

The economy



There are favourable signs emerging for the global economy but there is still a lot of uncertainty. Growth accelerated in the United States, remained weak in Japan, slowed down in China and other emerging economies; the situation in Russia was worrisome.

It is true that the fall in oil prices, the monetary expansion measures of the European Central Bank, the fall in interest rates and the exchange rate depreciation of the euro are all factors that will stimulate global demand in 2015. After years of crisis and a disappointing 2014 in terms of growth, economists expect an improvement in macroeconomic conditions in the eurozone and especially in Italy.

In 2014, the world economy grew at a rate of about 3%; the European Union closed the year with a +1.3% of the GDP for the EU28 and +0.9% for the eurozone.

In 2014, Italy registered a GDP of EUR 1,616,254,000 in current terms, with a 0.4% reduction in real terms over the previous year. The real GDP fell below the level recorded in 2000. In early 2015, growth remained moderate, and insufficient for now to be able to determine appreciable improvements in the labour market; a timid recovery estimated at +0.7% is expected during 2015, and around 1.6% growth in 2016.

Veneto in 2014 maintained pretty much the same GDP values as the previous year; there was a +0.1%, which means a better situation than for the whole country. Domestic demand was still weak; household consumption stabilised at low values and investment was reduced by 1.8%.

Veneto's quality specialisation and strong flexibility, which the economy of this region has always shown in the past, are characteristics conducive to grasping the elements of recovery: the fall in oil prices favouring Venetos' manufacturing industry, the exchange rate supporting the sale of products abroad and the ECB policies facilitating investment. 2015 estimates assume increased wealth by 1.1%, and a +1.7% consolidation is expected for 2016.



Will the new energies drive the recovery?





1. Will the new energies drive the recovery?¹

1.1 The global scenario

One of the main elements of discontinuity in the international economic scenario that emerged in the final stages of 2014 was the fall in oil prices. The extent of the contraction was significant, given that we went from a period of stable fall resembles the great turning points of the oil market in the past. For a discussion on international energy scenarios, see chapter 4 of this report.

Fig. 1.1.1 - Brent Crude Price (\$/barrel) - Years 1987-2015



Source: Processing by Veneto Region - Regional Statistical System Section on EIA - U.S. Energy Information Administration data

Major effects on the global macroeconomic environment have usually followed a correction of this size, although the intensity of the effects diminished in the most recent phase compared to the seventies, due to the lower energy intensity of production in advanced economies, especially after the outsourcing of economic activities .

Over the last 10 years, the price of Brent Crude reached a peak in summer 2008, then it dropped because of the financial crisis and the sharp de-

The collapse of oil prices...

cline in industrial activity worldwide, reaching a low point at the end of 2008. The following comeback led to a historic high in 2011, with subsequent substantial stability until summer 2014. The causes of the collapse in 2014 can be identified in both demand and supply factors, and not just economic ones. Economic elements related to demand can be identified in the weakness of commodity markets due to the slowdown in international manufacturing and, in particular, the slowdown in emerging economies. But there were also non-economic factors, such as the growing introduction of energy saving innovations, for example in the construction and transport industries, and the numerous investments in renewable energy sources made in recent years. However, these investments were urged by high oil prices, besides environmental reasons.

On the supply side, we have witnessed an increase in

...can change the competitive position of the various economies

oil production in recent years, especially in non-OPEC countries, and especially in the United States, mainly thanks to

the new technologies, which enabled the exploitation of shale oil and shale gas reserves. In recent months, a phase of steady demand and rising supply has led to an excess in the world stocks of crude oil and a consequent reduction in prices. This may have important redistributive effects between oil producing and consuming countries. The International Monetary Fund estimated that a 10% decrease in oil prices corresponds to a 0.2% global GDP increase.

Consuming countries are naturally the biggest beneficiaries of this increase, with consequent losses for oil producing countries. The increased real disposable income of oil importing countries could generate a response in terms of higher consumption, with multiplier effects induced on domestic demand.

World growth was moderate

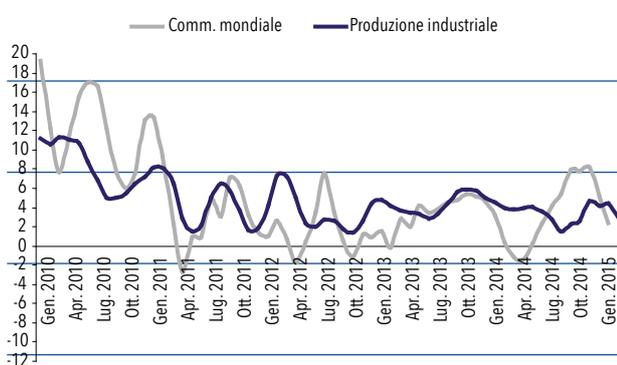
In 2014, the world economy grew at a rate of about 3%, a relatively moderate pace, both because emerging economies have been keeping growth lower compared to the sustained expansion of the 2000s and because, among the advanced economies, the eurozone did not confirm the signs of a full recovery of the cycle emerged earlier this year. The positive effects of falling oil prices are cancelled, for now, by the weakness of investments and the feeble outlook

¹ Ludwig Feuerbach, The Mystery of Sacrifice, or Man is what he eats, 1862
² Congiuntura REF - January 2015



for China, Russia, Japan and the eurozone. The only major economy that accelerated its activity was the United States. In the past few years, the unexciting growth rates of the international economy have been matched by the low elasticity of world trade growth. World trade registered a sharp slowdown in the first half of 2014 and then a recovery in the second half. In the first half, we saw the deceleration of imports from emerging countries, whose exchange rates depreciated since the end of 2013, as well as the fall in imports from Russia. In the second half, demand went back up, especially from Asian economies, and US imports accelerated, while the imports of Eastern Europe remained stagnant and those of the eurozone were very weak. In general, the picture of the world economy described by the International Monetary Fund (IMF) is still showing growth for 2015, albeit with some signs of deceleration.

Fig. 1.1.2 - Percentage changes in global trade of goods and services and industrial production worldwide - Jan. 2010-Feb. 2015



Source: Processing by Veneto Region - Regional Statistical System Section on International Monetary Fund data

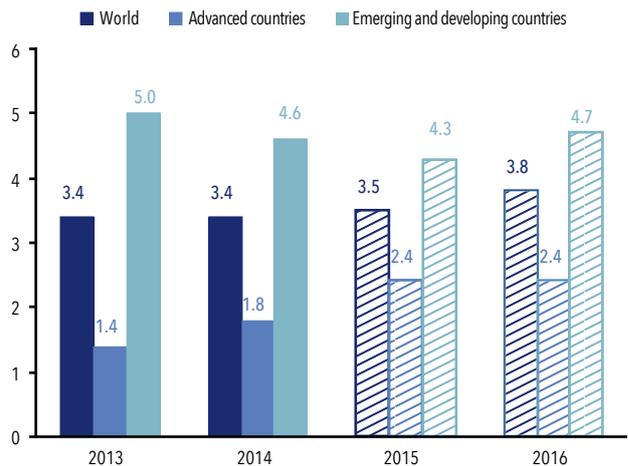
The Gross Domestic Product of the United States grew by 2.4% in 2014, a performance that exceeded the expectations of analysts, better than the 2.2% average of the post recession years, although far from the changes in excess of 3% of the Nineties. Domestic demand increased by 2.5%, business investment soared and there was a real estate comeback. The recovery seems assured by consumption aided by falling oil prices and continuing improvements in the labour market.

