 2024; Gornicka, L. and G. Koester (eds) (2024): "A forward-looking tracker of negotiated wages in the euro area", Occasional Paper Series, No 338, ECB.
[59] For more information, https://www.ecb.europa.eu/press/pr/date/2024/html/ecb.pr241218_1~1acca7fac8.en.html.
[60] New data release: ECB wage tracker continues to show easing wage pressures, https://www.ecb.europa.eu/press/pr/date/2025/html/ecb.pr250730~a2ed7e7d9e.en.html.

In addition to the labor market, the issue of inflation is closely linked to trends in bank lending. The effects that current interest rates are having on bank lending can be inferred from the latest edition of the Eurozone Bank Lending Survey[61] which offers some interesting insights.[62] In the second quarter of 2025, Eurozone banks reported substantially stable credit supply conditions for businesses (net percentage of banks at -1%). This follows a slight tightening of credit standards for loans to businesses in the first quarter of 2025 (net percentage of 3%), which was, however, lower than banks had expected in the previous survey (net percentage of 5%).

Figure 32: Bank lending conditions for enterprises, Eurozone – net percentage of respondents

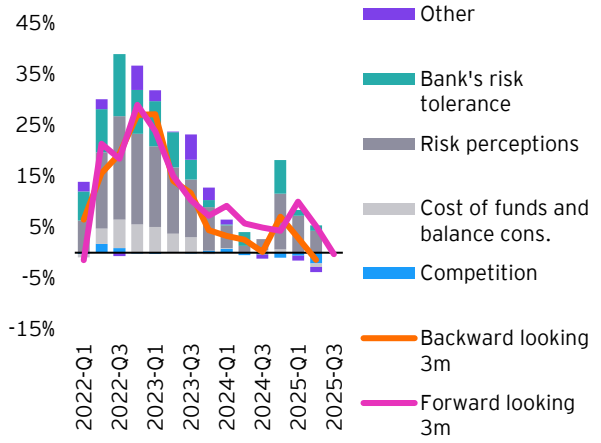
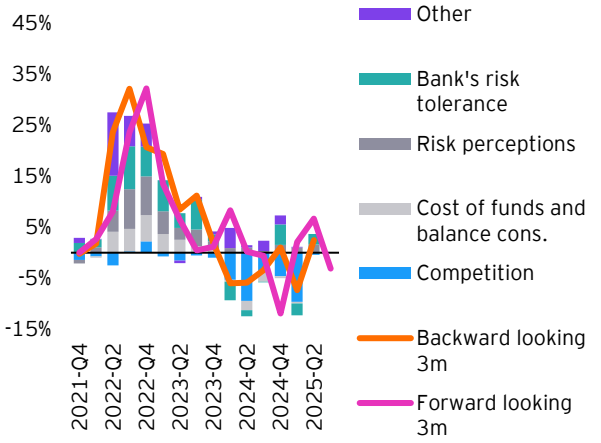


Figure 33: Bank lending conditions for households, Eurozone – net percentage of respondents



Source: EY elaborations based on European Central Bank data (Bank Lending Survey). For households, reference is made to the conditions of supply relating to loans for the purchase of a home. Net percentages are defined as the difference between the sum of the percentages of banks that responded 'significantly tightened' and 'slightly tightened' and the sum of the percentages of banks that responded '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 given factor contributed to a tightening and the percentage of banks reporting that it contributed to a loosening.

Among the main Eurozone economies, banks in Germany reported a net tightening of lending standards for businesses in the second quarter of 2025, while banks in Italy reported a net easing. In Spain and France, credit conditions remained broadly unchanged. Across all four countries, perceived risks related to the general economic outlook and sector-specific developments contributed to a tightening of credit standards. However, geopolitical uncertainty and trade tensions were not considered significant drivers of this tightening, according to survey respondents.

Competition among banks—and, to a lesser extent, from non-bank financial intermediaries—exerted a net easing effect on credit supply conditions for businesses. This effect was most evident in Italy. Meanwhile, Eurozone banks' risk tolerance, funding costs, and balance sheet constraints had a broadly neutral impact. Looking ahead to the third quarter of 2025, banks expect lending standards for business loans to remain unchanged (net percentage of 0%), regardless of firm size.

With respect to household lending, Eurozone banks reported a slight net tightening of credit standards for house purchase loans in Q2 2025 (net percentage of +2%). This follows a net easing in Q1 (−7%) and represents the most significant tightening since the end of the monetary policy tightening cycle in Q3 2023. However, the actual tightening was less severe than anticipated (expected net percentage of +7%). Among the four largest economies, only German banks reported a net tightening, while conditions remained stable in Spain, France, and Italy.

The tightening in household credit supply was primarily driven by increased perceived risks and lower risk tolerance. The easing effect from competition, which had been observed since late 2023, was negligible in

[61] 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 aimed at credit policy managers at the main banks in the area (around 150). The survey makes it possible to highlight, on the one hand, the factors influencing the supply of credit and the terms and conditions offered to customers and, on the other, the trend in credit demand and its determinants.
[62] The euro area bank lending survey – Second quarter of 2025.

Q2. In Germany, lower risk tolerance was the main factor behind the tightening. For Q3 2025, banks expect a slight easing in lending standards for house purchase loans (net percentage of −3%).

While the ECB's Bank Lending Survey shows an improvement in credit supply conditions in the Eurozone, which is reflected in positive credit trends, it is important to note that high interest rates, especially in previous quarters, have led to a deterioration in the ability of Eurozone households to repay their debts. This deterioration was more pronounced in the case of variable-rate debt, which was therefore more affected by the increase in monetary policy interest rates necessary to cope with high inflation,[63] a phenomenon similar to that observed in the wake of the Great Financial Crisis of 2007-2008.[64]

Moreover, higher interest rates tend to increase the share of new loans issued at variable rates (and vice versa when rates decline), gradually altering the composition of outstanding loans. This shift affects the rigidity of household budget constraints and modulates the strength of monetary policy transmission channels—particularly the impact on consumption, which is more pronounced when variable-rate loans dominate.[65]

Figure 34: Loans to businesses and households, Eurozone – YoY change

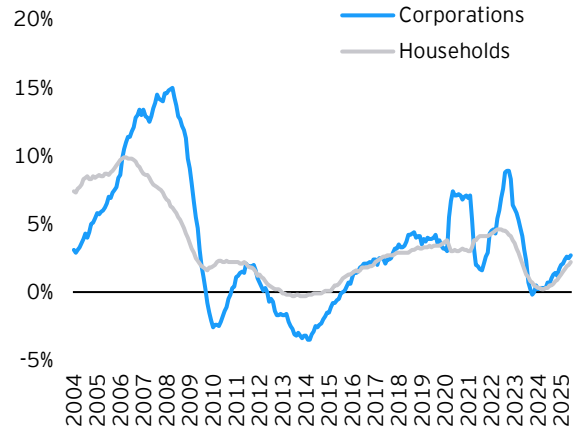
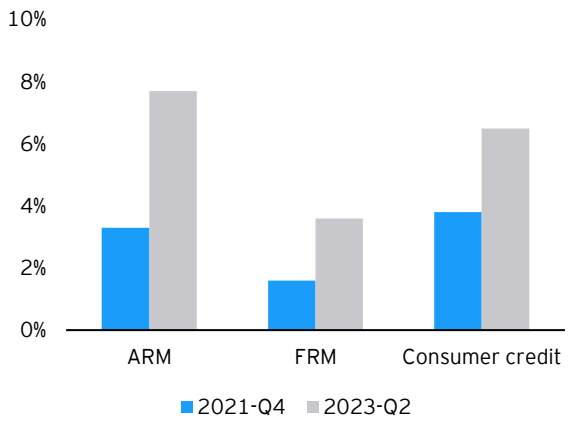


