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INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

CREDITWORTHINESS OF ITALY

September 28, 1953

Department of Operations  
Europe, Africa and Australasia

### **Conversion Rates for Italian Currency**

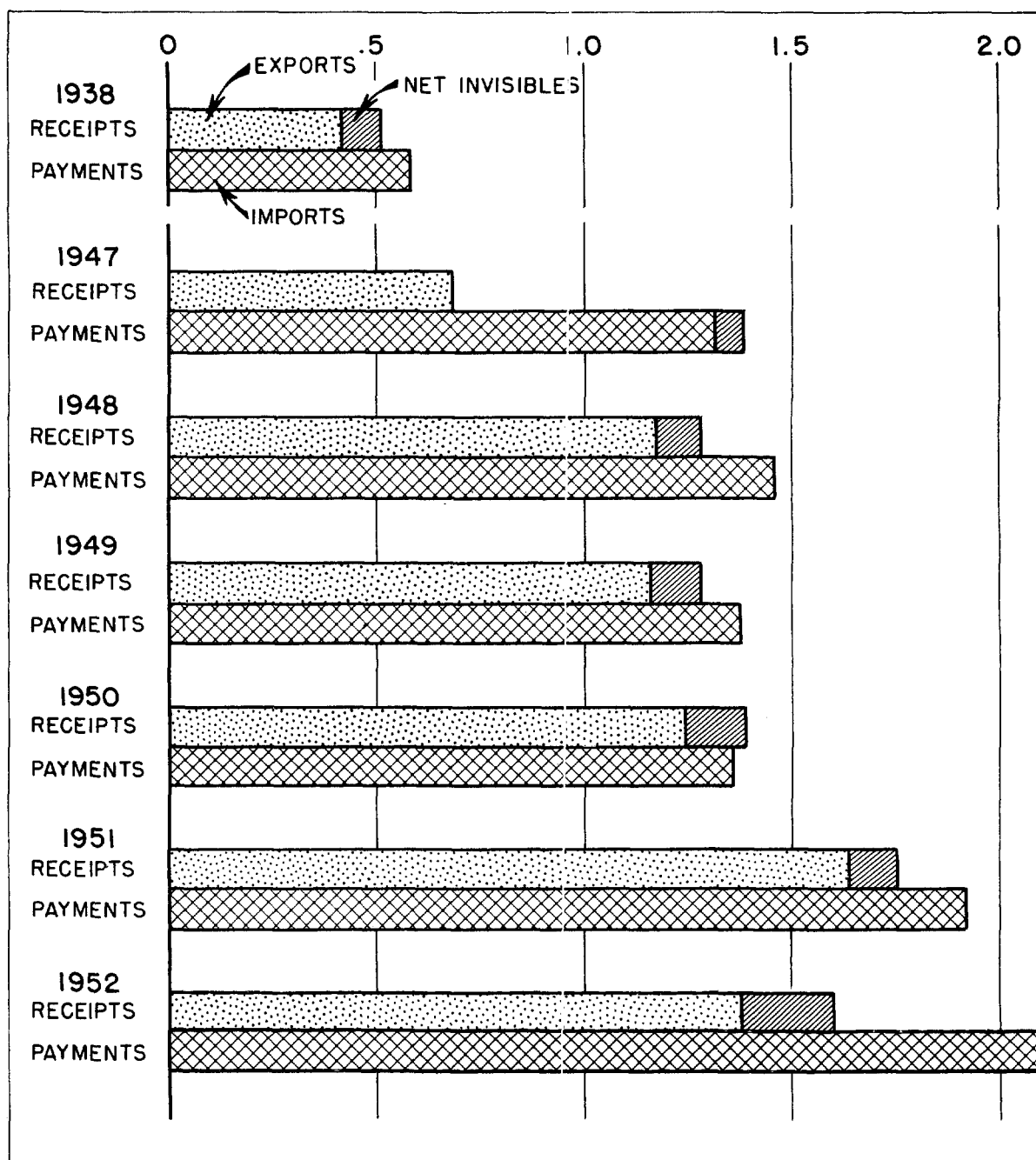
<b>U. S. \$1</b>	<b>= Lit. 625</b>
<b>Lit. 1</b>	<b>= U. S. \$.0016</b>
<b>Lit. 1,000,000</b>	<b>= U. S. \$1,600</b>

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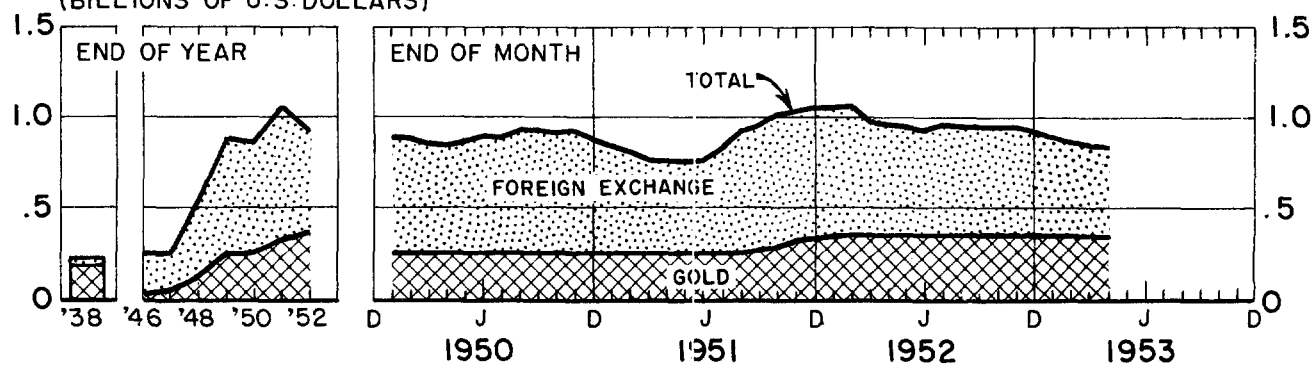
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# ITALY

## BALANCE OF PAYMENTS ON CURRENT ACCOUNT (BILLIONS OF U.S. DOLLARS)

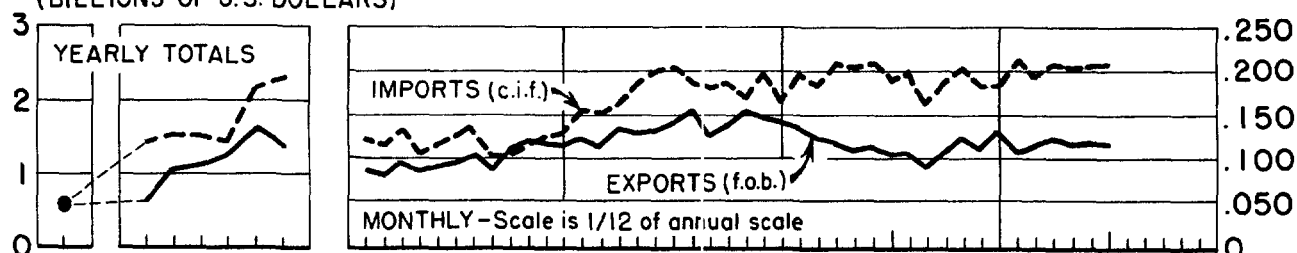


## GOLD AND FOREIGN EXCHANGE ASSETS (BILLIONS OF U.S. DOLLARS)

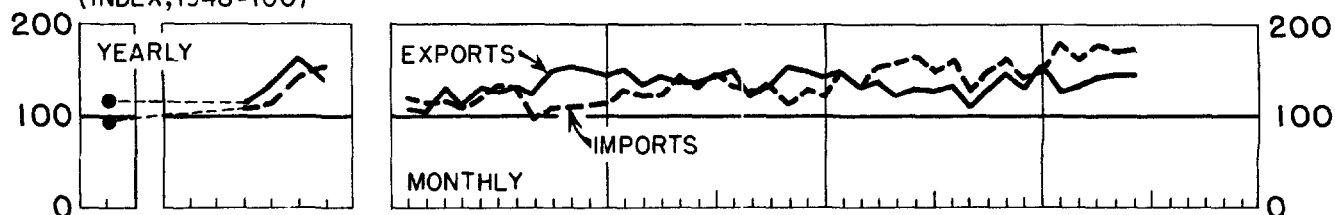


# ITALY

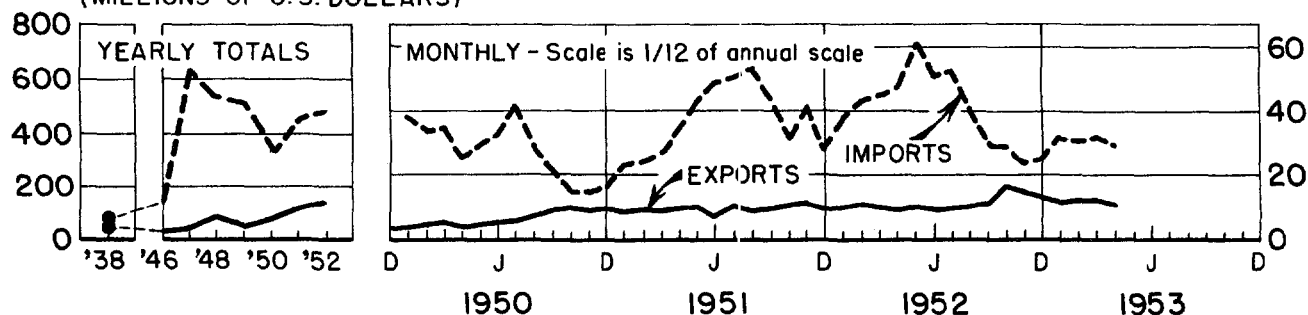
## TOTAL EXTERNAL TRADE (BILLIONS OF U.S. DOLLARS)



