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Overview of the Italian Banking Market



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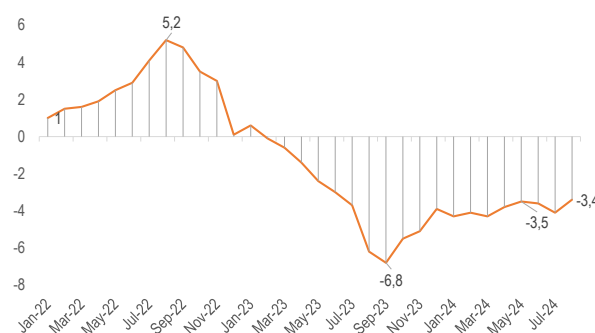
La banca
per un mondo
che cambia



The recovery of the Italian economy continues, although at a moderate pace. In Q2 2024, real GDP rose by 0.2% q/q, supported by domestic demand, while net exports contribution was negative. The decline of investment reflected the contraction of expenditure on dwellings, while that on machinery increased. Consumption moderately increased. Services value added continued to recover while the manufacturing sector further contracted. The labour market has showed significant improvements since Q2 2021. In Q2 2024, the employment rate rose to 62.2%, a historical peak that, nevertheless, remains low in comparison with the main EU partners

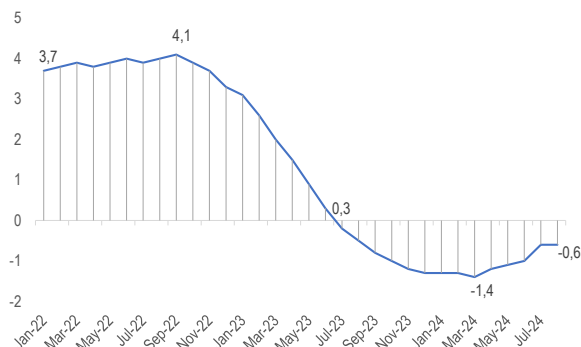
Italy: loans to Non-financial corporations

(y/y % changes)



Italy: loans to Households

(y/y % changes)



The negative trend in credit mainly reflected the weakening of demand, due to high interest rates, lower financial needs for investments and greater recourse to self-financing. The decline is also due to significant repayments of existing loans.

In August 2024, total adjusted outstanding loans to non-financial firms declined for the nineteenth month in a row. In the first eight months of 2024 loans declined on average -3.9% recording a further worsening with respect to 2023 (when the average rate of growth was -3.2%). In the first eight months of 2024 outstanding loans to households decreased by 1.0% y/y, after an average growth rate of 0.5% y/y in 2023. The dynamic of loans for house purchase has been particularly affected by the tightening of monetary policy and the increase of interest rates

The liquidity held by firms on deposits and current accounts remains high. At the end of August 2024 firms' deposits amounted to €428 billion, -€11 billion from the peak recorded in July 2022 and €121 billion more than 2019, before the start of the pandemic.



OVERVIEW OF THE ITALIAN BANKING MARKET

Economic Research

*BNL BNP Paribas**

Italy: economic outlook

The recovery of the Italian economy continues, although at a moderate pace. After increasing by 0.3% in Q1 2024, real GDP rose by 0.2% in Q2 and by 5.5% compared to Q4 2019. In Q2, domestic demand added 0.4 percentage points to the overall growth, while net exports contribution was negative (-0.5), as exports fell while imports slightly rose. From January to July, Italian sales to Germany declined by almost 5.5%. The contribution of stocks to the GDP increase was positive (+0.3).

In Q2 2024, consumption rose by 0.3%, after +0.1% in Q1, despite the propensity to save rose above 10%. The purchasing power of households increased above pre-Covid level, as nominal income rose while inflation decelerated.

The moderate growth of the economy mainly reflects the disappointing evolution of investment, which declined by 0.1% in Q2, after -0.5% in Q1. The breakdown by items of expenditure was mixed. Investment in dwellings recorded the second decline in a row, given the cancellation of fiscal incentives to improve the efficiency of buildings, while those in other type of construction, including infrastructure and industrial buildings, increased by 0.7%, after +2.9% in Q1. Despite the uncertainty around new public incentives for ICT equipment, investment in machinery rose by 0.8% (+8% compared to Q4 2019). Business confidence has slightly improved, remaining above long-term average.

