Istituto Affari Internazionali

Italian Exports and the Transatlantic Trade and Investment Partnership

by Umberto Marengo

ABSTRACT

Italy's exports increased by 11 percent between 2011 and 2015 (as of July), benefitting from two major macroeconomic developments: the global recovery and the depreciation of the euro. Beyond the EU common market, the United States continues to be Italy's first strategic trading partner due to its higher than average willingness to spend its growing purchasing power on Italian products and its appreciating currency. Furthermore, in view of the emerging economies' current slowdown, trade relations with the United States and the Transatlantic Trade and Investment Partnership (TTIP) are set to be of critical importance for the success of the "special export promotion plan" announced by the Italian Government.

Italy | United States | External trade | BRICS | TTIP

keywords

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by Umberto Marengo*

1. Italy's positive export record

Italy's exports of goods and services increased by 11 percent from 2011 to July 2015. This provided an important lifeline to the Italian economy in the second phase of its double-dip recession that ran from 2011 to 2014.[1] Italy's export performance remained strong throughout the crisis. Already in 2011, export had returned to pre-crisis levels and, after a period of stagnation in 2013, it increased by 2 percent in 2014. In the first seven months of 2015, export further increased by 5.5 percent compared to the same period in 2014. If this trend continues, by December 2015 Italy's exports could reach nearly 420 billion euros. This would account for over a third of the country's GDP. Export figures also show that Italy has a strong competitive position in manufacturing but its service sector continues to underperform in global markets. Export of goods accounts for roughly 25 percent of the country's GDP whereas export of services accounts for only 5 percent of GDP (the lowest share of export of services in the Eurozone).

Nevertheless, the increase in export coupled with a dramatic contraction of domestic demand and import, allowed Italy to achieve a positive trade balance from 2012 onwards. There were essentially three drivers of Italy's positive export performance:

1. the global economic recovery;
2. domestic wage compression and price deflation for certain products;[2] and
3. the depreciation of the euro, which resulted in Italy's products being more competitive outside the Eurozone.

[1] According to International Monetary Fund (IMF) forecasts, Italy's recession will end in 2015 when GDP is set to grow by 0.8 percent. IMF, *Global Economic Outlook*, October 2015, http://www.imf.org/external/pubs/ft/weo/2015/02/index.htm.

[2] See for reference: Marcello Messori (ed.), "In Search of a New Equilibrium. Economic Imbalances in the Eurozone", in *IAI Research Papers*, No. 17 (January 2015), http://www.iai.it/en/node/3252.

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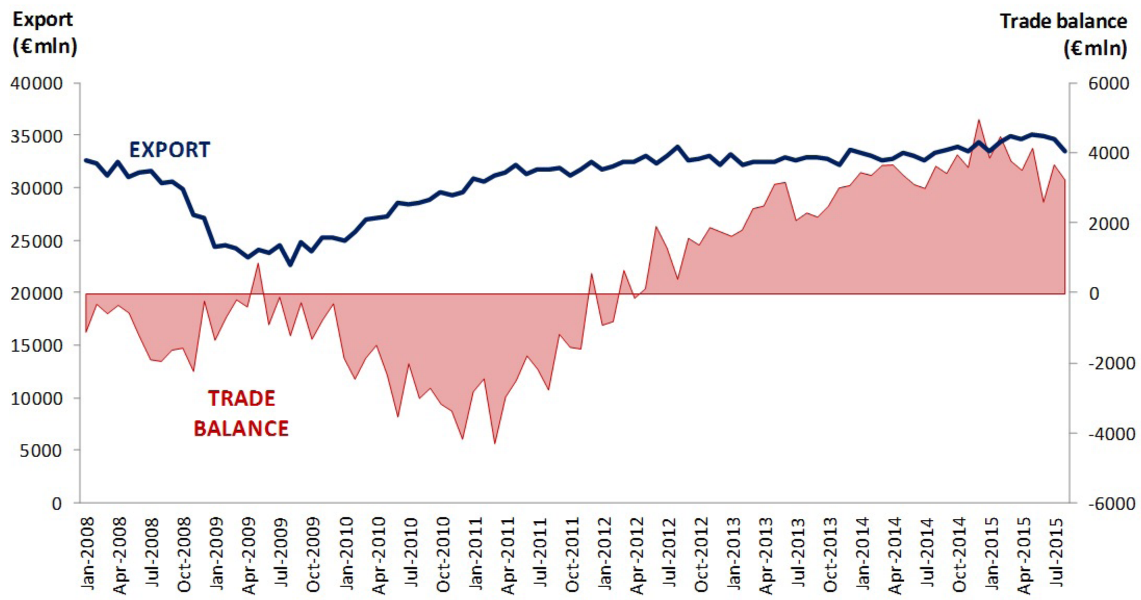
Figure 1 | Italy's trade balance with the rest of the world



Source: authors' elaboration on ISTAT data.

The ECB Quantitative Easing programme had a significant impact on the exchange rate of the euro.[3] Although the Chinese Central Bank decided to depreciate its currency by 3 percent last August in face of the economic slowdown in China,[4] from 2011 to July 2015 the renminbi had already appreciated by 30 percent against the euro.[5] The US dollar had also appreciated by 15 percent over the euro over the same period.

However, the power of depreciations and devaluations should not be overestimated. In trade relations, geographical proximity continues to be a decisive factor as this is still often a proxy of value chain integration. Ten out of fifteen of Italy's main export destinations are in the European Union. Notably, Italian companies export more to Belgium (population 11 million) than to China (population 1.3 billion). The functioning and deepening of the EU common market thus remains a key priority for Italy.