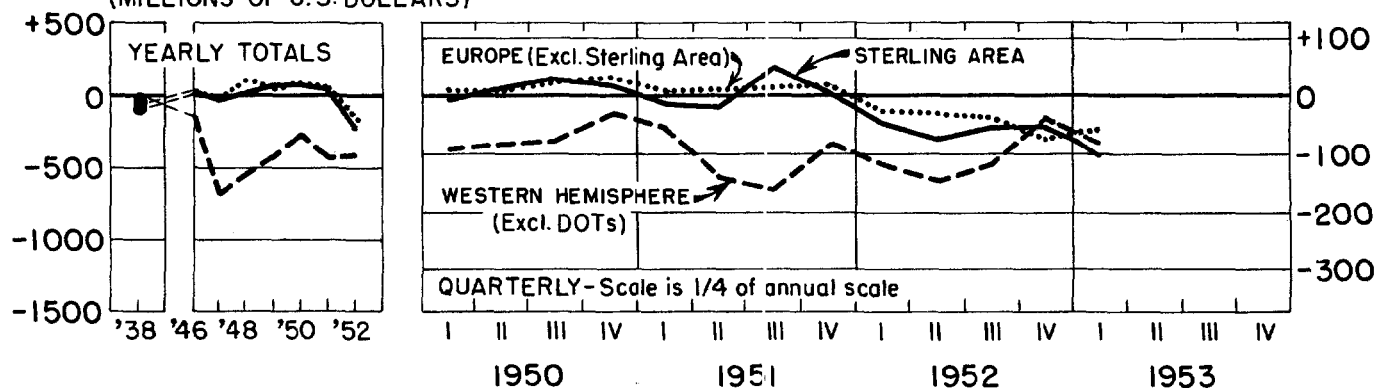
## VOLUME OF TRADE (INDEX, 1948=100)



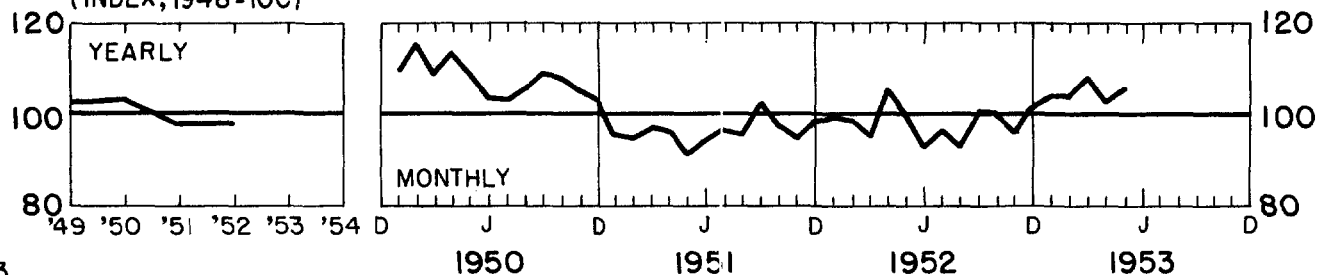
## EXTERNAL TRADE WITH U.S. (MILLIONS OF U.S. DOLLARS)



## TRADE BALANCES WITH SELECTED AREAS (MILLIONS OF U.S. DOLLARS)



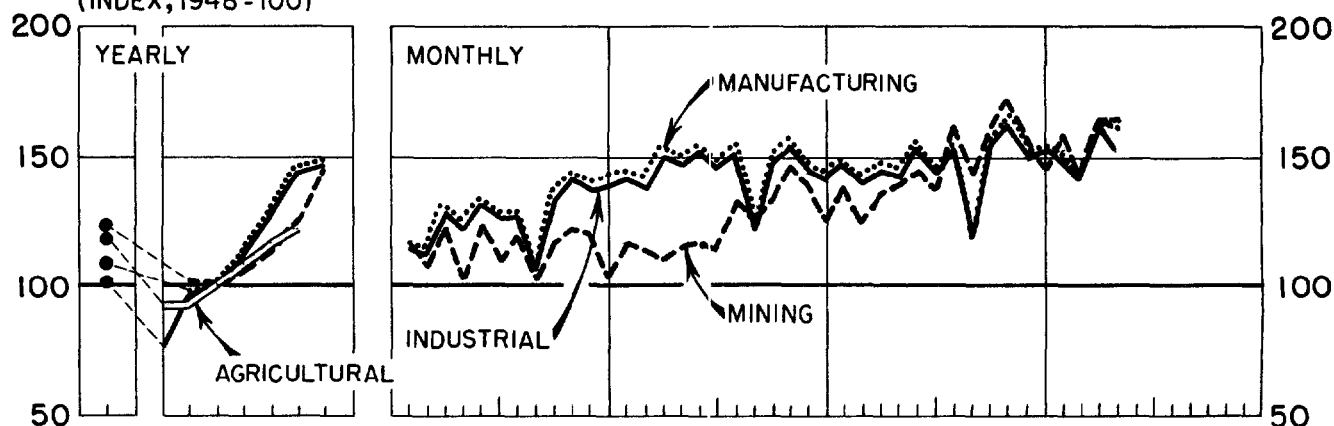
## TERMS OF TRADE (INDEX, 1948=100)



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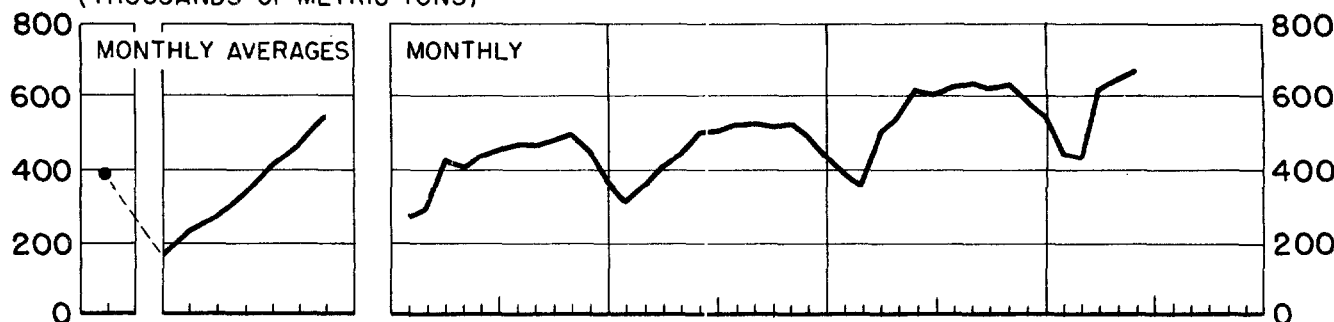
## PRODUCTION INDEXES (1948 WEIGHTS)

(INDEX, 1948 = 100)