The United States are driving the new cycle

Japan out of recession

Japan came out of recession, but at a lower rate than expected, highlighting the continuing difficulties of Abenomics in reviving the world's third world economy.

Fig. 1.1.3 - Annual percentage changes in GDP. World, Advanced countries, Emerging and developing countries - Years 2013-2016



advanced countries, emerging and developing countries - Years 2013-2016

Source: Processing by Veneto Region - Regional Statistical System Section on International Monetary Fund data and forecasts

The real gross domestic product decreased by 0.1% in 2014 compared to the previous year. The country is recovering from two consecutive quarters of contraction, attributed mainly to the consumption tax increase from 5% to 8% that became effective on April 1 last year, an event that had depressed consumption and induced consumers to move many durable expenses up to the first quarter of the year. The goal of the Chinese government for 2015 is a "new normal" economy, with lower growth, estimated at 7% in 2015. The golden days are gone forever; GDP growth in 2014 was 7.4%, the worst ever in 24 years.

China towards a "new normal" economy

But China, as stated in the 32-page speech of the Prime Minister at the opening of the annual session of the Chinese parliament for 2015, "must maintain an appropriate balance between ensuring steady growth and structural adjustments". It looks like there is a real change of pace from an export-oriented and labour-intensive production model to one based on domestic consumption and

³ Opening speech of the annual session of the Parliament for 2015 by Chinese Premier Li Keqiang

⁴ The reference year was moved from 2004/05 to 2011/2012 and the GDP at factor cost calculation was abandoned to adopt the one at market prices, the method of the International Monetary Fund



Tab. 1.1.1 - Economic indicators in the major industrialized countries - Years 2013-2016

	GDP (% Var.)				Internal demand (% Var.)				Inflation				Unemployment rate			
	2013	2014	2015	2016	2013	2014	2015	2016	2013	2014	2015	2016	2013	2014	2015	2016
United States	2.2	2.4	2.8	2.7	1.9	2.5	2.9	2.6	1.5	1.6	1.1	1.8	7.4	6.2	5.2	4.8
Japan	1.6	-0.1	1.3	1.0	1.9	-0.2	0.6	1.2	0.4	2.7	0.1	0.6	4.0	3.6	3.2	3.3
Eurozone	-0.5	0.9	1.4	1.6	-0.8	0.9	1.3	1.5	1.4	0.4	0.1	1.4	11.9	11.5	11.1	10.7
U.K	1.7	2.8	2.5	1.9	1.9	3.3	2.9	1.8	2.6	1.5	-0.1	1.3	7.6	6.1	4.9	4.7
UE28	0.0	1.3	1.7	1.7	-0.3	1.5	1.7	1.6	1.5	0.6	0.1	1.3	10.8	10.2	-	-

Source: Processing by Veneto Region - Regional Statistical System Section on International Monetary Fund, data and forecasts, marked in red

quality production. India's growth rates seem to overtake China's.

The Indian Government unveiled the new forecasts for the tax year closing in March 2015, predicting an acceleration of 7.4%.

In 2013/14, GDP growth was adjusted from 4.7% to 6.9%, the year before from 4.5% to 5.1%. As a matter of fact, it seems that merit should be attributed to the statistics that changed the GDP detection method rather than to the economic policies set in place by the government.

India running, Brazil slowing down

Brazil moved away from the prospect of an economic recovery. GDP growth in 2014 was 0.1%;

-1% is estimated for 2015 with inflation still high. The economic slowdown was confirmed to be longer than expected, as the country faced a serious crisis of confidence due to the discovery of a complex and widespread system of bribes and various episodes of corruption.

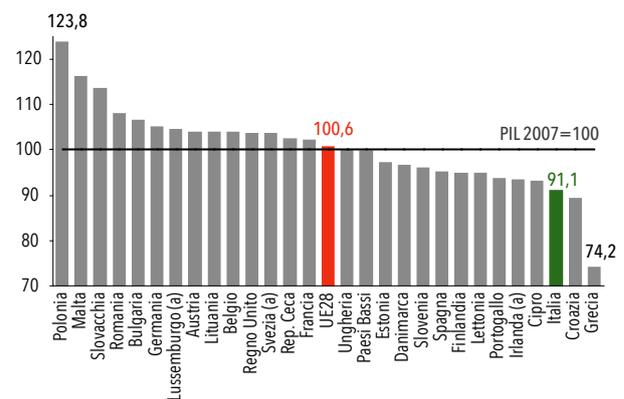
1.2 Europe

The GDP of the EU28 closed 2014 at 1.3%. Economic growth in the eurozone remained modest; over the quarters of 2014, growth was always slightly above zero, determining a + 0.9% for the entire 2014. For most European countries, what has been lost starting from 2007 has not been recovered yet.

The explanation for the worsening cycle occurred in the middle quarters of the year is to be found at least in part in the effects of the shock caused by the collapse of trade with Russia due to the embargo following

the crisis in Ukraine. In addition, the downward trend in inflation led to tighter financial conditions in the eurozone. From the point of view of the trends of the various eurozone economies, 2014 saw a return to growth by the peripheral countries, except for Italy, Greece included. France, Finland, Austria and the Netherlands performed lower than expected. The economies of the German area seem to have been greatly affected by their extensive exposure to trade with Russia. This also played a role in causing unfavourable trends in Italian industry.

Fig. 1.2.1 - Gross Domestic Product for some European countries (2007=100, concatenated values for year 2010) - Year 2014



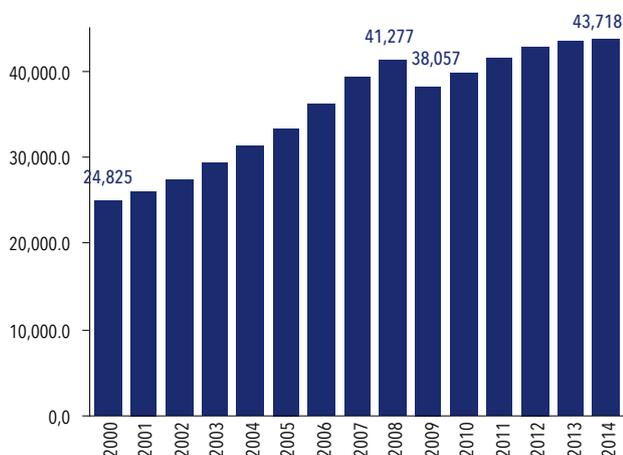
(a) Year 2013 data Source: Processing by Veneto Region - Regional Statistical System Section on Eurostat data



The Russia-Ukraine crisis had negative effects on all of Europe

Western sanctions and the collapse in oil prices significantly weakened the Russian economy, condemning it to stagnation. Even President Putin admitted that it will take two years to lead the country out of this difficult stage. GDP growth never reached 1% during 2014. The recession is now taken for granted, except for improbable and sudden rebounds of oil prices or an easing of international sanctions, of which there is no sign.

