

Italian growth delayed

Central bank chief says economic level of '07 is four years off

BY CHRISTOPHER EMSDEN

ROME—Italy's economy will take four years to grow back to its 2007 size, and public debt and deficits will grow perilously over the period, said Bank of Italy Governor Mario Draghi.

Mr. Draghi, who also sits on the European Central Bank's Governing Council, said he expected the Italian economy to grow next year, spurred by a global recovery.

Mr. Draghi was speaking to a Senate committee on the government's latest three-year economic and budget blueprint, known as the DPEF. The DPEF forecasts that gross domestic product will contract more than 5% this year and that the budget deficit will rise to more than 5% of GDP.

Higher public spending is inevitable in such a recession, Mr. Draghi said. But he said Italy would run a primary deficit—budget spending before considering interest pay-

ments on the public debt—for the first time in 18 years in 2009.

Italy should consider supporting its industrial sector, which includes many small and midsize firms, a "priority," as their collapse would permanently lower Italy's potential growth, Mr. Draghi said.

Sweeping structural overhauls will be needed to generate funding for the deficits to come, he said.

Italy's public debt is expected to rise sharply, then decline to 115% of GDP in 2013, according to the DPEF. That is close to the levels of the early 1990s, when Italy whittled down its public debt by embarking on Europe's largest privatization campaign.

Sales of state assets from 1995 to 2004 helped knock down Italy's public-debt level by 11 percentage points of GDP, but "there were no accompanying structural interventions on current spending trends to put public debt on a sustainable and declining path," Mr. Draghi said.

Starting next year, Italy will have to cut its budget deficit by one percentage point of GDP each year, Mr. Draghi said. The figure will rise to 3% of GDP a year in 2013 if social programs aren't cut, he added.

Mr. Draghi also urged a crack-down on tax evasion.

ECB President Jean-Claude Trichet said earlier this month that euro-zone members with large public debt would have to accelerate their budget-deficit reduction plans beyond the pace set forth in the Stability and Growth Pact in the wake of the current recession.

Istat, the Italian government statistics agency, estimates that around 16% of Italian GDP takes place in the untaxed informal sector. Others, including the Organization for Economic Cooperation and Development, have higher estimates.

The Finance Ministry said last week that 80% of Italians declared annual gross income in 2007 below €26,000 (\$36,990). That left 12% of the population to pay more than two-thirds of the income-tax bill.

Mr. Draghi said revenue from value-added tax fell 1.5% last year even though household consumption, which he said was the best proxy for sales-tax trends, rose 2.3%.

VAT revenue fell 10.2% in the first quarter from the year-earlier period, even though consumption declined just 2.6%, he added.

Taxes on full-time employees, who are subject to withholding taxes, declined just 0.9% in the first quarter, Mr. Draghi said.