Figure 35: Percentage of non-performing loans, Eurozone



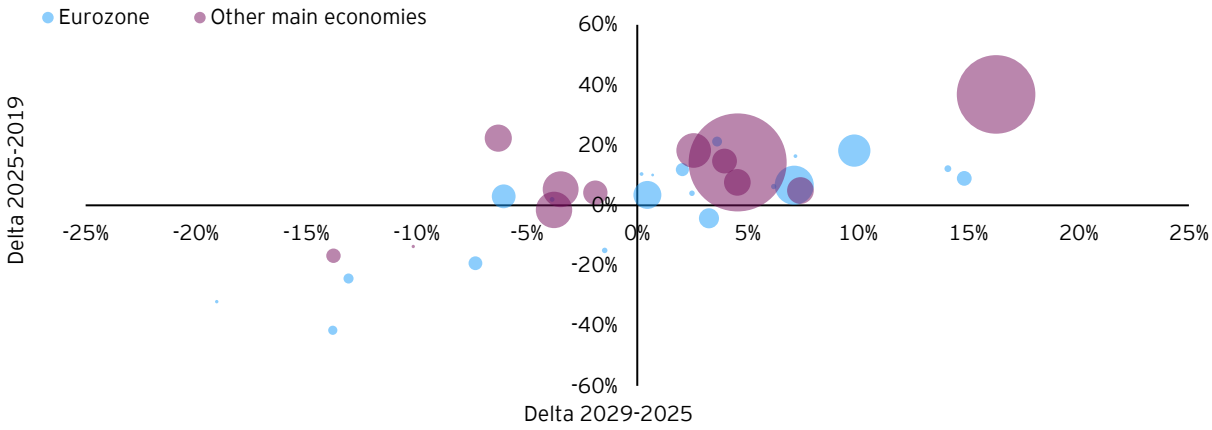
Source: EY elaborations on ECB data. ARM: adjustable-rate mortgages; FRM: fixed-rate mortgages.

Returning to the topic of inflation, it is worth noting that price dynamics may also be influenced by the level of public debt. A recent ECB study examined the interaction between fiscal policy and inflation in the Eurozone, highlighting how public debt levels can amplify the inflationary effects of fiscal expansions. Specifically, high debt levels tend to increase the sensitivity of inflation to expansionary fiscal measures.[66]

Overall, public debt-to-GDP ratios in Eurozone countries have risen significantly in response to the fiscal measures adopted during the pandemic and the energy crisis. These ratios remain elevated compared to pre-pandemic levels.

[63] Palligkinis, S. (2025). Bank lending rates and the riskiness of euro area household loans. ECB Working Paper Series No 3053.
[64] Di Maggio, Marco, Amir Kermani, Benjamin J. Keys, Tomasz Piskorski, Rodney Ramcharan, Amit Seru, and Vincent Yao (2017), Interest rate pass-through: mortgage rates, household consumption, and voluntary deleveraging, American Economic Review, 107(11), 3550-3588.
[65] De Stefani, A., & Mano, R. (2025). Long-Term Debt and Short-Term Rates: Fixed-Rate Mortgages and Monetary Transmission. *IMF Working Papers*, *2025*(024). Retrieved Jul 18, 2025, from https://doi.org/10.5089/9798400296086.001
[66] With regard to the relationship between public debt and inflation, according to the so-called fiscal theory of prices, an expansionary fiscal policy that is not accompanied by higher projected future primary surpluses leads economic agents to perceive greater real wealth, leading to an increase in consumption and, consequently, in prices. More generally, if the present value of future primary surpluses is less than the amount of nominal debt, the equilibrium price level is expected to increase (reducing the real value of the debt) to ensure solvency. For more information, Checherita-Westphal, C. D., & Pesso, T. (2024). Fiscal policy and inflation: accounting for non-linearities in government debt. ECB Working Paper Series No 2996.

Figure 36: Changes in the public debt-to-GDP ratio in the Eurozone and other major world economies, 2025-2019 and 2029-2025



Source: EY elaborations based on European Central Bank data. Size represents GDP in dollars. 'Other major economies' include: Argentina, Australia, Brazil, Canada, China, Korea, Japan, India, Iceland, the United Kingdom, Russia and the United States.

There may also be pressure on spending in the medium and long term due to higher planned expenditure in the defense sector and to address structural issues such as climate transition and population ageing. In this context, there could be an increased risk that the public debt-to-GDP ratio will not stabilise in the medium term but will continue to rise in the coming years. However, the increase in the public debt-to-GDP ratio is not a phenomenon unique to the Eurozone countries, but represents a widespread global trend, even among advanced economies.[67] It should be noted, however, that in the Eurozone, the Central Bank's securities purchase programmes have enabled countries to maintain a long-term issuance profile, alleviating short-term financing pressures.[68]

The overall picture for the Eurozone remains challenging. On the one hand, economic activity is essentially weak, with the industrial sector continuing to show signs of difficulty. Restrictive monetary policy has played an important role in reducing price increases, but the process of bringing inflation down seems to have slowed in recent months, partly due to positive developments in the labor market and wages. The current level of public debt and the prospects for growth in the coming years also pose a major challenge for the Eurozone economies, limiting the fiscal policy actions needed to address future complexities (e.g., defense spending, climate transition, and others). Finally, the political uncertainty that has been characterizing some Eurozone countries in recent months, specifically France, should also be taken into account, as it further complicates the overall macroeconomic environment, with possible spillover effects on the other countries of the Monetary Union.

[67] IMF Blog (2025), Debt is Higher and Rising Faster in 80 Percent of Global Economy. For more information, https://www.imf.org/en/Blogs/Articles/2025/05/29/debt-is-higher-and-rising-faster-in-80-percent-of-global-economy.
[68] 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.

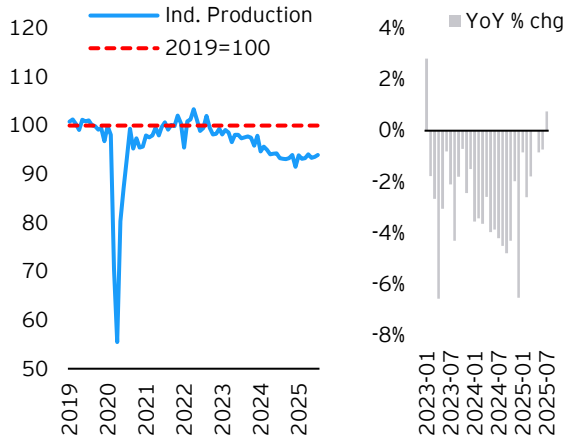
The Italian economy

The real economy

The Italian industrial sector remains in crisis, despite recording year-on-year growth in July (compared to the same month last year) after 29 months of negative growth. In July, the industrial production index in Italy recorded a year-on-year growth of 0.7%, after a contraction of the same magnitude in June and May (-0.7% and -0.8% respectively).