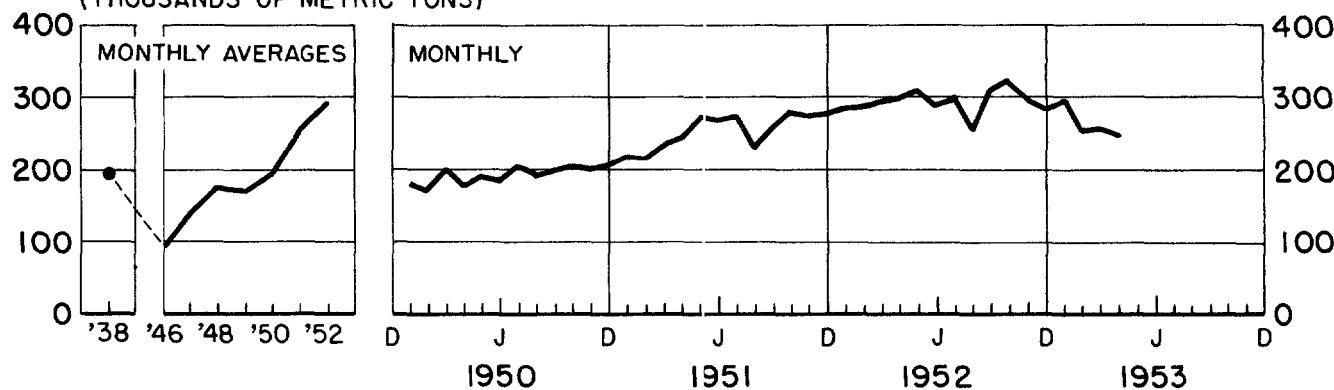
## PRODUCTION: CEMENT

(THOUSANDS OF METRIC TONS)



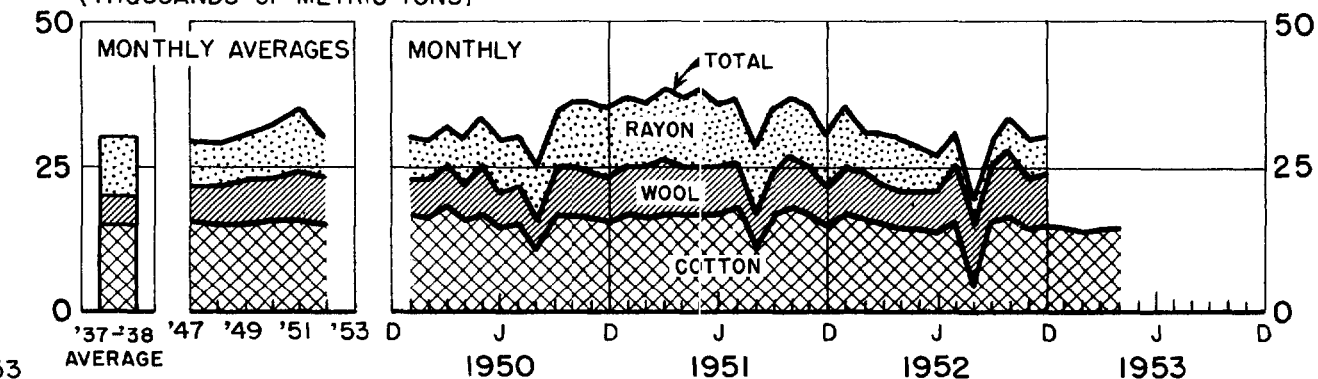
## PRODUCTION: CRUDE STEEL (INGOTS AND CASTINGS)

(THOUSANDS OF METRIC TONS)

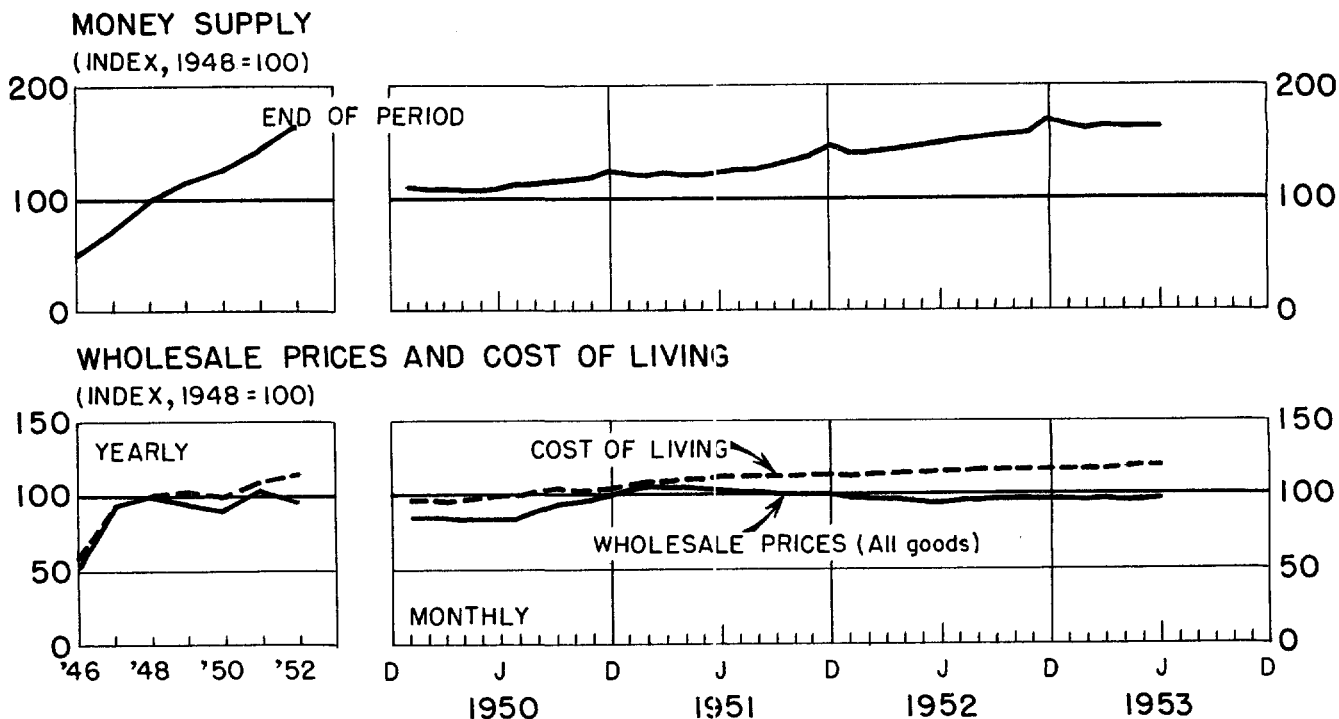


## PRODUCTION: TEXTILES

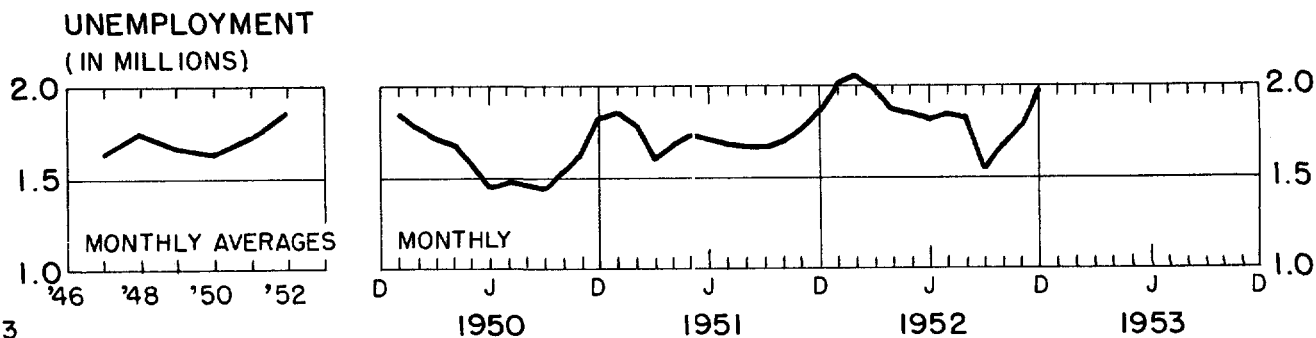
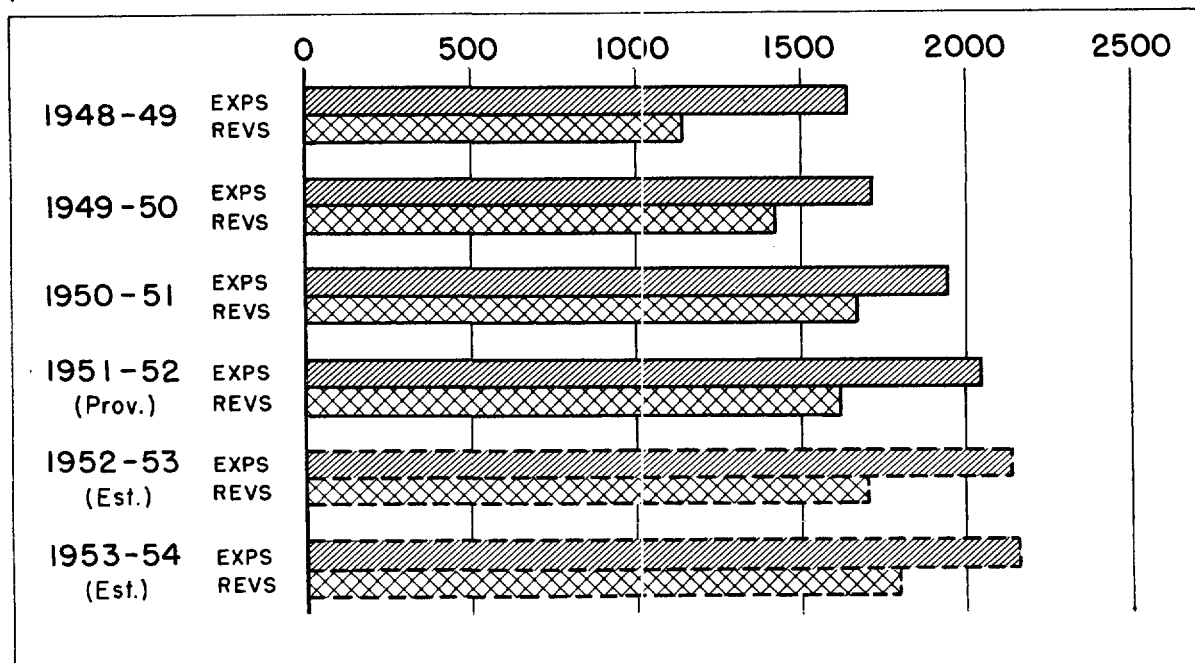
(THOUSANDS OF METRIC TONS)