Fig. 1.2.2 - Russia's gross domestic product (billion rubles at constant prices) - Years 2000-2014



Source: Processing by Veneto Region - Regional Statistical System Section on International Monetary Fund data

Spain and Portugal were less affected by the Russian crisis. Together with Ireland, they showed signs of overcoming the recession. Also the Greek economy went back to recording an increase in GDP in 2014, but after such a deep fall in previous years, it was not perceived by the population. The new government is taking note of the challenges involved in supporting a debt of considerable size with difficult social and economic conditions and modest prospects for future growth. The conditions of the European labour market are made difficult by the weak macroeconomic environment.

High rates of unemployment in Europe

The unemployment rate remained high, even though some peripheral countries

started recording an initial turnaround in this case too. These levels of unemployment and large spaces of unused productive capacity pose the risk of a deflationary spiral. These risks explain the turning point in ECB policies.

Just anticipating the start of the new monetary policy phase was enough for markets to start benefiting from it. The result was a recovery of the stock markets, a drop in interest rates and a period of depreciation of the euro exchange rate. Therefore the prospects for 2015 are more optimistic; the EU's GDP should increase by 1.7% in both 2015 and 2016. The outlook is slightly less optimistic for the eurozone (+1.4% in 2015 and +1.6% in 2016). A slight reduction in the percentage of the unemployed is expected for 2016,

down to about 10.7% in the eurozone.

The Juncker Plan will help investments

At the end of 2014, the new president of the European Commission, Jean-Claude Juncker, introduced to the European Parliament a plan to boost economic growth and make new investments without generating debt. It is a final € 315 billion plan but with an initial capital of 21 billion, of which only 13 are actual, for now. It will fill the void of investments inherited from the years of crisis. The plan includes the creation of a new European fund for strategic investments (EFSI) and the involvement of the European Investment Bank (EIB), an institution that the EU has used to finance long-term projects for the past 50 years or so. The EIB will use these 21 billion to issue bonds and raise funds on the market for a total of 60 billion, with which to start funding projects. From there on out, a multiplier effect will be expected along with the arrival of new "external" investments. In short, with these initial 21 billion set as guarantee, the goal is to create loans and then investments for at least € 315 billion between 2015 and 2017, through a leverage effect. Practically, the fund will take up the most important part of the risk, that is, by being responsible for the guarantee and agreeing to be paid after other creditors. This would facilitate the participation of private investors. Individual states will still be able to contribute their own resources. In fact, many European states, if not all, have no means to take on new investments and loans, which are considered crucial for the European economy to restart in a definitive manner. Trying to attract capital in these conditions would not be easy and would require too much time.

⁵ Alberto Quadrio Curzio - Sole 24 Ore - L'effetto Qe sull'economia e il rischio dei cambi [The Qe effect on the economy and the exchange risk], March 17, 2015
⁶ The European System of Accounts (ESA) is the frame of reference for measuring the economic and financial activity of an economic system, as well as its components and the relationships established between them in a given period of time.
⁷ Net indebtedness: the balance of the state budget, equal to the difference between the total of all revenue and the total of all expenses, both current and capital, excluding financial transactions (granting and repaying loans, granting and collecting credit, etc.).



Tab. 1.2.1 - Economic indicators in the major eurozone countries - Years 2013-2016

	GDP (% Var.)				Internal demand (% Var.)				Inflation				Unemployment rate			
	2013	2014	2015	2016	2013	2014	2015	2016	2013	2014	2015	2016	2013	2014	2015	2016
Germania	0,1	1,6	2,0	1,7	0,7	1,2	1,7	1,5	1,6	0,8	0,3	1,6	5,2	5,0	4,6	4,4
Francia	0,3	0,4	0,9	1,5	0,3	0,7	0,9	1,5	1,0	0,6	0,2	1,2	9,9	9,9	10,5	10,2
Spagna	-1,2	1,4	2,5	2,2	-2,6	2,1	2,4	2,1	1,5	-0,2	-0,3	1,4	26,1	24,5	22,3	21,2
Italia	-1,7	-0,4	0,7	1,6	-2,5	-0,6	0,3	1,3	1,2	0,2	0,0	1,3	12,2	12,7	12,7	12,1

Source: Processing by Veneto Region - Regional Statistical System Section on Istat, Eurostat and Prometeia data and forecasts, marked in red

According to Juncker, this plan could have the first loans allocated half way through 2015.

Quantitative easing will stimulate the economy

Quantitative easing (QE) is a manoeuvre that has the European Central Bank purchase bonds (government bonds, but not only) from various banks, which would have new money in return; a manoeuvre aimed at introducing new money in the European economy, encouraging businesses loans and getting inflation to grow. Deflation is very risky because it triggers a vicious circle that hurts the economy; consumers and companies defer purchases that are not strictly necessary, waiting for further falls, so demand remains weak and producers of goods and services further reduce prices.

Revenues are lower and companies need to reduce costs, often starting with their staff, and there is no investment. There is general agreement among economists that one of the most effective ways to get out of deflation is resorting to quantitative easing. QE is not a world first; Japanese premier Shinzo Abe has already implemented it, precisely to break the deflationary spiral that enveloped his country in recent years. And the Federal Reserve, the US central bank, implemented QE policies that, according to several observers, contributed to the recovery of the US economy recorded in recent months. The ultimate goal is therefore to make money "cheaper"; European governments could then afford to spend more to encourage and stimulate employment and consumption, as well as to invest in new infrastructure, from roads to railways and telecommunications. Another consequence could be a gradual depreciation of the euro, which, on the one hand would increase the level

of exports, but on the other would lead to the loss of purchasing power, especially with respect to oil, priced in dollars.

There was a strong depreciation of the euro against the dollar

The euro-dollar exchange, which in 2014, until May, was around 1.40, fell to 1.08 in March 2015, a decrease of 16% in the last six months and 5% in the last month. The euro had peaked against the dollar in July 2008 with \$ 1.58 per euro and hit a minimum in October 2000, with 0.85, but basically the average since the introduction of the single currency is \$ 1.29 for 1 euro.

The depreciation of the euro is certainly positive for a number of factors: the boost to European exports, especially Italian ones, the attraction of tourism and the increase of foreign direct investment into the eurozone with purchasing of companies, real estate and on the financial market, which would strengthen all of the real economy. Negative effects do not seem to be looming for the import of raw materials expressed in dollars and in particular energy sources, given the current depressed prices. However, there may also be adverse effects, including a massive outflow of cash to the dollar, both because today the ten-year US government bond yields 2.4% versus near zero rates for German bonds and very low rates for Italian bonds, and because there is fear of a further depreciation of the euro. Uncertainties and fluctuations in foreign exchange disturb industrial and commercial operators as well. The greatest danger, however, is the start of a guerrilla with competitive devaluations or protectionist measures that would have very serious effects. The larger question concerns China's position, which, by governing the dollar-yuan exchange rate,

⁸ Public debt: the debt of the state in relation to other entities, private individuals, companies, banks or foreign entities, which subscribed to bonds (such as, in Italy, BOT and CCT) to cover the financing needs of the state or any public shortfall.