While the growth in July is certainly a positive sign, on the other hand, it should be noted that the index value is significantly lower than the average values for 2021 (approximately 6 percentage points lower).

Figure 37: Industrial production index (average 2019=100) and % change YoY, Italy



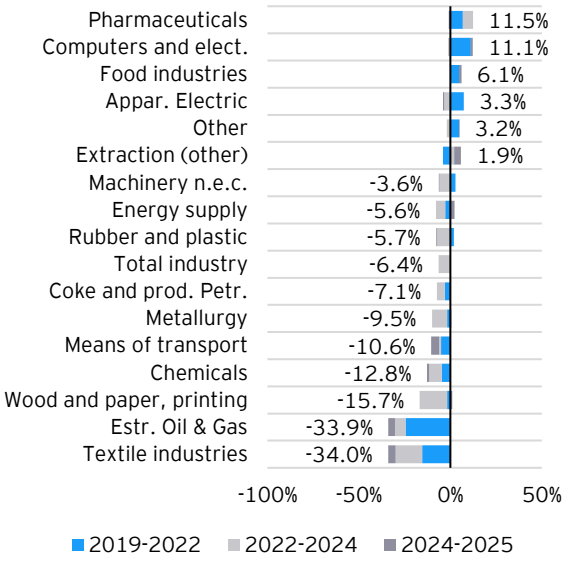
Source: EY elaborations on ISTAT data. The indices refer to seasonally adjusted indices. Latest data available: July 2025.

The month-over-month growth in June and July 2025 was also positive, with growth of 0.2% and 0.4% respectively.

The industrial production index provides an overall picture of the industrial situation in Italy, but detailed information can be obtained by analysing the dynamics of the indices for the various industrial sectors.

Specifically, in manufacturing, in July 2025, the manufacture of coke and petroleum refining products recorded the highest year-on-year growth, at 10.7%, followed by the manufacture of computers and electronics (5.8%) and the production of food products (5.1%). In contrast, chemicals, rubber and plastics, and textiles recorded declines on a year-on-year basis (-2.9%, -1.5% and -0.7%, respectively).

Figure 38: Industrial production index by industrial sector, Italy – % change compared to 2019 and contributions for years analysed



Source: EY elaborations based on ISTAT data. Machinery n.e.c.: Manufacture of machinery and equipment not classified elsewhere.

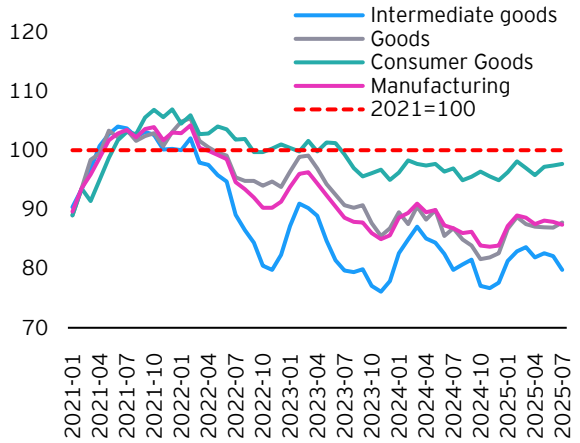
Taking a longer-term view, it is possible to obtain additional information on the performance of industry in Italy. Compared to 2019, the pharmaceutical industry, the manufacture of computers and electronic products, and the food industry are the top three industrial sectors in

terms of positive performance, with growth of 11.5%, 11.1% and 6.1% respectively.

On the other hand, the textile industry, crude oil and natural gas extraction, wood and paper products, and chemical production are still far from pre-crisis levels (with production down by 34.0%, 33.9%, 15.7% and 12.8% respectively). It should be noted that these sectors are among the most energy-intensive, and that the trend in energy costs in recent years has perhaps had a structural impact on the Italian industrial fabric.

The negative trend in Italian industry is also confirmed by business confidence, which is also below the average levels experienced during 2019, as shown by the latest results of the manufacturing business confidence survey.[69]

Figure 39: Business confidence in the manufacturing sector, Italy – index, 2021=100



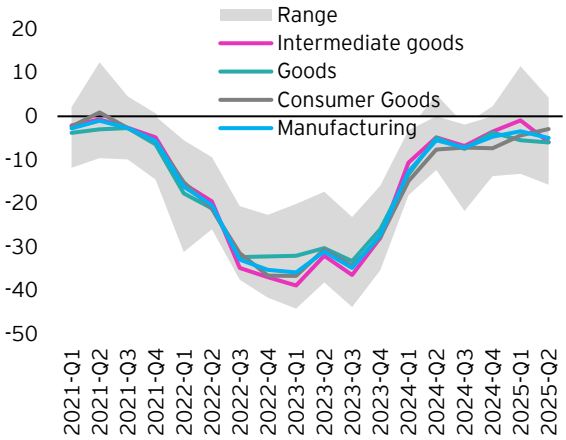
Source: EY elaborations based on ISTAT data. Intermediate goods: goods used as inputs in a production process; Capital goods: goods used in the production of other goods (machinery, means of transport, etc.), intended to be used for a period of more than one year; Consumer goods: goods used without further processing for the direct satisfaction of individual or collective needs (based on their duration, they are divided into durable consumer goods and non-durable consumer goods). For more information, https://www.istat.it/storage/IstatData/Coeweb/Glossario.pdf .

Confidence among manufacturing companies producing intermediate goods is experiencing a more pronounced decline than other components.

The dynamics of the industrial sector are also linked to the weakness of European industry and, in particular, Germany, which is one of the main markets for Italian intermediate products. Poor performance by German industry translates into lower demand for intermediate goods, which in turn leads to a slowdown in the Italian sector.

Despite the weakness of Italian industry and the unstable geopolitical context affecting the national economy, the gradual decline in interest rates is leading to a reduction in the number of companies experiencing difficulties in obtaining credit.

Figure 40: Access to credit for companies in the manufacturing sector, Italy – balance of respondents



Source: EY elaborations based on ISTAT data. The gray area represents the range within which the values of the various industrial sectors are contained. The series shown refer to the net balance of respondents based on their answers (more favorable access to credit, constant, less favorable, don't know).

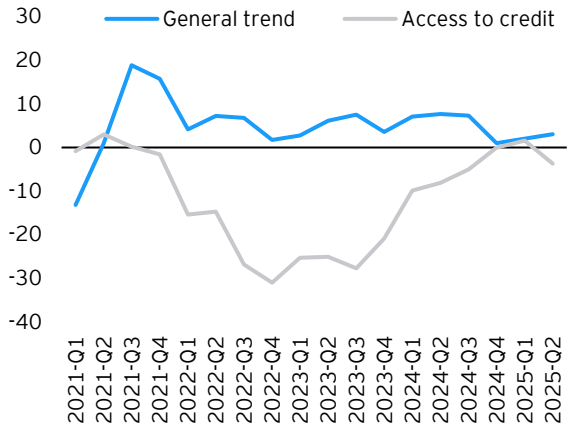
The most recent data show a net negative percentage among respondents to the manufacturing business confidence survey regarding access to credit. This indicates that a greater number of companies report less favorable conditions for access to credit than those reporting an improvement in this regard. However, it should be noted that the balance has been increasingly less negative in recent quarters, reflecting a complicated environment.