The recovery of the Italian economy remained mixed by sector. Value added of construction declined by 0.6% in Q2, after +0.4% in Q1. Services continue to increase, also benefiting from the further recovery of international tourism. From January to June, the number of foreigner travellers in Italy rose above 40 million, 2.2 more than in the same period of 2023. Manufacturing continued to be affected by the slowdown of both global demand and investment expenditures. In Q2, value added fell by 0.7% (-0.8% in Q1). Although declining on annual basis, manufacturing producer prices remain about 20% higher than at the beginning of 2021. Production has further declined, with a widespread contraction by sector.

In Italy, the labor market has showed significant improvements since Q2 2021. In Q2 2024, the number of people employed (seasonally adjusted value) reached 23.9 million, 409,000 units more than in Q2 2023, and 873,000 more than in Q4 2019, before the outbreak of the pandemic. The increase mainly involved the female component: in Q2 2024, there were 467,000 more women employed than in Q4 2019.

Thanks to these latest improvements, the employment rate in Q2 2024 in Italy rose to 62%, a historical peak that, nevertheless, is still lower than those of the main EU partners (77.6% Germany, 69% France, 66% Spain). Despite the improvement in the labor supply, in some sectors, Italian enterprises are experiencing some difficulties in finding the necessary skills. In the first half of 2024, among the companies associated to Confindustria (the association of Italian enterprises) that were looking for personnel, 70% (mostly large industrial companies) reported difficulties in finding skills related to the digital transition, internationalization and the green transition..

* Views and opinions expressed are those of the authors and do not necessarily reflect the view of the bank.

Bank loans

Credit growth has weakened considerably in Italy as a result of monetary tightening. Given the overall financial strength of companies and the availability of significant liquid assets, the impact of the change in monetary stance made necessary by the surge in inflation was less drastic than what could have been expected on the basis of historical experience. Monetary restriction led to a rapid increase in interest rates and a sharp slowdown in credit to non-financial companies; the growth became negative in December 2022, and was equal to -3.4 percent in August 2024.

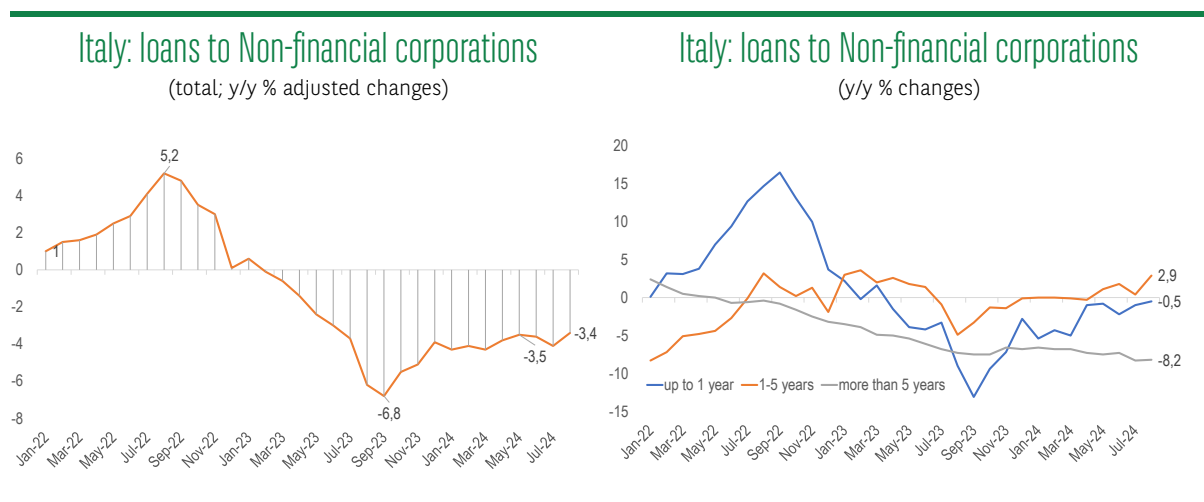
The trend in credit mainly reflected the weakening of demand, due to high interest rates, lower financial needs for investments and greater recourse to self-financing. The decline is also due to significant repayments of existing loans. Corporate liquidity, although lower than at the peak of the pandemic, still remains high.

In recent months the cost of bank funding decreased slightly, contributing to a modest decline in interest rates on loans to firms. While credit standards began to ease in the spring, bank lending to non-financial corporations contracted further, reflecting still weak credit demand. The growth in loans to households for house purchase showed some signs of improvement, although it remained low. In the third quarter 2024, firms reported virtually unchanged credit access conditions.