# ITALY



## REVENUES AND EXPENDITURES (BILLIONS OF LIRE)



## Basic Statistics

Population: 46,884,000

Area: 119,800 sq. miles

Currency Unit: Italian lire (Lit) U.S. \$1 = Lit 625

Trade Statistics (in million \$):

	<u>1949</u>	<u>1950</u>	<u>1951</u>	<u>1952</u>	<u>Jan - June</u>	
					<u>1952</u>	<u>1953</u>
Exports	1121	1199	1644	1383	710	692
Imports	<u>1545</u>	<u>1446</u>	<u>2167</u>	<u>2314</u>	<u>1190</u>	<u>1224</u>
Trade Balance	-391	-229	-525	-932	-480	-532

<u>Balance of Payments on Current Account:</u>	<u>1949</u>	<u>1950</u>	<u>1951</u>	<u>1952</u>
Deficit or Surplus (in million \$)	-102	731	-160	-573 (est)

<u>Gold and Foreign Exchange Reserves:</u>	(end of period)	<u>1949</u>	<u>1950</u>	<u>1951</u>	<u>1952</u>	<u>1953</u>
(Bank of Italy and Government)						(Apr.)
Gold (in million U.S.\$)		256	256	333	346	346
Foreign Exchange (in million U.S.\$)		<u>637</u>	<u>619</u>	<u>712</u>	<u>565</u>	<u>488</u>
Total		893	875	1045	910	834

<u>External Public Debt: (Dec. 31, 1952)</u>	U.S. \$	\$486 million
	Other	\$ 26 "
	Total	\$512 "

<u>Gross National Product (in billion \$)</u>	<u>1950</u>	<u>1951</u>	<u>1952</u>
	13.3	15.4	16.2

Real Income Per Head (1952): \$300 (est)

<u>Budgets:</u>	<u>1949/50</u>	<u>1950/51</u>	<u>1951/52</u>	<u>1952/53</u>	<u>1953/54 (est)</u>
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Expenditures (billion Lit)	1714	1935	2048	2132	2153
Receipts               "       "	<u>1419</u>	<u>1673</u>	<u>1624</u>	<u>1704</u>	<u>1787</u>
Deficits	-295	-262	-424	-428	-366

<u>Money Supply (end of period):</u>	<u>1949</u>	<u>1950</u>	<u>1951</u>	<u>1952</u>	<u>1953 (June)</u>
(In billion Lit)	2243	2495	2880	3364	3248

<u>Wholesale Prices:</u>	(1948 = 100)	1949	1950	1951	1952	1953 (Jan-June)
(Average)		95	90	103	97	97

<u>Cost of Living:</u>	(1948 = 100)	<u>1949</u>	<u>1950</u>	<u>1951</u>	<u>1952</u>	<u>1953</u> (Jan-June)
(Average)		101	100	110	114	117

<u>Industrial Production:</u>	(1948 = 100)	<u>1949</u>	<u>1950</u>	<u>1951</u>	<u>1952</u>	<u>1953</u> (Jan-May)
(Average)		110	127	144	146	154

<u>Agricultural Production:</u>	(1948 = 100)	<u>1949</u>	<u>1950</u>	<u>1951</u>	<u>1952</u>
		109	116	121	125 (est)



SUMMARY

1. The national income of Italy has recovered from the low levels to which it fell during and immediately after World War II. The income per head is now slightly higher than prewar in spite of a 10% increase in population.
2. This growth in national income and in income per head has resulted from an increase in agricultural output of about 7%, an increase in industrial production of approximately one-third and from the generally prosperous conditions in the construction and service fields.
3. Although Italy continues to be dependent upon imports of basic foodstuffs and raw materials and minerals, the recent discovery of natural gas has been very helpful, and according to present plans for its development, should provide Italy with the equivalent of about 9 million tons of coal annually by 1956.
4. With the reconstruction phase completed, Italian investment policy is now being directed toward the development of underdeveloped areas and the creation of additional employment opportunities.
5. The economic development prospects of Italy are relatively limited, but under the stimulus of favorable foreign and domestic demand, considerable increases in output appear possible both in agriculture and in industry.
6. However, because of the rapid growth in population, even an intensive investment program and reasonably favorable emigration prospects are not likely to reduce significantly the present level of structural unemployment of 1.3 million. Unemployment and underemployment remain the most unfavorable feature of the Italian economic and social situation.
7. Italy has enjoyed relative price stability ever since the monetary stabilization of 1947 and even the inflationary pressures which arose after the outbreak of hostilities in Korea have been held in check very satisfactorily.
8. The condition of public finances remains difficult and will be further aggravated by the reduction of counterpart availabilities as U.S. aid declines. However, public revenues should continue increasing as national income rises and a more determined effort is made to collect the newly enacted direct taxes. Moreover, the recently rising level of savings should permit the continuation of projected public investment activity without further encroachment on financing availabilities for the private sector.
9. The Italian balance of payments is affected by two basic weaknesses (a) while her imports consist of essential foodstuffs and raw materials, her exports largely fall in the "soft" categories, such as textiles and specialty foods; and (b) she generally earns a surplus in inconvertible or partially convertible currencies, while she is in deficit with the dollar area.
10. After achieving a small surplus in her balance of payments in 1950, Italy's external accounts deteriorated seriously in 1951 and especially in 1952. This deterioration largely resulted from a decline in Italian exports to the United Kingdom and other sterling area countries and France which had

to deliberalize, and from an increase in Italian imports because of a stepped up rate of domestic investment.

11. There is, however, no reason to expect a continuation of an Italian deficit with E.P.U. Indeed, if her major trading partners pursue liberal commercial policies, Italy should be able to balance her accounts with E.P.U. without any great difficulties.

12. It will probably be more difficult to eliminate the dollar deficit, but increasing availabilities of non-dollar wheat, cotton and fuel (including domestic methane) should make possible a redirection of many basic dollar imports once U.S. aid ends. Moreover, some further increases of Italian exports to the U.S. and increased dollar earnings from tourism and emigrants' remittances is possible provided that the U.S. national income continues to grow and her commercial policies do not become more restrictive.

13. Thus while the balancing of Italian external accounts in general and with the dollar area in particular still remains a serious problem, it does not appear to be insoluble provided that high levels of production, income and trade are maintained by Italy's major trading partners and their commercial policies are further liberalized.

14. Service on the Italian external public debt is relatively light, amounting to between 2 and 3% of Italy's foreign exchange earnings. Its chief burden arises from the fact that most of the Italian debt is in dollars and service payments on this portion account for roughly 10% of her dollar earnings.

15. Because the Italian debt service record has been very satisfactory and in view of the previously mentioned prospects for improving somewhat her dollar earnings and diverting elsewhere some of her basic dollar imports, Italy should be able to manage her present, or an even slightly higher dollar indebtedness.

16. In these circumstances, Italy may be regarded as a reasonably good risk for another \$10 million loan at this time to the Cassa per il Mezzogiorno.