Less favorable access to credit affects not only the manufacturing sector, but also the service

[69] L'indagine è finalizzata alla rilevazione di variabili qualitative quali giudizi e aspettative a breve termine (3 mesi) delle principali variabili aziendali (quali giudizi e aspettative su ordinativi, produzione e liquidità; giudizi sulle giacenze di prodotti finiti; aspettative sull'occupazione e sui prezzi di vendita) e valutazioni sulla situazione generale dell'economia italiana. Trimestralmente sono richieste ulteriori informazioni su diversi aspetti aziendali dell'impresa (quali capacità produttiva, numero di ore lavorate, nuovi ordinativi, scorte di materie prime, volume delle esportazioni, ostacoli alla produzione, durata della produzione assicurata e grado di utilizzo degli impianti) e sulla posizione concorrenziale dell'impresa. L'unità di rilevazione e di analisi è l'impresa.

sector, despite the overall positive trend in economic activity in the sector.

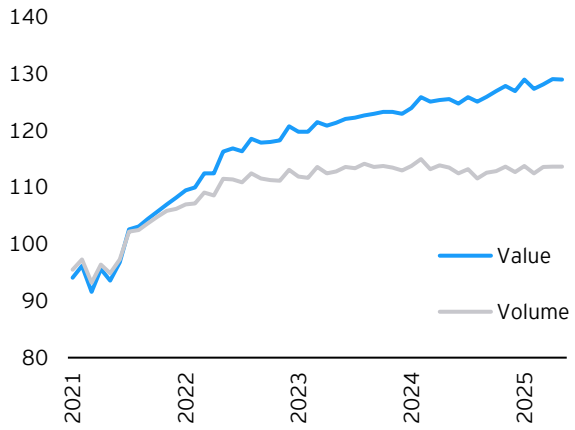
Figure 41: Confidence in the service sector and access to credit, Italy – balance of respondents



Source: EY elaborations based on ISTAT data.

With regard to the performance of the services sector, which accounts for more than 70% of Italy's total added value, it should be noted that the trend is not particularly positive, despite showing better overall dynamics than those of industry. An analysis of the sector's turnover shows that, in nominal terms, growth has been significant (an increase of around 30% since 2021); however, this growth is largely attributable to the rise in prices since 2022: in real terms, overall growth has been more modest (around 15%).

Figure 42: Index of the value and volume of turnover for services, Italy – index, 2021=100

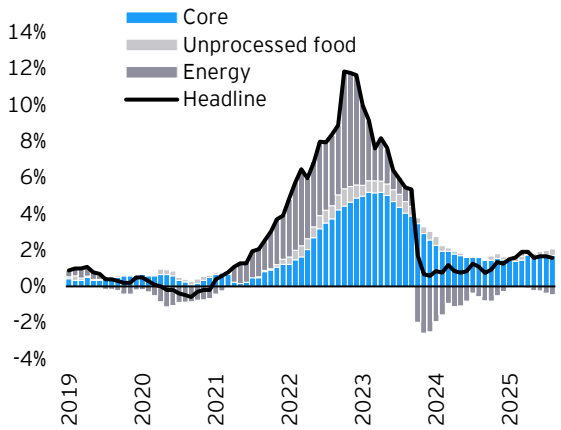


Source: EY elaborations based on ISTAT data. Latest data available: June 2025.

Price trends and the labour market in Italy

After rising between September 2024 (inflation rate of 0.7%) and April 2025 (1.9%), the inflation rate remained essentially constant in the second quarter and the first month of the third quarter, hovering between 1.6% and 1.7% YoY percentage change (1.6% in August).

Figure 43: Inflation and components, Italy – % YoY change and percentage points

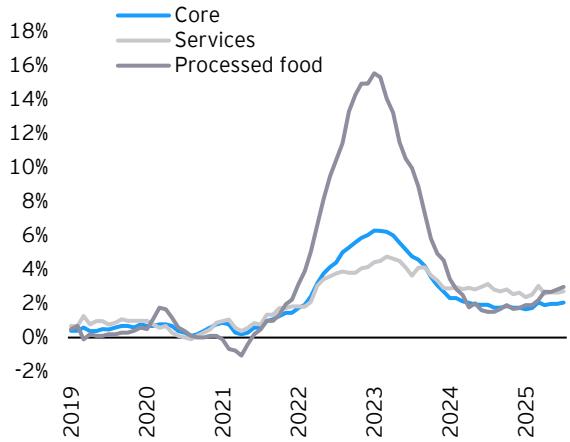


Source: EY elaborations based on ISTAT data. Latest data available: August 2025.

This trend is the result of a slightly negative contribution to price growth from the energy component, against a substantially stable core component (core inflation) and a food component that continues to show a positive contribution to price growth.

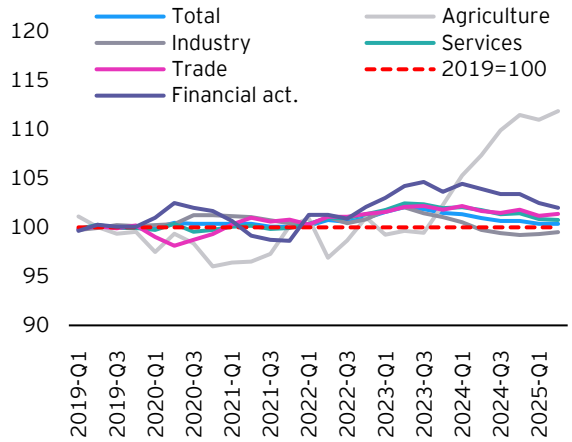
Core inflation in August rose by 2.1% compared to the same month last year, a figure broadly in line with that seen in recent months (April-July average: 2.0%). This is mainly due to the performance of the services component (stable since 2024) and a processed food component that has made a more significant positive contribution in recent months.

Figure 44: Core inflation and components, Italy – % change YoY and percentage points



Source: EY elaborations based on ISTAT data. Latest data available: August 2025.

Figure 45: Markups by sector of activity, Italy – index, 2019=100



Source: EY elaborations based on ISTAT data. The markup is calculated as the ratio between the output deflator and variable unit costs. With regard to sectors: for agriculture, reference is made to the "agriculture, forestry, and fishing" sector; for industry, reference is made to the "mining, manufacturing, electricity, gas, steam, and air conditioning supply, water supply, sewerage, waste management, and remediation activities, construction" sector; for trade, reference is made to the sector "wholesale and retail trade, repair of motor vehicles and motorcycles, transport and storage, accommodation and food services, information and communication services"; for financial activities, reference is made to the sector "financial and insurance activities, real estate activities, professional, scientific, and technical activities, administration, and support services"; for services, reference is made to all other services.