The decline in interest rates on loans to non financial companies and loans for house purchases remained limited, almost in line with that recorded in other major economies of the Eurozone. The three rate cuts implemented by the ECB, the last one on October 17, have started the path of progressive reduction of rates. The future monetary decisions, as repeatedly underlined by the ECB, will be guided by economic data.

Loans to Non-financial firms

In August 2024, total adjusted outstanding loans to non-financial firms declined for the nineteenth month in a row. In the first eight months of 2024 loans declined on average -3.9% recording a further worsening with respect to 2023 (when the average rate of growth was -3.2%).



The decrease of loans to non-financial corporations affected both the segment of loans with maturities up to one year (-3.3 % y/y on average between January and August 2024; -4.2% on

average in 2023) and the segment with maturities beyond 5 years (-7.3 % y/y in the first eight months of the year; -5.9% on average in 2023). More favourable remained the evolution of loans with maturities between 1 and 5 years. The growth rate of loans within this maturity bucket increased by 0.7% in the first eight months of 2024 and recorded a +0,2% y/y on average in 2023.

According to the ECB Bank Lending Survey, in Italy in the third quarter of 2024, credit standards for loans to firms remained unchanged. The overall terms and conditions became slightly more favourable, mainly thanks to lower lending rates, which, in turn, were also due to the reduced margins. Firms' demand for loans, which has been falling since the beginning of 2023, declined further, albeit slightly, reflecting greater use of internal financing and alternative finance.

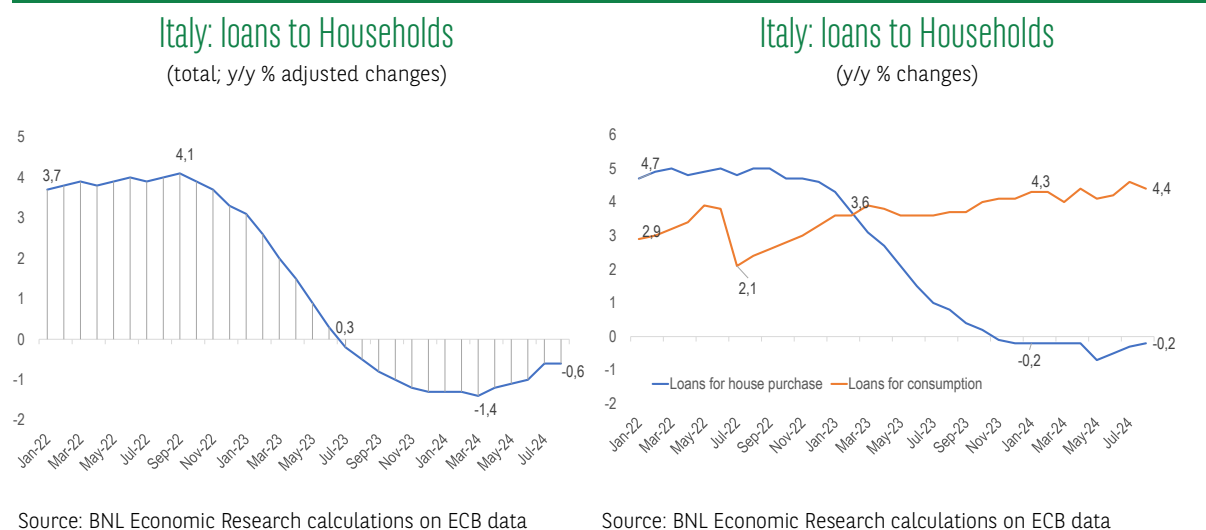
The liquidity held by firms on deposits and current accounts remains high. At the end of August 2024 firms' deposits amounted to €428 billion, -€11 billion from the peak recorded in July 2022 and €121 billion more than 2019, before the start of the pandemic.

Between November 2023 and August 2024, the interest rate on new bank loans to firms remained high, even showing signs of reduction (from 5.6% to 5.1%).

Loans to Households

Lending to households gradually attenuated in 2023, and then turned into a contraction due to the decline in households consumption and signs of worsening of the real estate market associated with the rapid rise in interest rates.

According to the ECB Bank Lending Survey, in Italy in the third quarter of 2024 households' demand for mortgages grew sharply again, while the increase in consumer credit demand was smaller. In the fourth quarter of 2024, the demand for loans from firms and households is expected to grow across all loan segments.