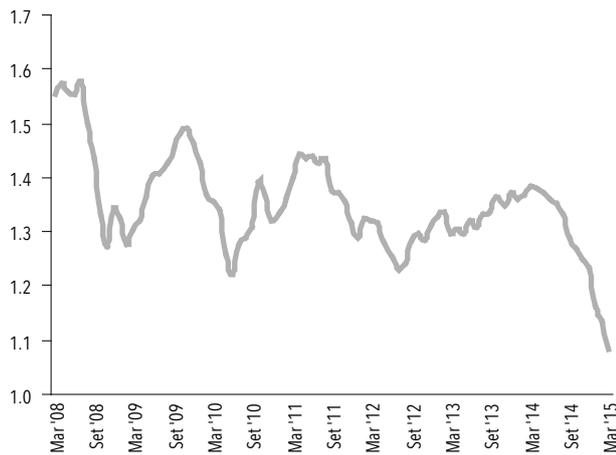
⁹ Tax on corporate income.

¹⁰ L.D. 185 of 2008 Art. 15 "realignment and voluntary revaluation of book values" and Law no. 228 of 24/12/2012, Stability Law for 2013.11 Congiuntura REF - Gennaio 2015.



followed much of its revaluation against both the euro and the yen. With the start of Abenomics, there has been a close to 40% depreciation of the yen against the dollar since 2013.

Fig. 1.2.3 - Dollar-euro exchange rates - Mar. 2008-Mar. 2015



Source: Processing by Veneto Region - Regional Statistical System Section on Bank of Italy data

The flexibility of the Stability and Growth Pact

The accounting transition to ESA 2010, now available for all countries, resulted in a 0.1% reduction of the deficit/GDP ratio of the eurozone. As of 2014, the net indebtedness amounted to 2.4% of the GDP, an improvement compared to 2013 due to the reduction in interest payments and a more favourable trend of revenue over expenses. Public debt was 91.9%, an increase compared to 2013. At the end of 2014, the European Commission introduced some guidelines for the application of the Stability and Growth Pact, which formalise the conditions to be able to enjoy its flexibility margins. The fiscal adjustment required of member countries will vary depending on the economic cycle and the level of debt. The goal is to encourage structural reforms and public investment, and therefore the recovery of the eurozone, in line with the objectives of the Juncker plan.

1.3 Italy

Italy's 2014 GDP was EUR 1,616,254,000 in current terms, with a 0.4% reduction in real terms over the previous year. The real GDP fell below the level recorded in 2000. There was a 3.3% contraction in gross fixed investment, while domestic final consumption registered a zero variation. The contribution of domestic demand to GDP growth was negative by 0.6 points and that of changes in inventories by 0.2 points, while net foreign demand provided a positive contribution. In 2014, the final consumption expenditure of households grew in real terms by 0.3%, marking a slight recovery compared to the accentuated decline of 2013 (-2.9%).

Tentative signs of recovery in domestic demand

Goods consumption expenditure remained unchanged, while the expenditure for services increased by 0.7%. In terms of consumption functions, the highest increases involved spending on alcoholic beverages and tobacco, 2.3%, health services, 2.0%, and recreation and culture, 1.9%; the only component marking a decrease was shopping for home furniture, appliances and maintenance, down 1.5%. Spending by public administrations and private social Institutions (ISPs) recorded respectively 1% and 0.3% decreases.

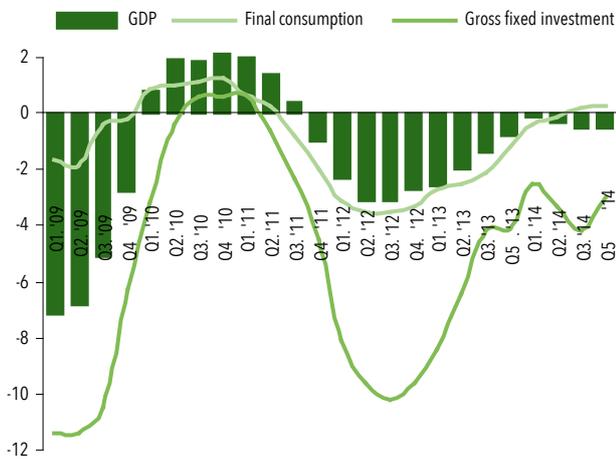
Investments still down

The contraction in gross fixed investment, 3.3%, was lower intensity than in 2013 (-5.8%). The biggest drop concerned the construction component, down 4.9%, while investment in machinery and equipment fell by 2.7% and in transport by 1.1%; the intellectual property products component registered instead a slight increase of + 0.3%. Exports of goods increased by 2.6%, while imports declined 1.8%.

The total added value decreased by 0.4% in 2014; a slightly better situation than in 2013, when it recorded a drop of 1.4%. All sectors marked negative changes; the decline was more pronounced in construction, 3.8%, and in agriculture, 2.2%, while it was lower in industry excluding construction, -1.1%. Overall, the service industry had a slight +0.1% increase. The Italian economy showed weak signs of recovery in the



Fig. 1.3.1 - Percentage changes of GDP, final consumption and investments on the respective period of the previous year. Italy - Q1 2009-Q2 2014



Source: Processing by Veneto Region - Regional Statistical System Section on Istat data

last months of 2014; short-term growth prospects still largely depend on foreign demand and the intensity of the relationships that bind the export sector to the national production chains. It is also true that Italy is among the countries that benefit the most from the fall in oil prices and the reduction in spreads. At the beginning of 2015, growth remained moderate and currently insufficient to determine appreciable improvements in the labor market; during 2015, a still timid recovery estimated at + 0.7% is expected, and around 1.6% growth in 2016.

Public finances

The net debt of the public administrations in relation to the GDP was 3.0% in 2014, compared to 2.9% in the previous year. In absolute terms, the debt is -49,056 billion euro, an increase of 1.6 billion compared to the previous year. The primary balance (debt net of interest payments) was positive and amounted to 26,126 billion euro, a 1.6 percentage of the GDP (in 2013, it was 1.9). The current account balance (savings or deficit of the public administrations) is positive and equal to 2,370 million euro, compared to 1,204 million in 2013. This improvement is the result of a 6.7 billion euro increase in current revenue and about 5.5 billion in current expenditure. In 2014, the total revenue of the public administrations increased by 0.6% over the