## INTRODUCTION

The ability of Italy to service additional dollar indebtedness depends upon her success in carrying further the already substantial improvement in her balance of payments, particularly with the dollar area, which she has achieved since the war. As a result of the heavy damage sustained by her economy during the war, Italy ran balance of payments deficits in excess of half a billion dollars a year during the immediate postwar years. By 1950, however, her national income had risen above the prewar level in real terms, and she was able to earn a slight balance of payments surplus on current account. Her national income has continued to rise since 1950, but she has not again been able to achieve a balance of payments equilibrium. The deterioration in her balance of payments has, moreover, not been due solely to post-Korean world economic developments. It is rather a reflection of weaknesses inherent in the Italian economy which have yet to be overcome. From a balance of payments point of view, Italy's greatest handicaps are her dependence upon imports, especially from dollar sources, for her basic foodstuffs and raw materials, and the restriction of her exports to non-essential agricultural products, textiles, and other manufactures generally produced at rather high costs. Limitations of a more fundamental character, however, are her scarce natural resources, her excessive and rapidly increasing population and her low national income, which limits her capacity for the investment required for any substantial increase in that income. Since Italy's external creditworthiness depends upon her ability to overcome these handicaps, the present paper is concerned mainly with analyzing them and assessing her prospects for success in surmounting them.

## NATIONAL INCOME AND EXPENDITURE

The Italian national income fell to catastrophically low levels during and immediately after World War II. It is estimated that in 1945 it was only about half as great as before the war. Aided by foreign relief and reconstruction grants, however, the economy recovered very rapidly, and by 1950 the national income sufficiently exceeded the prewar level to offset the growth in population and to provide a real income per head at least equivalent to that of 1938. There were further increases in real national income of roughly 5% in 1951 and 2 - 3% in 1952. Although the Italian income per head remains among the lowest in Western Europe - roughly equivalent to \$300 at the current rate of exchange - and leaves much room for improvement, the postwar performance of the Italian economy demonstrates its basic vitality and holds out promise of further growth, provided that favorable domestic and international conditions prevail.

The increase in national income has made possible a small improvement in private and public consumption and a more intensive investment policy. Per capita personal consumption is now somewhat higher than prewar, with the increase concentrated on industrial products and services. Consumption of foodstuffs which absorbs 58% of gross consumption expenditures is probably not yet as high as before the war. Governmental consumption has also risen both relatively as well as absolutely, especially as a result of increased spending for defense purposes. The level of gross investment reached approximately 16% of the gross national product in 1951. High profits

during 1951 induced increased private investment in 1952; public investment also rose; and the over-all level of gross investment slightly exceeded 18%. Until very recently, the principal aims of Italian investment policy have been to reconstruct the productive plant destroyed or damaged by the war and expand basic industries. With these objectives virtually achieved, the primary emphasis has now shifted to the development of underdeveloped areas and the creation of additional employment opportunities. In both these fields, the program of the Cassa per il Mezzogiorno plays a key role. The continued maintenance of adequate levels of private and public investment is a basic prerequisite for the future growth of the Italian economy and for the solution of its major structural problem of unemployment.

### Agriculture

Although agriculture is Italy's primary economic pursuit, employing approximately 41% of the total working population and producing about 30% of the national income, Italy's land resources are not adequate to enable her to achieve self-sufficiency in foodstuffs or staple raw materials. She is dependent upon imports for a large fraction of her wheat and, in lean years, olive oil, and such important raw materials as wool, cotton, hides and rubber. On the other hand, she produces a surplus of a wide variety of less basic agricultural commodities, such as citrus and deciduous fruits, nuts, vegetables and cheeses. Although these commodities are produced under relatively favorable cost conditions, the large fixed investment required for their production and the immobility of the large labor force employed makes it difficult for their production to respond quickly to changes in demand. Since most of these commodities are in the luxury or semi-luxury class, moreover, they are among the first to feel the adverse effects of contractions in business activity in the countries to which Italy sells or to fall under the axe of restrictions when these countries encounter balance of payments difficulties. The result is not only to affect Italy's export position adversely but also to bring serious distress to a large section of Italian agriculture which cannot readjust itself rapidly to a sudden change in external demand. The postwar commercialization of Italian agriculture, with its concomitant heavy investments in irrigation for tree crops and other expensive civil works, have accentuated this situation.

Over-all agricultural production has recovered very satisfactorily from the depths to which it sank in the immediate postwar years. By 1950, it had reached the prewar level, and further increases in 1951 and 1952 have brought it up to roughly 7% above prewar. However, this increase is attributable mainly to a few specialized commodities, in particular vegetables, fruit, sugar beet, milk, and olive oil, the output of which is now well above prewar levels. The production of wheat, corn and potatoes has generally lagged behind the best prewar years, and this lower level of output, combined with a 10% increase in the population, has made it necessary for Italy to import very much larger quantities of wheat than before the war. The bumper wheat crop of 8.5 million tons in 1953 has now improved this situation.

Although the Italian Government plans to make efforts to increase agricultural production substantially, it does not anticipate any marked increase in self-sufficiency in basic foodstuffs. Its present program calls for an increase of about 15% in over-all output during the five years ending 1956/57. However, production of rice, corn, rye, barley and wheat are

expected only to regain or slightly exceed prewar levels. A small increase is projected in the output of oils, especially olive oil. On the other hand, sugar beet production is expected to continue its expansion. Fodder production is to be increased to make possible a 10% increase in livestock numbers and an improvement in the quality of the herds with a consequent increase in meat production from about 8,000 to about 8,500 tons a year. Finally, a very substantial increase is projected in fruit and vegetable production, its exact magnitude depending upon the volume of export demand.

The increase in agricultural output is to be achieved not through an expansion in the area under cultivation, but through a drive to increase yields and a shift of acreage to crops to which Italian soils and practices are best adapted. The fulfillment of these goals depends upon the implementation of a well-balanced long-term investment program of which the Cassa program constitutes an integral part. With the extension of additional farm credit for mechanization, better seed selection, and the use of more insecticides and fertilizers, it should prove possible to increase yields and reduce costs. Indeed, the objective of producing from the present area under wheat, of 4,724,000 hectares, roughly the same 8 million tons produced in 1937-39 from an area of 5,163,000 hectares (about 10% larger) has already been achieved. While the over-all aims appear realizable and their achievement should strengthen Italian agriculture considerably, because of her physically limited farming resources and a continually growing population, Italy's heavy dependence on imported basic foodstuffs and raw materials is not likely to alter appreciably in the foreseeable future.

#### Mining and Energy

As in the case of soil resources, Italy suffers from a serious deficiency in known basic minerals and metals. Most of the coal, petroleum, iron ore and copper consumed by the Italian economy must be imported. Extractive industries consequently play a relatively minor role in the Italian economy, being responsible for only 1% of the national income. Since the war, most phases of mining which are economically sound have regained or exceeded prewar levels. The output of bauxite, zinc, mercury and manganese in particular have increased satisfactorily. The output of other minerals, including iron ore and sulphur, are however still below prewar, and the possibilities of further expansion are extremely small because of limited deposits, high extraction costs and, in certain cases, excessive transport costs. Furthermore, the prospects of discovering new deposits of any considerable size do not appear very bright.

The only exception to the generally unpromising outlook in subsoil resources is natural gas. Its recent discovery in northern Italy is the most outstanding natural resource discovery in Western Europe since the war. Development has been very rapid, with Italian natural gas production increasing as follows:

<u>Year</u>	<u>Million cu. m.</u>
1950	505
1951	957
1952	1,435
1953	2,500 (estimated on basis of January-May output)

Present plans call for an annual output within five years of 7,000 million cubic meters, a goal which does not appear to be unrealistic. Such an output would provide Italy with the equivalent of roughly 9 million tons of bituminous coal annually, or nearly nine-tenths of recent coal imports. Although the savings in coal imports are not likely to be anywhere near such proportions because of increasing domestic and industrial consumption, the development of domestic methane will permit a substantial growth in fuel consumption while at the same time lightening the burden on the Italian balance of payments imposed by coal imports. The discovery of natural gas has also raised hopes of the existence of significant quantities of petroleum in Italy and exploration is now in progress.

No expansion of Italian production would have been possible in the postwar period without a growth in electric power capacity which was inadequate and badly balanced at the close of the war. Although the problem of the power deficit has not yet been completely solved, there has been considerable progress as a result of an increase in generating capacity of 23% between the close of 1948 and the close of 1951, which has made possible an increase in production from 22,240 million kwhs in 1948 to 30,900 million in kwhs in 1952. In addition, the recent completion of ECA financed thermal plant should go far toward eliminating the threat of power shortages such as occurred in 1949 as a result of inadequate rains and snowfall. It is now estimated that demand for power will increase by about 7% a year in the next few years. To satisfy these requirements, a program has been formulated which envisages an increase in production capacity to 42,500 million kwhs in 1956. This should be more than adequate to cover the estimated requirements in that year of 40,500 million kwhs. The completion of this program should assure Italy of a reasonably ample power supply in the foreseeable future.