The two main components present different dynamics: while mortgages are weakening, consumer credit continues to grow, albeit at a slower pace than in the past. In the first eight months of 2024 outstanding loans to households (calculated using adjusted data) decreased by 1.0% y/y, after an average growth rate of 0.5% y/y in 2023. In the first eight months of the year consumer credit increased by 4.3% y/y (on average +3.8% in 2023) although a general slowdown

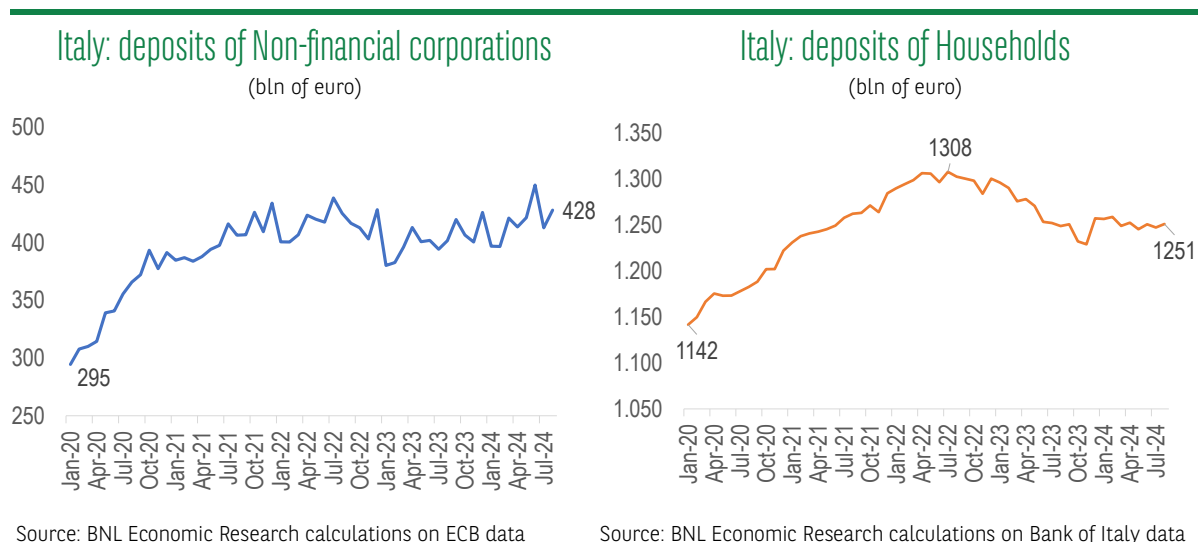
in spending, and not favorable supply conditions. Loans for house purchase declined by 0.3% (1.6% on average in 2023).

The dynamic of loans for house purchase has been particularly affected by the tightening of monetary policy and the increase of interest rates. After reaching a peak of 4.5% in November, the cost of new loans to households for house purchase showed first signs of reduction falling to 3.6% in August 2024.

Deposits and asset quality

Since the start of the interest rate hike cycle, growth in residents' deposits has gradually weakened, reflecting developments in current account deposits. In 2024, households continued to reduce their current accounts in part shifting their savings towards longer-term deposits on which banks offer higher interest rates than those on demand deposits.

In the first eight months of the year, households deposits declined by 1.5% (on average) recording in August (+0.2% y/y) the first positive value after eighteenth negative growth in a row while deposits of non financial companies grew by 5.4% after decreasing on average -3,2% in 2023.



Between May and August, the marginal cost of bank funding decreased by around 15 basis points (to 1.9 per cent). Contributory factors were the fall in interbank market rates, due to the cut in key interest rates, and the lower cost of bond funding (from 4.4 to 3.9 per cent); the latter declined further in September.

Interest rates on current account deposits remained broadly unchanged at 0.5 per cent, while those on new deposits with an agreed maturity decreased by 0.2 percentage points, to 3.3 per cent. The considerable spread between these two rates continued to support the shift towards deposits with an agreed maturity. Bank bond funding grew significantly: in the second quarter, net issuance was €14.9 billion (compared with €2.8 billion in the previous quarter)

The stock of non-performing loans continues to remain at a low level. The sale of non-performing loan in a more developed market, together with a reduced flow of new NPLs and solid liquid conditions of non financial companies have contributed to maintain a sound credit quality. In Q2 2024 the stock of non-performing loans was €55bn.



In the first quarter of 2024, the new non-performing loans rate was 1.3 %, a level slightly higher than the one recorded in the previous quarter (1.1%). According to Bank of Italy's projections, the overall ratio between new non-performing loans on total loans for households and firms might increase driven by the higher cost of debt. However, this ratio is projected to remain well below the level seen in previous times of crisis for both households and firms.

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