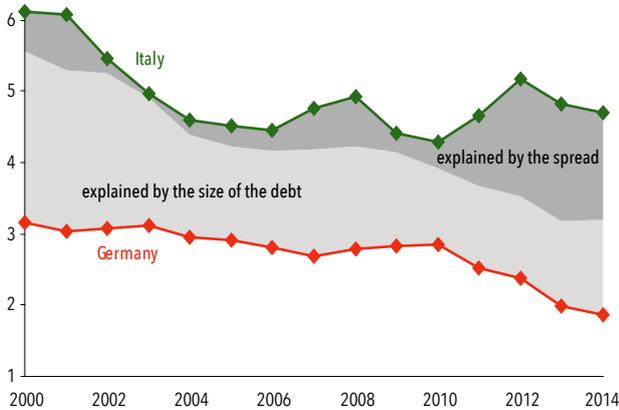
previous year (+ 0.1% in 2013). As a percentage of the GDP, it was 48.1%. Current revenues recorded a 0.9% increase, resulting in 47.6% of the GDP. More specifically, indirect taxes increased by 3.5%, mainly reflecting the VAT revenue increase and the introduction of the Tax on Indivisible Services (TASI). Direct taxes were down 1.4%, due to the sharp reduction of the IRES, partially offset by moderate growth in substitute taxes. Actual social security contributions marked a slight increase (+ 0.5%) compared to 2013. The sharp fall in capital revenue (-21.3%) was mainly due to the reduction of capital taxes, due to the disappearance of the one-off substitute tax payment on the realignment of book values according to the international principles of the IAS. The overall tax burden (amount of direct, indirect and capital taxes, and social contributions in relation to the GDP) stood at 43.4%, exactly the same as in 2013.

In 2014, the total expenditure of the public administrations grew by 0.8% compared to 2013. In relation to the GDP, they amounted to 51.1%, with current expenditure growing 0.7%. Specifically, intermediate consumption increased by 0.5%, while employees compensation decreased by 0.6% (-0.7% in 2013), due to the reduction of the work units of the public administrations and the continued blocking of contract renewals. Social benefits in cash increased by 2.7% (+ 2.6% in 2013), due to a limited increase in pension benefits and a substantial increase in social assistance benefits, in large part determined by the dispensing of the Bonus established by art. 1 of L.D. 66/2014, converted into Law no. 89/2014 (80 Euro Bonus). Interest expense decreased by 3.5% after a reduction of 7.3% in 2013. The strong increase in other capital expenses in 2014 was due to the recognition of certain refundable tax credits, recorded for the full amount in the year when they were generated.

The recent reduction of the spread, which is the cost of debt, should be of benefit to the Italian budget. In fact, an analysis conducted by the REF Ricerche research center shows that if you compare the level of interest payments on the GDP in Italy and Germany, there is a difference of almost 3% of the GDP; if Italy spent as much as Germany on interest, our budget balance would break even.



Fig. 1.3.2 - Interest expense as % of GDP: comparison between Italy and Germany - Years 2000-2014



Source: Processing by Veneto Region - Regional Statistical System Section on Congiuntura REF data

The difference in interest payments depends on two factors: the first is a higher ratio of public debt compared to the GDP in Italy than in Germany; the second is due to the higher cost of Italian debt. The spread had reached minimum levels before the crisis, about two tenths of the GDP, and then increased to a level of almost 1.5%. Practically, the spread costs us over \$ 20 billion more in spending annually. Its reduction would thus have a significant effect on the evolution of Italian public finances.

Fig. 1.3.3 - Spread: difference between Italian BTPs and German Bunds (x 100) - Jan 2011-Mar 2015

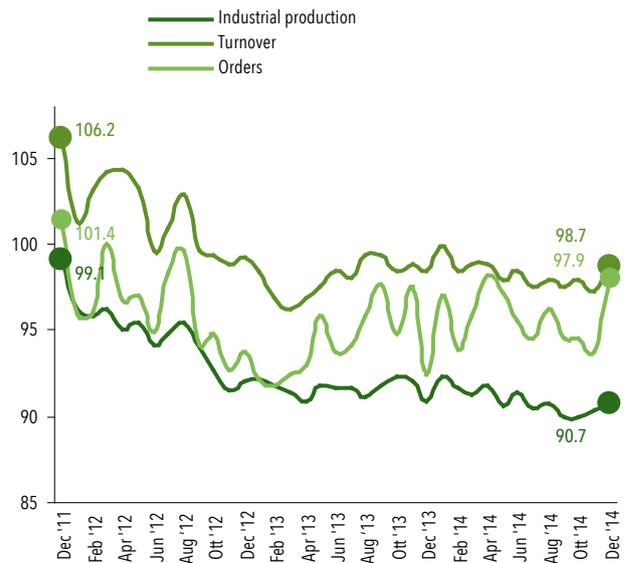


Source: Processing by Veneto Region - Regional Statistical System Section on Eurostat data

Industrial activity

The industrial production index in the whole of 2014 fell by 0.8 percentage points compared to 2013. Industrial activity has fallen continuously since the end of 2011; from September 2011 until now, the index has shown values below 100, which is lower than in 2010, reaching values around 90 in 2014. The good news is that in recent months the index has not retreated and has been supported by the positive sign of the orders index trend, up 1.2%, and of the industry revenue index, up 0.2% compared to 2013. Both orders and sales grew due to the increase of the foreign component. The main support for manufacturing came from the sectors of capital goods and consumer durables, compared to a decline in the energy sector.

Fig. 1.3.4 - Seasonally adjusted indices of industrial production, turnover and orders (base year 2010=100). Italy - Dec 2011-Dec 2014



Source: Processing by Veneto Region - Regional Statistical System Section on Istat data

In recent times, the confidence indicators of households and firms have taken on an increasing role in the analysis of the economic situation, thanks to the speed with which they are disclosed and, in some cases, for their leading properties in the economic cycle.

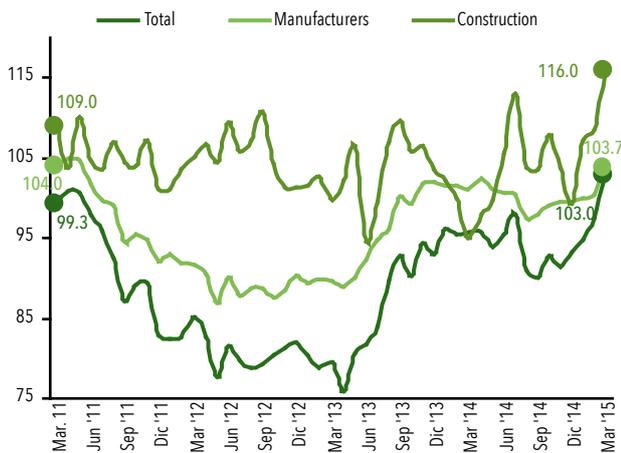
Italy's confidence climate improved

¹³ Source: 'Veneto Lavoro' for the period 2006-2013. Employment measured in standard work units.
¹⁴ Calculated in 2005 euro, to make an assessment of the historical trend while purifying it from the effect of inflation.
¹⁵ It represents the amount of current resources of operators intended for final use (consumption and savings).
¹⁶ Work units were used to standardize investments. A work unit is the amount of work done in a year by a full-time employee, or the equivalent amount of work provided by part-time workers or workers who have two jobs.
¹⁷ Added value/work units



Qualitative indicators anticipate an expansion of industrial production; business confidence increased in 2014 over the previous year, had a fall in August, but then recovered and in early 2015 stood on the levels

Fig. 1.3.5 - Monthly balance of business confidence climate; total, manufacturing and construction (seasonally adjusted data, 2010=100). Italy - Mar 2011-Mar 2015