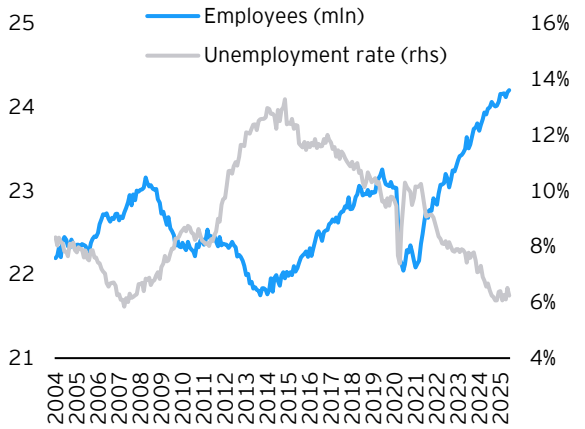
In general, the trend in the price index is also partly linked to the trend in mark-ups in individual sectors of the Italian economy, for which there are significant sectoral differences.

In the period following the pandemic (2022-2023), there was an increase, albeit not particularly pronounced, in mark-ups in the main economic sectors in Italy. In this context, two sectors showed different dynamics compared to the general trend: the agricultural sector, where mark-ups will remain similar to the average quarterly values for 2019, and the financial sector, which saw an increase in mark-ups of around 4.5% towards the end of 2023.

In the following period (2024-2025), sector dynamics underwent further changes: while most sectors, as expected by many analysts, recorded a reduction in their mark-ups, bringing them closer to pre-crisis levels (2019), the agricultural sector is again an exception, recording growth of around 12% compared to the average quarterly values for 2019.

Inflation trends are also linked to labor market dynamics. In this regard, total employment remains at historic highs (around 24.2 million); the unemployment rate remains around 6%, with a substantially stable trend (January-July average of 6.2%).

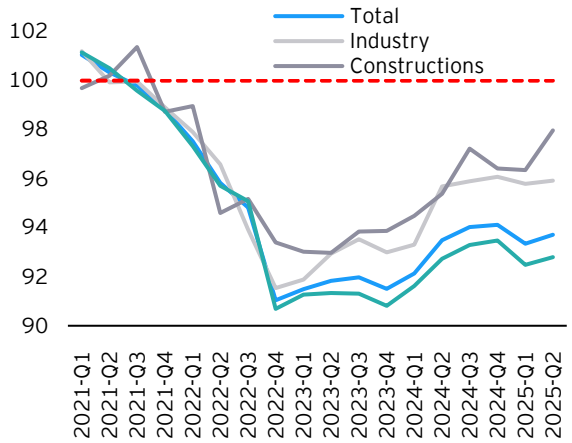
Figure 46: Employment and unemployment rate, Italy



Source: EY elaborations based on ISTAT data. Latest data available: July 2025.

While the positive employment trend is reflected in wage growth (up 1.9% in the second quarter compared to the same quarter of the previous year), it should be noted that real wages per hour worked remain below the level recorded in 2021, despite the positive trend in recent quarters.

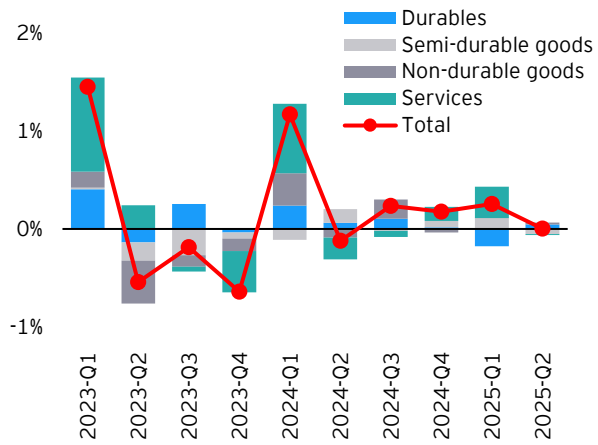
Figure 47: Real wages per hour worked in the macro-sectors of the economy, Italy – index, 2021=100



Source: EY elaborations based on ISTAT data.

Despite the positive trend in the labor market, consumption remained essentially flat in the second quarter of 2025 (0% growth). An analysis of the main components of household consumption (durable, semi-durable, and non-durable goods) shows that the lack of growth affected all categories of goods, with the exception of a few minor movements.

Figure 48: Household final consumption expenditure by expenditure item, Italy – % change QoQ and contributions to growth

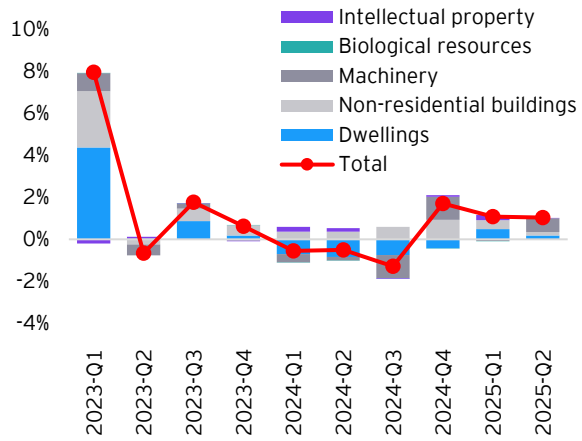


Source: EY elaborations based on ISTAT data.

This halt in household consumption growth can be partly attributed to the general climate of uncertainty that characterized the second quarter of the year, as well as to the stagnation of real wages.

With regard to the other components of GDP, investment continues to show a positive trend, with growth of 1.0% compared to the previous quarter, following similar growth in the first quarter (1.1%) and more sustained growth in the last quarter of 2024 (1.7%).

Figure 49: Investment, Italy – QoQ change and contributions to growth



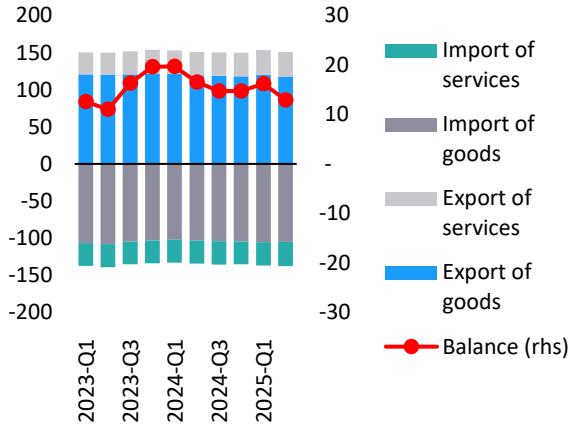
Source: EY elaborations based on ISTAT data.

This growth was partly supported by an increase in investment in plant and machinery, and by a positive contribution from investment in

housing (up 0.6% compared to the previous quarter) and non-residential buildings (0.7%).

Finally, with regard to foreign trade, Italy continued to record a trade surplus (€13 billion) in the second quarter of 2025, mainly supported by exports of goods (€118 billion).

Figure 50: Exports and imports, Italy – billions, €



Source: EY elaborations based on ISTAT data.

Trade remains a risk factor to be monitored closely, given the possible changes in the geopolitical scenario and trade policies, which make the overall context particularly uncertain.

Overall, the Italian economy remains characterized by substantial weakness on the one hand, due to a context of strong uncertainty and a struggling industrial sector, while the services sector shows greater dynamism. On the other hand, signs from the labor market appear encouraging, with the number of people in employment at an all-time high and a potential upturn in consumption in the near future; inflation is essentially stable and in line with the price stability target set by the European Central Bank.