### Industry

The manufacturing industries account for roughly 40% of the Italian national income, and employ 36% of the working population. Badly damaged during the war, their plant has been completely reconstructed, modernized, and, in some fields, expanded, with the aid of substantial public and private investments. As early as 1949, therefore, the index of manufacturing production was already 3% higher than prewar, and by 1951, it surpassed the prewar level by 36%. In 1952, it increased by only 1% more, for substantial increases in certain branches of industry were offset by decreases in others. Production in the textile industry, for example, fell by 8% compared with 1951, because of a sharp decline in export demand, offset only in part by a rise in domestic demand, especially in the South, during the latter part of the year. On the other hand, the metallurgical and mechanical industries, roughly one-third of whose capacity has been reportedly unused during the postwar period, increased their output by approximately 10%.

In spite of a more satisfactory showing in the early months of 1953, the long-run outlook for Italian industry is somewhat uncertain. The Italian OEEC program to raise output by 25% in the five years beginning with 1952 has already fallen behind schedule because of a drop in export demand during 1952. Several deep-rooted obstacles stand in the way of further expansion of Italian industry. The relatively low average real income limits domestic demand, while the surplus of manpower and the consequent threat of unemployment act as a drag on productivity, slowing down output and raising costs.

High interest rates and the dependence of Italian industries upon imported raw materials and fuels further accentuate the cost problem. The result of all these factors is to weaken Italy's competitive position as an exporter of industrial products, and her engineering and shipbuilding industries have been suffering from chronic overcapacity. On the other hand, her textile industry, which has until now appeared to enjoy a relative cost advantage, is among the first to be subjected to import restrictions by Italy's major trading partners and in the future may be expected to encounter increasing competition from Japan and the expanding textile industries in underdeveloped countries. Thus, hampered by a limited domestic demand and by unstable foreign markets, Italian industrial expansion will have to proceed most cautiously.

### Construction and Services

The recent expansion in Italian production, incomes and profits has acted as a powerful stimulus to the service and construction industries, which contribute roughly a quarter of the national income. The improved position of the consumer coupled with Government subsidies for low-cost housing have increased residential construction to boom levels by Italian standards. Some 770,000 habitable rooms were completed in 1952, as compared with 592,000 in 1951. In addition, high rates of public and private investment activity increased non-residential construction so markedly that a serious cement shortage developed and it was necessary to resort to voluntary allocations and imports. The outlook for the building and construction industries remains favorable provided that investment is maintained at the projected rate and that national income grows as forecast.

With high levels of output in agriculture and industry and with a construction boom in progress, most service industries appear to have been prospering. Noteworthy among these, from the point of view of national income and even more from that of the balance of payments, are the activities centering around tourism, hotels, etc., and ocean shipping. The hotel trade, a significant index of tourism and a vital factor in the Italian balance of payments, has been very prosperous, and barring further deterioration in the international situation, its outlook is very favorable. A price level lower than in many other parts of Western Europe and the active attempt of the Cassa to develop and popularize new tourist attractions should help to encourage more tourists to come to Italy. In the case of shipping, the Italian merchant marine has staged a comeback and war losses have now been fully made up. As a result, the Italian balance of payments deficit on shipping and freight is being gradually compressed. Indeed, there are reasonably good prospects that, with the further expansion of the Italian passenger and tanker fleet, Italy's deficit on account of transportation can be eliminated or that she may even achieve a small surplus on this account.

### Population and Manpower

The most serious structural problem of the Italian economy stems from her relative overpopulation. During the past 15 years the population has been increasing at an annual rate of 0.68%, rising to a total of over 47 million. The recent decline in the birth rate has been offset by a similar decline in the death rate, and the present outlook is for an annual increase of roughly 400,000. Since emigration is not likely to remove more than 150,000 persons annually, the net increase in population may be estimated at

250,000. The labor force is expected to be augmented by about 130,000 annually, with a consequent further aggravation of the already serious unemployment problem. Despite the vigorous investment policy pursued during the past several years, structural underemployment is widespread and unemployment remains at a level of about 1.3 million. Bridging the gap between the growing labor force and available employment opportunities constitutes the greatest challenge to economic and social policy. While the projected high levels of investment will help to cope with the manpower problem, unemployment is likely to continue in the coming years to be the most adverse feature of the economic and social situation.

#### INTERNAL FINANCES

In the immediate postwar period, when the Italian economy was still partially paralyzed, expansion in bank credits to business and the financing of Government deficits led to one of the most violent inflations experienced in Western Europe, with the price index rising to 60 times its prewar level. Stabilization measures were taken in the fall of 1947, and prices have remained relatively stable since then. Even the outbreak of hostilities in Korea and the ensuing sharp increases in the prices of many imports had a slighter impact on the price level in Italy than in many other countries. The wholesale price index rose about 15% from 1950 to 1951, but it has since declined and now appears to have stabilized at a point only 8% above 1950. On the other hand, the cost of living index which rose by only 10% after the outbreak of Korean hostilities continued to advance during 1952 and is now roughly 17% above 1950. In part, the rise in the cost of living resulted from an increase in indirect taxes and in wages, especially of civil servants, whose increased disposable income exerted an inflationary influence on the prices of consumption goods. It is likely also that the lack of vigorous competition among sellers contributed to the rise in certain retail prices and, as a result, in the cost of living.

By pursuing a deliberately restrictive credit policy, Italian monetary authorities have managed for several years to hold down the growth in the means of payment to well within the limits of expanding national output. This policy has made it necessary to keep interest rates on commercial loans at 8% or higher, and may on occasion have restrained legitimate business expansion. It has, however, prevented undue speculative activity, and has paid off in the form of relative price stability and a sound currency. During 1952 the money supply expanded more rapidly than national income, largely as a result of increased deposits and credits extended to the business community, but this did not result in any significant pressure on the price level. The continuing vitality of the Italian economy coupled with a substantial import surplus, appear to have contributed toward the maintenance of a stable lira.

Public finances continue to be somewhat strained and are a cause of concern to the public authorities. Government revenues have been rising as a result both of the growth of the national income and recent increases in indirect tax rates, although the fiscal reforms with their greater emphasis on direct taxation appear thus far to have yielded very meager results. However, expenditures have also been on the increase because of larger defense



outlays, increased civil servants' salaries and a stepped-up public investment program. In 1951/52 the Government had a cash deficit of Lit. 410 billion, or roughly a quarter of total expenditures. Excluding the accumulated lira counterpart of E.C.A. aid of Lit. 196 billion from the revenues, the deficit amounted to Lit. 670 billion, or over one-third of the expenditures. The cash deficits in 1952/53 and 1953/54 are estimated at Lit. 443 and Lit. 366 billion respectively.

Despite budget deficits, Treasury operations during the past few years have actually had a slightly deflationary effect on balance because the deficits were financed out of current savings by the economy, and a slight contraction in the means of payment resulted from Treasury activities. In keeping cash disbursements down, however, the Government has greatly increased the volume of its arrears. These arrears represent a potential Treasury liability and have made it necessary for contractors to obtain temporary financing from the commercial banks. The continuing excess of expenditures over revenues and the elimination of counterpart funds, as FOA aid is reduced, present a real challenge to Italian fiscal authorities. There are indications, however, that a more resolute effort will be made to collect the new direct taxes, while the rising national income should result in larger revenues from existing indirect taxes. Moreover, according to most recent indications, the rise in the over-all level of savings appears to have made it possible for the Government to market a larger volume of its own securities at the same time allowing a healthy expansion in the loanable funds available to the business community. Indeed, the striking liquidity of the Italian banking system which developed in 1952 may well be expected to continue providing national income and savings continue to rise at the projected rates. Thus, while public finances continue to present some real problems, these do not appear to be insurmountable, and it should be possible to continue the current rate of public investment without seriously disturbing monetary stability. Should such a threat develop, however, Italian monetary authorities, judging from their recent record, may well be relied upon to cope with it rapidly and decisively.