Source: Processing by Veneto Region - Regional Statistical System Section on Istat data

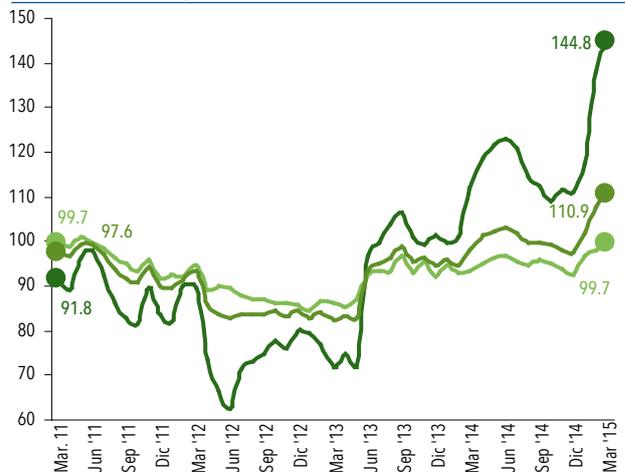
Fig. 1.3.6 - Monthly balance of business confidence climate for market services and retail trade (seasonally adjusted data, 2010=100). Italy - Mar 2011-Mar 2015



Source: Processing by Veneto Region - Regional Statistical System Section on Istat data

observed in 2010. The composite business confidence climate index, which incorporates the opinion of entrepreneurs from all sectors, improved thanks to the optimism of manufacturing, services and trade and finally also the building sector. Order evaluations and production waiting time improved for manufacturing companies. In construction, order evaluations and/or construction plans improved, as well employment expectations, albeit slightly. As for service companies, evaluations and production waiting time improved as well as expectations for the economy in general. In retail, evaluations on current sales worsened, while expectations on future sales improved. The climate of opinion of households is also turning progressively optimistic; in the first part of the year, confidence remained high, falling in the last months of 2014, but recovered strongly in the first months of 2015, while maintaining a high value.

Fig. 1.3.7 - Monthly balance of consumer confidence climate (seasonally adjusted data, 2010=100). Italy - Mar 2011-Mar 2015



Source: Processing by Veneto Region - Regional Statistical System Section on Istat data

Government targets for 2015

On 10 April 2015, the Council of Ministers approved the Economic and Financial Document (DEF), which updates the policy framework on which executive actions are based. The fiscal stance of the DEF for 2015 is summarized in the following points: support the economic recovery, avoiding tax burden increases



and boosting investment; set the public debt to GDP ratio on a path of reduction, thus boosting market confidence; and strengthen the recovery phase of the economy, which will lead to a strong employment recovery in the next three years. The basic economic strategy outlines seek recovery of productivity by enhancing human capital, reducing business costs due to the complication and inefficiency of the public administration, simplifying the administration's bureaucracy and enforcing its transparency and, finally, eliminating uncertainty in the legal frameworks of certain sectors, from the point of views of both general discipline and the instruments that ensure their effectiveness. The complete implementation of the education system reform (The Good School) has been planned in support of these priorities so as to increase significantly the quality of the country's human capital. This reform provides for merit to have a greater role in determining teacher promotions, greater transparency in the management of schools and the introduction of tax incentives for private investment in school infrastructure and courses offered.

The complete implementation of the labor market reform (Jobs Act) has also been planned, with four implementation decrees already approved. The goal is to make it more advantageous not only to hire new staff, but also to stabilize existing flexible labor relations, so as to encourage investment in education for workers and training for businesses. The will to boost investment was confirmed, so the economic recovery may consolidate and productivity may accelerate. The European Fund for Strategic Investments (EFSI) will guarantee and finance projects in infrastructure, energy, education, research, protection of natural resources, innovation and SMEs, both with debt instruments and capital investment. Next to this opportunity is also the Compact Investment package, whose implementation will support businesses in temporary difficulties, increase funding possibilities for the internationalization of enterprises, increase benefits for start-ups, increase tax breaks for research and development and patents, etc.

All these actions will be accompanied by a series of constitutional and public administration reforms, which will help to streamline and speed up the mechanisms of government, as well as to make some cuts in public spending. DEF measures do not provide for linear cuts or increasing the tax burden, but a review of public expenditure in the order of 10 billion

euro, in order to recover efficiency in Public Administration action and to reallocate and limit such action according to an organic vision, so as to avoid a VAT increase. The rationalization of subsidiaries was planned for this purpose, along with the strengthening of the system of needs and standard costs for local authorities, the publication of performance and cost data of individual administrations, the review of the businesses incentives system and, finally, the full implementation of the fiscal mandate, with particular attention to the creation of a traceability system for electronic business transactions.

Resources will also be recovered thanks to the return of capital from abroad (voluntary disclosure) and the introduction of a new cooperation model between tax authorities and taxpayers, the so-called "tax interview." The new cooperation, involving the dispatch of notices to taxpayers with the information available to the tax authorities, resulting from the intersection of the income and expenses record and VAT returns, should stimulate spontaneous compliance, leading to a financial impact estimated as EUR 908 million for 2016 (EUR 700 million for 2015). The desire to rationalize municipal taxes has also been confirmed, by replacing IMU and TASI with a single Local Tax. The document also shows an endowment of 1.5 billion euro - known as "tesoretto" - available to the Government for the current year, the result of the positive update of the macroeconomic data with respect to previous forecasts.

With the implementation of the aforementioned structural reforms, the government estimates a growth of 0.7% in 2015; faster growth is expected in the following years, with the GDP increasing by 1.4% in 2016 and 1.5% in 2017. The nominal deficit will fall to 2.6% of the GDP in 2015, and 1.8% and 0.8% respectively in the two following years. The structural budget balance has been confirmed for 2017, while the resetting of the nominal deficit-GDP ratio will occur in 2018.

1.4 The Veneto economy

The official regional accounting data stop at the year 2013, therefore we will refer to Prometeia Research Institute estimates and forecasts for our 2014 analysis. In 2014, Veneto's GDP stayed on the levels of the pre-



vious year; there was a +0.1%, thus a better situation than on the national scene.

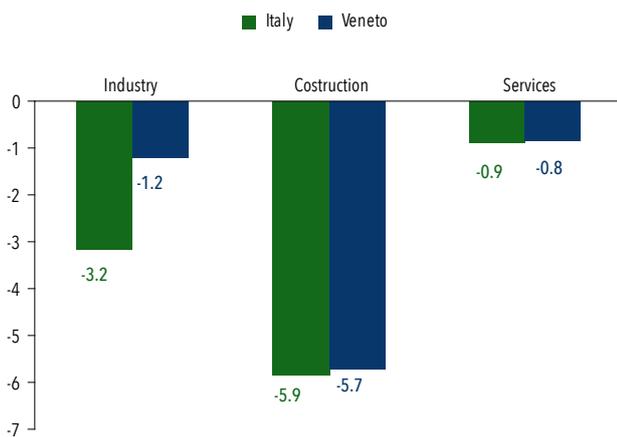
Domestic demand was still weak; household consumption stabilized at low values and investment was reduced by 1.8%. The result of 2014 is attributable mainly to the added value from services holding up, +0.3%, and the stability of industry excluding construction, down 0.1%, which partially offset construction sector losses, -1.9%.