Focus: A historical perspective of the labour market in Italy

Key messages:

1. *Over the last twenty years, Italy's demographic composition has seen a significant increase in the over-45 population, with a direct impact on employment. Growth in employment has been driven mainly by older age groups, particularly the over-55s, who gained around 5 percentage points in the total share of employment between 2018 and 2024.*
2. *From 2015 to 2025, there was a significant decrease in the number of unemployed (-50%) and inactive (-15%) people in the 20-64 age group. This trend was only interrupted by the pandemic crisis in 2020, but subsequently resumed, contributing to employment growth.*
3. *3. Employment growth was mainly driven by permanent employees; after 2022, there was also an increase in the number of self-employed workers.*
4. *The service sector consolidated its central role in the labor market, accounting for around 70% of total employment and with a growing share of total employment over the last twenty years. The construction sector made a positive contribution in the post-pandemic period, thanks in part to tax incentives.*

Recent developments in the Italian labor market make it necessary to carefully examine and analyze the available data in order to obtain additional information useful for accurately understanding the performance of the Italian economy.

A first fundamental element to consider is the composition of the population by age group. Analyzing the phenomenon from a long-term perspective, it is clear that the composition of the Italian population over the last twenty years shows a higher concentration of people over 45, to the detriment of younger age groups. The quarterly analysis of population growth by age group highlights this trend even more clearly, showing how, in a context of overall population decline, the number of people over 45 has increased over time.

Figure 51: Composition of the Italian population by age – percentage of total, 2004 and 2024

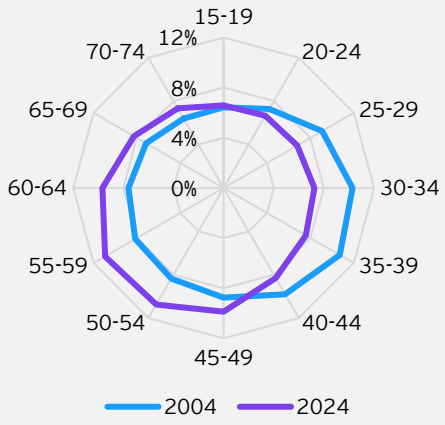
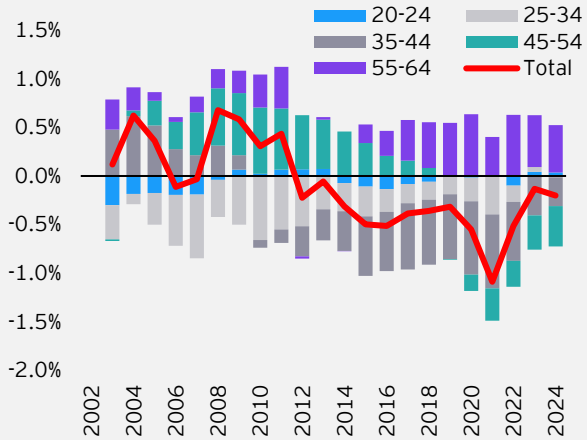


Figure 52: Change in the Italian population by age – millions



Source: EY elaborations based on ISTAT data.

This trend is also reflected in the growth in the total number of people in employment. It is important to note that this increase was largely attributable to growth in the number of people over 55 in employment and, to a lesser extent, to people in younger age groups. It should be noted that, overall, between 2018

and 2024, the composition of employment by age saw an increase in the share of over-55s of almost 5 percentage points, rising from 21% of the total population to around 26%. Conversely, the overall percentage of employment attributable to younger age groups has fallen by an equivalent amount in the total number of employees. This result can potentially be explained in part by the 2011 reform, which raised the retirement age.

Figure 53: Growth in the number of employees by age, Italy – contributions, percentage points

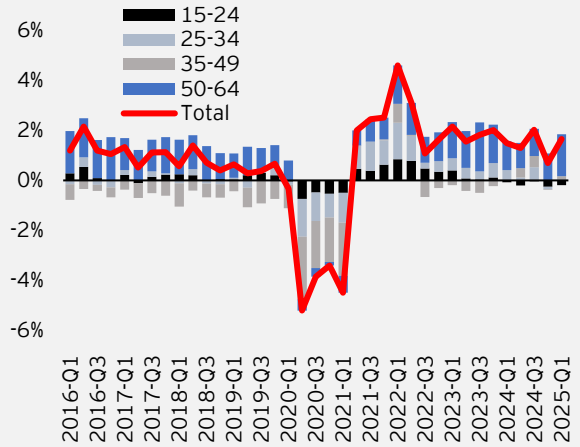
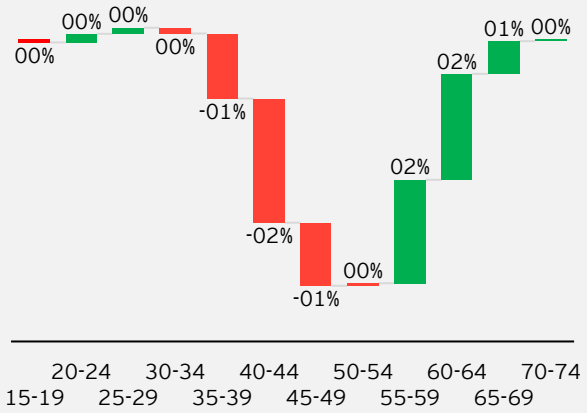


Figure 54: Change in the composition of employees, Italy – 2018-2025



Source: EY elaborations based on ISTAT data.

Parallel to the growth in the number of employees, recent years have seen a reduction in the number of unemployed and inactive persons in the 20-64 age group. The reduction in the number of unemployed and inactive people was greater than the increase in the number of employed people between 2015 and 2025, a phenomenon due in part to the transition of these categories of people to the employed category, and in part to the exit of a portion of the population from the 20-64 age group.

Figure 55: Population by employment status and change 2015-2025, Italy

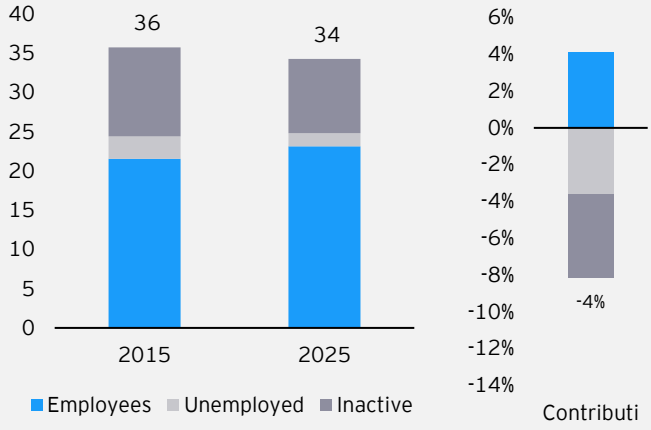
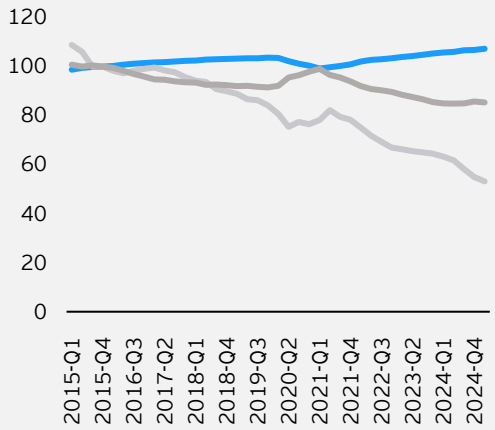


Figure 56: Population by employment status and change, Italy – index, 2015=100



Source: EY elaborations based on ISTAT data.