#### EXTERNAL ECONOMIC POSITION

The basic weakness in Italy's external economic position is the fact that while she depends on imports for her essential raw materials and foodstuffs, such as wheat, cotton, coal, petroleum and wool, between half and two-thirds of her exports consist of textiles and food specialties. The semi-luxuries and other "soft" commodities which she exports are hard hit when her trading partners experience adverse business conditions or encounter balance of payments difficulties, but her own ability to compress imports is relatively limited. Additional difficulties arise from the geographic structure of Italian foreign trade under conditions of inconvertible, or only partially convertible, currencies. Western Europe and the sterling area have emerged as Italy's best markets, while the dollar area has become an important source of her imports. In spite of these handicaps, Italy's external economic position has developed favorably since the war and given high levels of production, income and trade both at home and abroad, the prospects that she can balance her foreign accounts appear reasonably good.

## Foreign Trade

Wartime damage and dislocations of trade relations reduced Italy's foreign trade to exceedingly low proportions in the immediate postwar years. In 1947, she was exporting less than half as large a volume of goods as before the war, and even in 1949 her exports were still below prewar volumes. Foreign relief and reconstruction assistance enabled her to sustain a considerably higher level of imports, financing a trade deficit in excess of half a billion dollars a year. Exports expanded very vigorously, however, and by 1950, had risen to a level about 20% above prewar, in volume terms, compared with an increase of only 14% in imports. Since the Italian terms of trade were also improving, the trade deficit declined markedly, falling to \$267 million in 1950.

The outbreak of hostilities in Korea resulted in a reversal in earlier favorable trends. Exports continued their rapid expansion in 1951, increasing by another 18% in volume, but imports increased by 23%, and the Italian terms of trade deteriorated. Italy's trade deficit rose, in consequence, to \$489 million. In 1952, as a result of deliberalization measures taken by the United Kingdom and France, Italian exports fell, while imports, buoyed up by a high rate of domestic investment, rose. The trade deficit increased, therefore, to \$930 million or 40% of the value of Italian imports in 1952. In the first six months of 1953 the trade deficit was running at an annual rate of \$1060 million. There are indications, however, that the situation is improving. Many of the British import restrictions were removed in March, and since March, the Italian trade deficit has been running slightly below the levels of the corresponding months of 1952.

For an explanation of Italy's trade difficulties in 1952, a brief picture of the composition of her trade is essential. Close to 80% of her imports are accounted for by four categories of commodities - foodstuffs, fuels and textile raw materials, which each make up 20% of the total, and machinery and metal products, which constitute another 15-18%. Her principal export is textiles, which accounted for 37% of the total in the boom year 1951 and, in spite of a great falling off in sales in 1952, to 23% in that year. Foodstuffs and machinery each account for another 20% with a miscellaneous group of commodities, including metal products, minerals, and chemicals making up the remaining 25-35%.

The deterioration in Italy's trade position in 1952 was the result of special factors affecting a very small number of commodities. Virtually the entire decline in her exports was attributable to textiles, exports of which declined by \$286 million compared with a total decline in exports of \$264 million. All classes of textiles were affected - exports of cotton textiles fell from \$207 million to \$92 million, synthetics from \$181 million to \$79 million, and woollens from \$84 to \$43 million. On the import side, machinery and apparatus and other metal products accounted for virtually all the increase. Imports of these commodities increased by \$156 million compared with an increase of \$146 million in all imports. It would appear, therefore, that the decline in Italian exports in 1952 was the result of the world wide depression in textiles in 1952 accentuated by import restrictions imposed by the United Kingdom and other sterling area countries and France. At the same time, heavy domestic investment swelled

Italian imports of machinery and other metal products, while the unchanged demand for exports other than textiles, higher Italian consumer incomes and an open door policy toward EPU imports prevented demand for other imports from falling. It is significant, for example, that in spite of the sharp decline in textile exports, imports of textile raw materials declined only slightly in value terms and actually increased in volume (raw cotton from 198,000 to 230,000 tons and raw wool from 59,000 to 81,000 tons), resulting in increased inventories of these commodities.

War and postwar dislocations have significantly altered the geographic pattern of Italy's foreign trade to her disadvantage so long as many of the currencies for which she sells remain inconvertible. Immediately after the war, she was, like every other Western European country, excessively dependent upon the dollar area for imports while, as before the war, selling little to it. Although she has been able to shift some of her imports to other regions and to increase her exports to the dollar area, even in 1952, the United States, Canada and Central America supplied 24% of Italian imports, compared with 12% prewar and took only 13% of her exports, compared with 8% prewar. On the other hand, Italian exports to EPU countries, their overseas territories and sterling non-member countries have risen to 64% of the total, compared with 45% prewar, but the share of these countries in Italian imports has remained unchanged at 55% of the total. Changes in the relative importance of other areas in Italian foreign trade merely reinforce the effect of those cited above, with the net result that Italy's sales are made much more largely in inconvertible currencies than her purchases.

Italy - Foreign Trade by Major Areas  
(In millions of U.S. dollars)

	<u>1951</u>		<u>1952</u>	
	<u>Exports</u>	<u>Imports</u>	<u>Exports</u>	<u>Imports</u>
EPU countries <sup>1/</sup> (except sterling)	643	630	592	758
Sterling area <sup>2/</sup>	495	475	290	522
U.S., Canada & Central America	141	530	173	560
All others	366	532	328	474
TOTAL	1645	2167	1383	2314

<sup>1/</sup> Includes overseas territories

<sup>2/</sup> EPU sterling countries, overseas territories, and sterling non-member countries

Until 1950, the geographic pattern of Italian foreign trade was even more unfavorable to Italy, and her huge trade deficit in this period was attributable mainly to the dollar area. Her trade with the EPU countries earned her a surplus of \$120 million a year. As reconstruction rendered her less dependent upon imports from the dollar area her dollar deficit declined from \$500 million in 1948 to \$262 million in 1950, and her over-all deficit showed a parallel decline.

In 1951, when as a result of the post-Korean boom her imports of raw materials rose and her terms of trade deteriorated, her trade deficit with all areas other than the EPU countries rose by a total of \$281 million. Her already substantial trade surplus with EPU countries rose in contrast by \$59 million.

It was the inability of the sterling area and France, to continue any longer to funnel convertible currencies to EPU countries, a process from which Italy, among others, had benefited, that hit Italy's trade hard in 1952. The abrupt retreat of the United Kingdom and France from their foreign trade liberalization policy reduced Italy's exports to sterling EPU countries by over \$100 million and to France by over \$50 million. Italy, still a large EPU creditor continued to permit EPU imports virtually unrestricted entry and her imports from EPU countries rose sharply. As a result, a 1951 trade surplus toward EPU countries of \$173 million was converted into a deficit of \$149 million in 1952. Sterling area retrenchment policies also increased the Italian deficits toward sterling area non-EPU countries and EPU overseas territories. In contrast, Italy's dollar trade deficit remained unchanged at about \$385 million, while her deficit toward South America declined slightly, Italian exports to South American countries declining less than her imports from them.

In assessing Italy's future trade prospects, a distinction must be drawn between her over-all and dollar trade positions. Although the deterioration in Italy's trade balance in 1952 was attributable to the EPU countries and their currency areas, this group of countries does not represent Italy's major trade problem. Although, so long as their currencies remain at least partially convertible into dollars, Italy can probably not hope to earn a surplus from them over an indefinite period of time, there is no reason to anticipate that she must continue to run a deficit of 1952 proportions (\$400 million) or indeed any deficit at all. Provided that there is a continued expansion in world economic activity, Italy should be able to increase her exports substantially. The demand for her textiles should rise above the depressed level of 1952 even though a return to 1951 levels seems improbable. In spite of competition from other manufacturing countries, Italy should also be able to increase her exports of a wide variety of manufactured goods, including machinery and other metal products and chemicals. The prospect for an expansion of her exports of foodstuffs, particularly within Europe, are very promising; she can increase her output of fruits and vegetables greatly, if rising consumer incomes in Europe provide the necessary increase in demand and the markets are opened to her.

Should the increase in exports fail to bring her trade into balance, she can achieve some savings in imports. A compression of imports of textile raw materials should be easily possible, if textile exports fail to recover, since the volume of imports of these commodities rose in 1952, in spite of a decline in textile exports. As a result of the discovery and rapid development of Italy's natural gas resources, fuel imports can be reduced even if Italian economic activity expands. A reduction in imports of machinery from the 1952 level is possible without seriously impairing investment activity, although it would somewhat slow up the processes by which Italy's industries and agriculture are expanding and becoming more efficient. Finally, some import savings are possible through the curtailment of non-essential consumption.

If the necessary saving in imports is unattainable under Italy's present trade policies of virtually unrestricted imports from EPU countries, she can and probably would alter those policies.