Some positive signs at the end of 2014...

In the estimates for 2015, the recession seems to fade because, in Veneto, and the whole country, the last months of the year gave encouraging signs.

Veneto's quality specialization and strong flexibility, which the economy of this region has always shown in the past, are characteristics conducive to grasping the elements of recovery: the fall in oil prices favoring Veneto's manufacturing industry, the exchange rate supporting the sale of products abroad and the ECB policies facilitating investment. In light of these elements, a 1.1% GDP growth is conservatively estimated, with positive contributions from sales abroad and domestic consumption, as household spending is expected to grow 1.7%.

Fig. 1.4.1 - Change of added value for 2014/13 by economic activity sector. Veneto and Italy

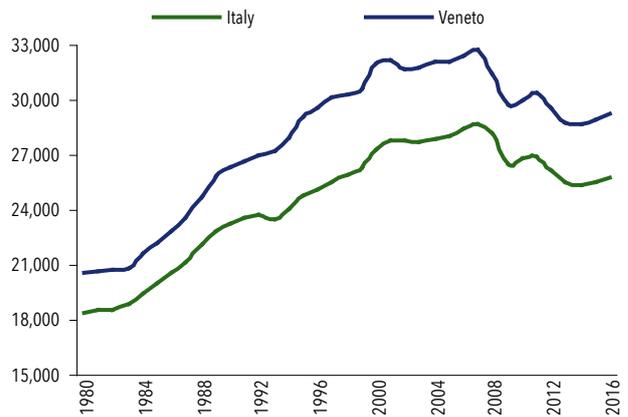


Source: Processing by Veneto Region - Regional Statistical System Section on Istat data and Prometeia estimates

The added value of the tertiary sector and industry in the strict sense should give a 1.1% boost to the growth of each, and construction is expected to slow

its fall (-0.6%). An overall consolidation amounting to + 1.7% is expected for 2016.

Fig. 1.4.2 - Gross domestic product per capita (euro, year 2010). Veneto and Italy - Years 1980-2016



Source: Processing by Veneto Region - Regional Statistical System Section on Istat data and Prometeia estimates

Despite the economic difficulties, Veneto was still Italy's third wealth producing region, after Lombardy and Lazio; 9.1% of the national GDP was produced in Veneto. In 2013, the GDP per Veneto inhabitant was € 30,030, up 12.5% compared to the national level. From the point of view of the labor market, Veneto recorded a 63.7% employment value, and a 7.5% unemployment rate, once again among the leading regions with the sixth highest employment rate and the second lowest unemployment rate.

Indicators over time

Over the past 25 years, Italy has suffered three major recessions: in 1992-93 and then again in 2007-08 and 2010-11, the last two considered as one single phase by some economists. The one in 1992-93 reduced the GDP only by 0.9% over a year and a half, but cost Italy about 1 million jobs. Veneto took advantage of that lira currency crisis time by selling large quantities of goods abroad, which led to a 1.4% GDP increase. The other two recessions were triggered by the large global financial crisis of 2007 and the European sovereign debt crisis of 2010, and cost Italy the loss of more than 9 GDP points and a million jobs over seven years. The recession of 2007-2014 caused a sharp reduction of Veneto's GDP: -9.5%, amounting to almost 15 billion



Tab. 1.4.1 - Macroeconomic picture (percentage changes on linked values with 2010 as reference year). Veneto and Italy - Years 2012-2015

	2012		2013		2014		2015	
	Italy	Veneto	Italy	Veneto	Italy	Veneto	Italy	Veneto
Gross domestic product	-2.8	-2.5	-1.7	-2.5	-0.4	0.1	0.7	1.1
Final consumption expenditure of households	-3.9	-3.9	-2.9	-3.3	0.3	0.5	1.0	1.7
Final consumption expenditure of Public Administrations and ISPs	-1.3	-1.0	-0.2	-0.8	-0.9	-0.2	-0.8	-0.4
Gross fixed investment	-9.3	-8.1	-5.8	-5.1	-3.3	-1.8	0.5	-0.1
Imports (a)	-5.3	-7.7	-5.1	3.4	-1.6	0.9	4.3	3.3
Esportazioni (a)	3,8	1,7	0,0	2,9	2,0	2,7	7,0	5,9

(a) Current values

Source: Processing by Veneto Region - Regional Statistical System Section on Istat data, and Prometeia estimates and forecasts, marked in red

euro. Although Veneto is in a better position than the average of all Italian regions, it has lost nearly 21,000 enterprises and about 116 thousand work units from 2007 until today. The loss of wealth by sector from 2007 to 2014 was as follows: the value produced by industry excluding construction was lower by about € 6.5 billion, construction € 3.5 billion, and service industry about € 3 billion.

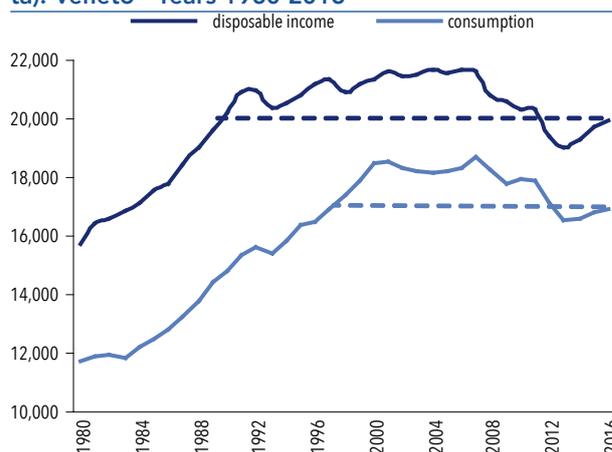
The GDP per inhabitant, which is commonly used to measure the degree of well-being of an area based on the amount of wealth created by the economic system, collapsed starting in 2007 both in Veneto and nationally. While still maintaining a level of more than € 3,000 above the Italian average, it is expected that in 2015 Veneto's GDP per capita will rise slightly in real terms compared to 2014, only reaching 1995/96 values, however.

Disposable income summarizes the economic well-being the residents of an area, considered as consumers and savers, may enjoy. It includes all inflows and outflows attributable to residents, even if occurred outside the area of residence, whereas it excludes resources obtained in the measured area by persons residing elsewhere. In 2014, the disposable income per capita of Veneto households was about € 19,300, higher than the national average, but, in real terms, falling and comparable to the value reached at the end of the 80s. Forecasts assume it will rise slightly in 2015. The consumption per capita of households,

Per capita GDP returned to 1995 levels

evidently linked to income level, showed the same trend: a decrease starting 2007, a short recovery in 2010 when the light at the end of the tunnel was being glimpsed, further falling and stabilization for the next biennium. The expected levels of 2014 are those of the years 96/97.