In this context, it is interesting to observe the dynamics of the population by employment status since 2015. While the number of employees grew during the period under review, with the sole exception of the pandemic period, the number of unemployed and inactive persons fell by approximately 50% and 15%, respectively. The above trends have been observed since the beginning of the period analyzed, with the exception of the phase characterized by the pandemic crisis of 2020, during which there was an increase in both the number of unemployed and inactive persons.

Employment in recent years has also been potentially stable and solid, as confirmed by an analysis of population data by professional position. In fact, when the working population is divided into fixed-term employees, permanent employees, and self-employed workers, it can be seen that permanent employees are the largest category of workers and represent the largest positive contribution to the growth in the number of workers in the period 2015-2025. The growth in the number of permanent employees is also followed by a smaller increase in the number of fixed-term employees, while the number of self-employed and independent workers has decreased.

Analysis of the latest quarterly data also shows that, after 2022, employment growth is essentially attributable, almost entirely, to the growth in the number of self-employed workers, which is a positive factor for household consumption trends.

Figure 57: Population by occupational status and change 2015-2024, Italy

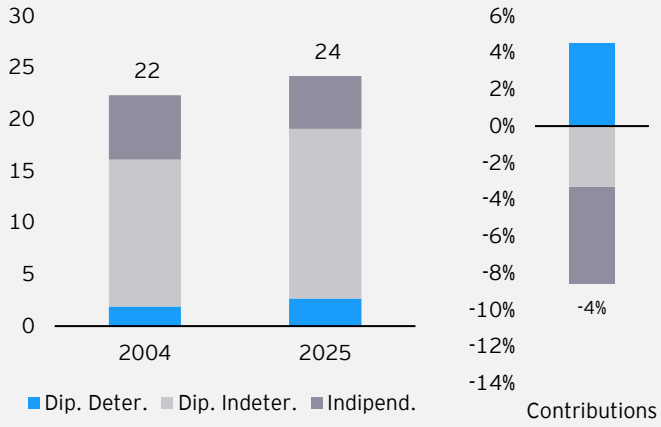
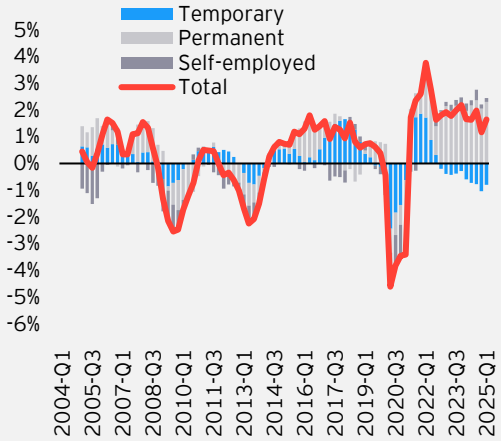


Figure 58: YoY change in population by occupational status, Italy



Source: EY elaborations based on ISTAT data.

Finally, from a sectoral perspective, analysis of long-term data confirms the importance of the service sector, showing not only that around 70% of employment is in the service sector (sectors identified by codes 4 to 10 in the chart below), but also that, over the 20 years analyzed, the percentage of total employment attributable to the service sector increased by around 4%, to the detriment of other sectors (mainly industry, excluding construction).

Figure 59: Employment by sector of activity, Italy – percentage of total

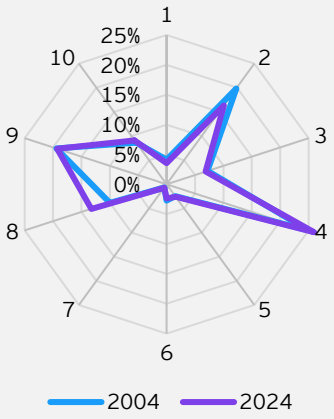
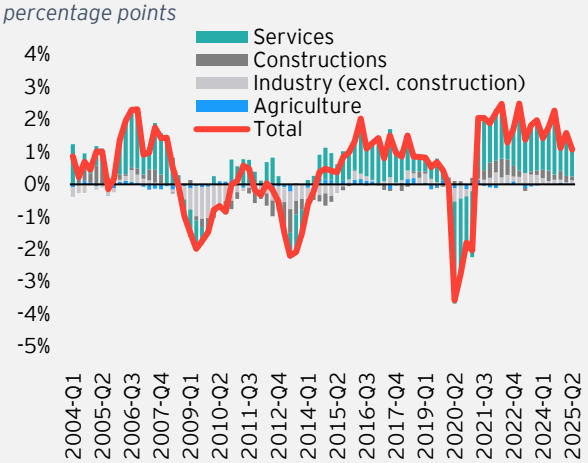


Figure 60: YoY change in employment by sector, Italy – percentage points



Source: EY elaborations based on ISTAT data. 1 – Agriculture; 2 – Industry (excluding construction); 3 – Construction; 4 – Wholesale and retail trade, repair of motor vehicles and motorcycles, transportation and storage, accommodation and food services; 5 – Information and communication services; 6 – Financial and insurance activities; 7 – Real estate activities; 8 – Professional, scientific and technical activities, administration and support services; 9 – Public administration and defense, compulsory social security, education, health and social assistance; 10 – Artistic, entertainment and recreational activities, repair of household goods and other services.

This trend has also been confirmed in recent quarters, where employment growth is mainly attributable to growth in the services sector, while industry and agriculture account for a marginal share. Finally, the construction sector made a notable positive contribution to employment growth in the post-pandemic period, mainly thanks to the fiscal measures and incentives put in place to support the economy after the crisis (e.g., 'Superbonus 110%').

Overall, therefore, it can be said that Italy has seen growth in the number of people in employment over the last twenty years, and that these workers enjoy a certain degree of contractual stability, a phenomenon that has been even more evident in the last few years of the period under review. At the same time, there has been and continues to be a reduction in the number of unemployed and inactive people, following the trend that has been in place since 2015. On the other hand, however, it is important to consider that the growth in employment is mainly attributable, especially in recent quarters, to an increase in employment among older age groups.

The Italian Economy: GDP and EY Forecasts

The second quarter of 2025 saw a quarter-on-quarter contraction (compared to the previous quarter) of 0.1%, following growth of 0.3% in the first quarter. The second quarter result was mainly due to a sharp contraction in exports (-1.7%), following strong growth in the previous quarter (2.1%). The contraction in exports was also accompanied by growth in imports (0.4%), resulting in an overall contribution to foreign trade growth of -0.7 percentage points. Another factor to consider is private consumption, which remained essentially stable compared to the previous quarter (0.0%). On the other hand, the contribution to growth in investments in the second quarter was positive (0.2 percentage points).

From a year-on-year perspective, household consumption and public consumption supported growth with contributions of 0.4 and 0.1 percentage points, respectively. These, together with the strong acceleration in investment (2.5%, corresponding to a contribution to growth of 0.6 percentage points), a negative contribution from foreign demand (-0.8 percentage points) and a slight positive contribution from inventories, led to a year-on-year growth in GDP of 0.4%.