The achievement of an over-all balance in Italy's trade will, however, still leave unsolved the problem of her dollar deficit. Even in 1952, when Italy's position vis-a-vis other areas was so much worse than in earlier years, the dollar area still accounted for over 40% of her total trade deficit. The dollar deficit has up to now proved intractable. After a decline of about \$240 million between 1948 and 1950, it rose by \$125 million to a total of about \$390 million in 1952. The fluctuations have been due in the main to variations in the magnitude of Italy's dollar imports, for although Italian exports to the dollar area have increased, the rise has been small. The increase in exports has, however, been gratifying because of the wide variety of commodities encompassed. The entry of such Italian manufactures as Olivetti typewriters, Necchi sewing machines, and Vespa scooters into the U.S. market are noteworthy achievements. A further expansion in exports to the U.S. should prove possible, especially if the U.S. national income keeps growing and her trade policies do not become more restrictionist. However, the prospect that the gap between dollar imports of \$560 million and dollar exports of \$173 million can be overcome by an increase in exports is obviously not promising. Any substantial improvement in Italy's dollar position appears to depend upon a reduction in her imports from the dollar area, and, of course, primarily from the United States. The most important of these imports are, however, essentials.

Five commodities or commodity groups accounted for 75% of Italian imports from the United States in 1952: raw cotton, \$134 million, coal \$70 million, wheat, \$54 million, machinery and vehicles, \$85 million and iron and steel rolled products, \$17 million. Although Italian imports of these commodities cannot be significantly reduced, Italy's dollar position can be improved by a shift to other suppliers. It should not be impossible for Italy to secure from other sources a large part of the 565,000 tons of wheat, the 134,000 tons of cotton, and the 3,405,000 tons of coal she purchased from the United States in 1952. Turkey, with which Italy had a surplus of \$24 million in 1952 and which is interested in a number of commodities sold by Italy - in particular, machinery, and possibly textiles, until her own textile industry becomes capable of meeting Turkish domestic requirements in full - can supply both wheat and cotton. Argentina is a possible source of wheat and Brazil of cotton. Indeed, Brazil from which Italy brought no cotton in 1952 supplied her with 28,000 tons in 1948. Italy has had no difficulty in selling her exports in these two South American countries. She was compelled to restrict exports to both in 1952 to the equivalent of her imports from them because of the large credits she found herself extending. In the case of both Argentina and Brazil, however, the shift depends upon their economic policies, not on Italian demand. Finally, Italy may be able to meet more of her machinery and metal products requirements at home or in other European countries, especially Germany.

#### Balance of Payments

While the Italian balance of payments is largely dominated by movements in trade, invisibles have traditionally played an important role. Two items - emigrants' remittances and tourism - have yielded substantial

surpluses in the past and promise to continue doing so in the immediate future.

In line with the reconstruction progress of the Italian economy and the stabilization of the lira, the balance of payments has registered a substantial improvement in recent years, its course paralleling the course of the Italian trade balance. In 1950, earnings from services more than offset the greatly reduced trade deficit, and Italy achieved a surplus on current account equivalent to roughly \$30 million. The deterioration in Italy's trade position in 1951 and 1952 was reflected in a worsening in her payments position: in 1951 she had a current deficit equivalent to \$160 million, which rose in 1952 to an estimated \$473 million. These global deficits conceal both the surpluses Italy attained outside the dollar area and her continuing substantial deficits with the dollar area, which amounted to U.S. \$212 million in 1950, \$307 million in 1951 and around \$270 million in 1952. Up to now the deficits with the dollar area have been more than covered by E.C.A. aid, with the result that by the end of 1951 official Italian gold and foreign exchange reserves stood at the equivalent of U. S. \$346 million and U.S. \$567 million respectively. Of the foreign exchange reserves, 30% were in U.S. dollars. Although some decline in foreign exchange holdings has occurred recently, the gold reserves remain unimpaired. In addition, Italian banks and individuals hold substantial U.S. dollar balances.

Although Italy's balance of payments position remains a matter of some concern, this is more because of the character and geographic pattern of Italian foreign trade than because of a long run tendency for Italian consumption and investment expenditures to exceed national output. The fact that Italy has had a traditional dollar deficit and a surplus in the only partially convertible currencies of Western Europe, renders the transfer problem a difficult one. She managed to earn U.S. \$92.7 million through E.P.U. in 1951, but has paid it back in 1952 and her ability to rely in the foreseeable future on her major European trading partners as a substantial source of U.S. dollar earnings, is highly questionable.

If Italy's major trading partners are able to maintain prosperous and expanding economies, and if they pursue reasonably liberal commercial policies, however, she should be able to bring her foreign transactions into balance. Her projected investment and economic development program should not only raise output but also improve her balance of payments. The projected increases in the output of fruits, vegetables and other food products, should boost Italian exports to Western Europe, especially if the currently discussed trade liberalization policies affecting agricultural products become a reality. The continuing outflow of migrants should help to maintain the overall level of remittances. Likewise, the prospects of increased earnings from tourism appear good. In quantitative terms, it should prove possible to adjust exports and imports to limit the trade deficit to about the equivalent of \$200 million. Net earnings from remittances and tourism could cover this gap and leave a margin for debt service.

Closing the dollar gap which has amounted to \$200-\$300 million annually in recent years will prove more difficult of achievement. Italy's dollar earnings from exports can probably be increased. She can probably count also on a small increase in emigrants' remittances, and should the U.S. national income keep growing, in dollar earnings from tourism. The ultimate

closing of the dollar gap will depend mainly, however, on the further successful compression or redirection of some basic imports elsewhere. Some of these objectives are likely to be realized promptly; others may take considerably longer. In the meantime, the dollar gap in the Italian balance of payments continues to be met by U.S. assistance, now in the form of defense support of \$102 million and of offshore purchases for NATO of about U.S. \$80 million during fiscal 1952/53.

### CONCLUSIONS

The ability of Italy to service her present external debt or a slightly larger one depends upon her achieving equilibrium in her balance of payments, especially with the dollar area. Numerous internal and external developments will have a bearing on this, with the continuing growth in her national income and a net increase in emigration playing a crucial role. The outlook with respect to most of the major relevant developments appears reasonably good. The recent high levels of private and public investment and the long-term Cassa program give promise of a continuing rise in the output of the Italian economy. Recent bilateral migration arrangements as well as continuing interest on the part of such international bodies as the Intergovernmental Committee on Migration and OEEC in fostering Italian emigration, are encouraging developments which should contribute toward the solution of Italy's basic structural problem of over-population. In spite of the deterioration in the Italian balance of payments during 1951 and 1952, her very satisfactory performance in 1950, and the continuing high level of investment provide reasonable grounds for expecting that she can again bring her current balance of payments into equilibrium. Even the dollar problem which continues to be difficult, should become much easier to manage as possibilities for compressing or redirecting dollar imports increase. In this connection, the growing availabilities of coal, wheat and cotton against non-dollar currencies are most encouraging, since these commodities are responsible for most of the Italian deficit with the dollar area.

The present external debt of Italy amounts to a total of approximately \$512.4 million equivalent, of which the U.S. dollar debt accounts for almost \$486 million. In addition, Italy is liable for war reparations equivalent to about \$260 million. Against these reparations there are, however, Italian assets and claims which in the case of some countries may wholly or partially offset them. Annual service payments on this debt (excluding reparations) are \$39 million in 1953 and average less than \$35 million in the 1954/59 period, declining steadily thereafter. Of these amounts, amortization payments account for between \$20 million and \$25 million in the earlier years, and under \$20 million in the later ones. These total service payments constitute only about 2% to 3% of Italy's global foreign exchange earnings and would be relatively light under conditions of convertible currencies. Their burden, therefore, arises solely from the fact that practically the entire debt is in U.S. dollars and service payments on this portion of debt are around 10% of U.S. dollar earnings.

The Italian debt service record is very satisfactory. There was no record of default on any publicly-held external obligations of Italy until June 1940 when Italy entered the war. Since 1947, Italy has made every effort to place all of its external public issues on a paying basis. Debt service

payments on dollar bonds were resumed under the "Lombardo Plan" which went into effect in December 1947. Similar plans were adopted in 1948 for the sterling bonds and in 1951 for the Swiss franc bonds. To date all plans have been carried out according to schedule. Although the dollar balance of payments position of Italy remains difficult, her dollar earnings have been rising recently and the prospects of further increases from additional exports to the dollar area, emigrants' remittances and tourism appear reasonably good. Moreover, the prospects of redirecting many of the basic dollar imports have recently improved substantially. In view of these favorable considerations, Italy may be regarded at this time as a reasonably good risk for a second loan of \$10 million to cover the dollar impact of the second Lit. 100 billion expenditures by the Cassa per il Mezzogiorno.