Fig. 1.4.3 - Final consumption expenditure and disposable income of households (euro, year 2010 per capita). Veneto - Years 1980-2016



Source: Processing by Veneto Region - Regional Statistical System Section on Istat data and Prometeia estimates

In 2014, the increase in purchasing power due to low inflation did not translate into a similar increase in



Brent Crude Price (\$/barrel) - Years 1987-2015

consumption; households increased their savings rate, obviously influenced by the country's uncertain prospects. This happens also because the people of Veneto traditionally focus primarily on having a job; they are not accustomed to high levels of unemployment and worries in this sense have a negative impact on expectations and spending decisions. Some economists expected that during this recession consumers would try and maintain constant their standard of living, in spite of a reduction in their disposable income. This is what happens in business cycles when the situation is deemed to be temporary. In this case, however, the opposite happened: consumption contracted more than proportionally to the decline in earnings. This suggests that consumers perceived the current negative phase as a permanent worsening of the economic situation, so much so that they reacted by increasing precautionary savings.

Fig. 1.4.4 - Fig. 1.4.4 - Propensity to save by households. Veneto and Italy - Years 1980-2016



(* *Proportion of savings on household disposable income*)
 Source: Processing by Veneto Region - Regional Statistical System Section on Prometeia data and estimates

Among other components that contribute to the formation of the GDP, we analyzed gross fixed capital representing the value of durable goods purchased by resident producer units, to be used in the production process, as well as the value of the services incorporated into fixed capital goods purchased. In 2014, Veneto's investments per worker had a further decline (-2.4% compared to the previous year) and an increase is expected only in 2016.

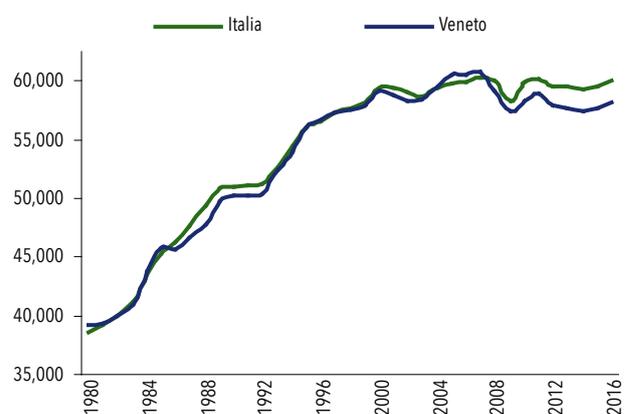
Fig. 1.4.5 - Gross fixed investment per work unit (euro, year 2010). Veneto and Italy - Years 1980-2016



Source: Processing by Veneto Region - Regional Statistical System Section on Prometeia data and estimates

After a decline in 2009, productivity recovered, although never again reaching the peak of 2007; it fell to a low in 2014 and is expected to accelerate in the coming years.

Fig. 1.4.6 - Added value per work unit (euro, year 2010). Veneto and Italy - Years 1980-2016



Source: Processing by Veneto Region - Regional Statistical System Section on Prometeia data and estimates

The prices in Veneto

Inflation continues to slow down in Italy, and in 2014 reached the rate of 0.2%. The so-called "shopping cart" is clearly slowing down compared to 2013. The



rate of change of the price of food and of house related and personal expenses went from 2.2% in 2013 to + 0.3% in 2014. But the zero inflation is largely due to the sharply declining trend in energy prices caused by the further marked decrease in fuel prices. Looking ahead, based on the recent survey by Bank of Italy-Ill Sole 24 Ore, businesses expect to maintain substantially stable the selling prices of their products in 2015. The average inflation measured in Veneto was still lower than the national average: it was nil. A -3.5% in energy prices was recorded, partly offset by a rise in the prices of services, +0.9%. With regard to specific items of expenditure, Veneto showed a sharp drop

Inflation was affected by weak demand and falling oil prices

in prices for communication devices (-16.2%), telephone services (-5.2%) and computer equipment (-6%), as well as a depreciation of electricity, gas and other fuels (-4.2%), household textile articles (-1.9%), apparel (-0.7%) and food (-0.6 %). As for services, there was an important decline for insurance services (-4.8%). The prices of holiday packages increased in 2014, along with the prices of books and stationery, the cost of education, postal services, purchasing vehicles and alcoholic beverages.

1.5 The Russian crisis: the impact on Veneto's economy

From 2000 to 2014, Veneto's exports to Russia showed intense growth, almost four times larger than the growth recorded by the region's total exports. Russia went from ranking 25th in the list of target markets in 2000 to 12th in 2004 and 8th in 2014.

In 2014, Russia's economy suffered a substantial slowdown: from a 1.3% GDP growth in 2013 to 0.6%. The fragility of a growth model that includes little diversification and is overly biased toward the energy sector came to the fore; the collapse in oil prices that occurred in 2014 significantly affected Russia. Furthermore, geopolitical tensions with the European Union aggravated the situation further with the application of sanctions on Russia, while at the same

Fig. 1.5.1 - Veneto's export performance to Russia and overall (2000=100) - Years 2000-2014



Source: Processing by Veneto Region - Regional Statistical System Section and Prometeia on Istat data

time Russia blocked imports of certain agribusiness products from EU countries. The ruble depreciated substantially, inflation rose. Based on these premises, it is estimated that in 2015 a further deterioration will lead to recession in the Russian economy. Continuing tensions with Western countries will favor the escape of foreign capital, thus producing a negative effect on investment, while household consumption will be affected by reduction in real wages as a consequence of soaring prices (in March, the inflation level reached 17%). Weak domestic demand and a further depreciation of the ruble will have a negative impact on the dynamics of imports. To assess the impact of the Russian situation on Veneto in 2015, we performed a simulation using national, international and regional forecasting models by Prometeia. Our underlying assumptions are a 4% drop in the Russian GDP and a depreciation of the ruble by 50% in 2015. On the basis of the simulation, reduced Russian demand would have a negative impact on Veneto's exports of about 1.2 percentage points, reverberating on the added value of the various sectors, as per the relationships described in the models. The added value of industry excluding construction would be affected the most (-0.67 percentage points), while the impact on other sectors would be more modest, ranging from -0.14 for agriculture to -0.08 percentage points for services. The downsizing of the Russian economy, together with the fall of the ruble, could cost our region's GDP more modest growth for about two tenths of a per-



cent, amounting to a loss of about 338 million euro in real terms. However, some clarifications are in order. These results we obtained arise from the underlying assumptions we made (see above). Therefore, exogenous shocks of a different size would inevitably have a different impact on Veneto's economy. Secondly, our results were derived from a mechanical feedback of econometric models, which necessarily neglect some aspects. For example, our simulation cannot estimate how much the uncertainty associated with geopolitical tensions will condition the behavior of operators, especially their investment decisions.

Tab. 1.5.1 - Simulation of the impact of the Russian crisis on Veneto's economy: absolute and % differences compared to the baseline scenario - Year 2015

	Differences compared to the baseline scenario	
	absolute (a)	%
GDP	-337.9	-0.24
Exports	-615.2	-1.20
Added value:		
- agricultur	-3.5	-0.14
- industry	-206.0	-0.67
- construction	-6.7	-0.11
- services	-72.0	-0.08

(a) million euro - real values
 Source: Processing by Veneto Region - Regional Statistical System Section and Prometeia on data from various sources