Figure 21: GDP components, Italy – contributions to growth, percentage points

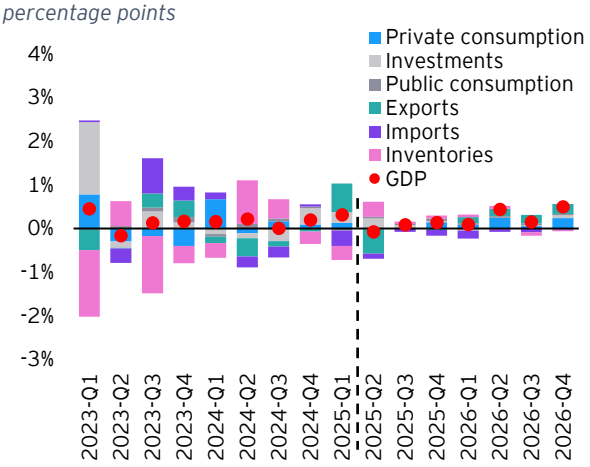
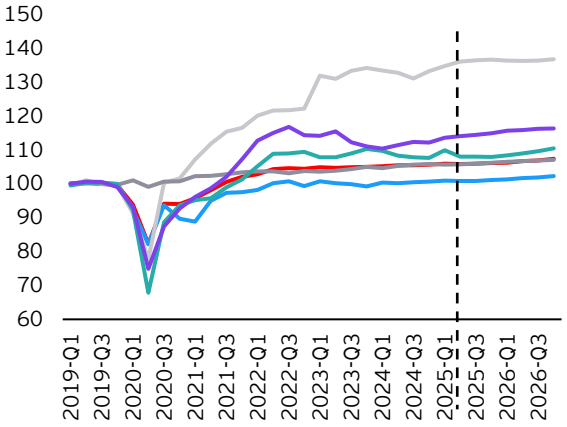


Figure 22: GDP components, Italy – index, quarterly average 2019 = 100



Source: EY elaborations based on Eurostat data and EY forecasts. The dotted line represents the forecast horizon. EY forecasts begin in 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 previous sections and the latest available data, it is possible to outline EY's outlook for the Italian economy. After a slight contraction of 0.1% in the second quarter, weak growth (0.1%) is expected in the third quarter, mainly supported by investments (+0.3%, corresponding to a positive contribution of 0.1 percentage points). Foreign trade will contribute negatively to growth (-0.1 percentage points), while consumption is expected to remain stable. Finally, similar growth is expected in the fourth quarter, with a slight positive contribution from private consumption and a substantial stagnation in investment.

Overall, 2025 is expected to close with growth of 0.5%, mainly driven by investment growth (2.5% for a positive contribution of 0.6 percentage points) and, to a lesser extent, by the positive trend in private consumption, which is expected to grow by 0.5% (for a positive contribution of 0.3 percentage points). Weak growth in exports (0.1%) and more significant growth in imports (2.4%) will lead to an overall negative contribution from foreign demand (-0.6 percentage points), while public consumption is expected to make a positive contribution to growth (0.1 percentage points).

Table 1: Forecasts on the Italian economy

	2021	2022	2023	2024	2025	2026
GDP, % change	8.8%	5.0%	0.8%	0.5%	0.5%	0.7%
Household consumption, % change	5.8%	5.3%	0.4%	0.4%	0.5%	0.8%
Investments, % change	21.5%	7.7%	9.2%	0.0%	2.5%	0.3%
Exports, % change	14.2%	10.6%	0.5%	-0.3%	0.1%	0.8%
Imports, % change	16.0%	13.6%	-1.3%	-1.5%	2.4%	1.5%
Unemployment rate	9.5%	8.1%	7.7%	6.6%	6.4%	6.8%
Consumer price index, % change	1.9%	8.2%	5.6%	1.0%	1.9%	1.9%
Deficit, % of GDP	-8.9%	-8.1%	-7.2%	-3.5%	-3.5%	-3.3%
Public debt, % of GDP	146.1%	138.4%	134.6%	135.5%	137.3%	136.3%

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 note that growth in 2025 will be largely supported by public investment (up 7.7%), while private investment will be less dynamic (up 1.6%). These differences are expected to continue in 2026, when private investment is forecast to contract slightly (-0.6%) while public investment will continue to support growth (4.7%). A more in-depth analysis of investment items shows that the weakness of private investment is largely linked to a contraction in investment in housing (-1.4% in 2025 and -2.4% in 2026), which is in turn due to the end of public incentives (e.g., "Superbonus 110%").

Other investment categories, on the other hand, are expected to grow: investment in non-residential buildings is expected to grow by 7.5% and 0.8% in 2025 and 2026, respectively; investment in machinery is expected to grow by 2.7% and 1.9%; Finally, investments in intangibles will continue on their growth path, with rates of 2.7% and 1.5%.

As for the labor market, the unemployment rate is expected to be 6.4% in 2025, followed by a slight acceleration (6.8%) in 2026. Inflation will remain around the 2% threshold in 2025 and 2026 (1.9% over the two years), in line with the ECB's price stability objective.

The public deficit is expected to be 3.5% in 2025 and 3.3% in 2026, while the public debt-to-GDP ratio will increase, reaching around 136.3% in 2026, after 137.3% in 2025. The forecasts remain subject to a scenario of considerable uncertainty and therefore present significant risks, both downside and upside, mainly related to the global macroeconomic environment.

Assumptions to forecasts

Forecasts and analyses are based on data available as of September 24, 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 2.4% is expected in 2025, followed by a less dynamic growth in 2026 (1.9%);
- **Natural gas prices:** the price of natural gas (based on the Dutch Title Transfer Facility) is assumed to average around $12.2/mmbtu in 2025 and $11.0/mmbtu in 2026;
- **Oil prices:** the average price of oil is expected to be approximately $67.6 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 1.17;
- **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;[70]
- **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.
- **Monetary policy and interest rates**: interest rates are expected to fall by 0.25 percentage points by the end of 2025; rates are expected to remain stable in 2026. The long-term interest rate (10 years) is also expected to show a stable differential with the short-term rate.

Finally, given the current scenario of high uncertainty, below are some downside and upside risks to provide a more complete picture of what could happen over the forecast period.

Upside risks

- Reduction in trade tensions: trade tensions could partially subside and diminish over time, leading to a recovery in trade and supporting the economies of Italy and its main trading partners;
- Labor market: lower wage pressure on prices could reduce the risk of persistent inflation;
- Monetary policy: an acceleration of monetary policy easing by the European Central Bank could support growth in the euro area countries;
- Readjustment of supply chains: a faster readjustment of value chains at European and global level would lead to less pressure along these chains, bringing with it greater security of supply of raw materials and world trade;
- Acceleration of foreign demand: stronger economic growth for key trading partners such as China, Germany, and the United States, thanks in part to the end of uncertainty over trade policies, would translate into a greater contribution from foreign trade to Italian growth;

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

Downside risks

- Increased geopolitical tensions: the conflicts currently underway may not be resolved in the short/medium term, adding uncertainty to an already precarious global context. This could be compounded by worsening tensions in the Middle East. If other countries become involved, there would be even more significant humanitarian and economic repercussions, with potential negative consequences for the prices of energy (mainly oil) and other commodities;
- 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;[71]
- 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.

[71] 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[72]

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). [73]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.

[72]The model was created in collaboration with the Department of Economics of the University of Bologna.
[73]"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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