[3] Grégory Claeys, Álvaro Leandro and Allison Mandra, "European Central Bank Quantitative Easing: The Detailed Manual", in *Bruegel Policy Contributions*, No. 2015/02 (March 2015), http://bruegel.org/?p=803.

[4] Chatham House, *Europe and China: Financial Connections through the Renminbi Markets*, 9 October 2015, https://www.chathamhouse.org/node/18789.

[5] European Central Bank (ECB), *Euro Foreign Exchange Reference Rates*, https://www.ecb.europa.eu/stats/exchange/eurofxref (historical variation calculated on annual averages).

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Table 1. Italy's main trading partners

Rank	Trade partner	Export 2014 (€ bln)	Export growth (%) 2014-2015*	Change (%) in local currency/euro 2011-2015*
1	Germany	50.1	3.9	=
2	France	42.0	3.4	=
3	US	29.8	24.6	+15.4
4	UK	20.9	7.8	+11.4
5	Switzerland	19.1	4.5	+14.2
6	Spain	17.9	11.9	=
7	Belgium	13.2	10.2	=
8	China	10.5	1.7	+30.0
9	Poland	10.3	7.2	+1.1
10	Turkey	9.8	7.3	-19.6
11	Russia	9.5	-28.8	-38.0
12	Netherlands	9.3	3.3	=
13	Austria	8.3	3.8	=
14	Romania	6.2	8.5	+0.3
15	Hong Kong	5.5	10.1	+15.4
16	UAE	5.3	14.8	+15.4
17	Brazil	4.7	-11.5	-24.9

* As of July 2015.
Source: authors' elaboration on ISTAT and ECB data.

2. The uneven effects of euro depreciation on Italian exports

The depreciation of the euro stimulated the export of Italian products outside the Eurozone. All things being equal, it can be argued that imports are directly affected by the importers' purchasing power of euro-denominated Italian products. Purchasing power, in turn, depends on economic growth and currency exchange fluctuations. From January 2011 to July 2015, if we consider real economic growth and currency exchange variations, the purchasing power (wealth in "current euro") of Italy's trading partners grew on average by 7.6 percent per year while Italian exports increased on average by 3.7 percent per year.

Italy's export performance is far from even across the world, however. For example, while the purchasing power of the Chinese increased by about 19 percent per year from 2013 to July 2015, export growth was more modest (about 4 percent per year) since Chinese economic growth is now powered mainly by domestic demand.[6] The appreciation of the renminbi raised the purchasing power of Chinese consumers and did not produce a real increase in demand for foreign products. In addition,

[6] Gabriel Wildau and Ben Bland, "China imports slump as growth expected to slide below target", in *Financial Times*, 3 October 2015, http://on.ft.com/1VPcLra.

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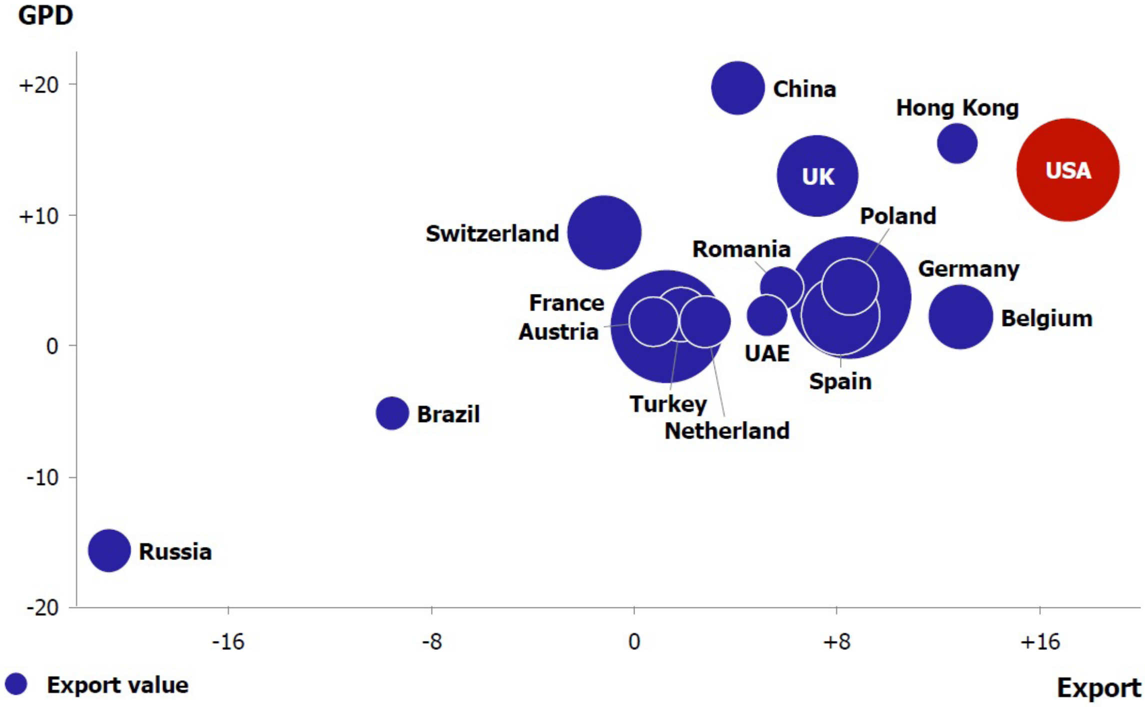
it should be noted that other emerging economies such as Brazil and Russia are currently going through a severe recession accompanied by sharp devaluations and/or depreciations that are making Italian products less competitive in such markets.

Figure 2 | Evolution of Italian exports and purchasing power of its main trading partners

Average annual GDP and export variation (%) of Italy's trade partners, 2013-2015 - current €



Source: authors' elaboration on ISTAT, IMF and ECB data.

On the other hand, the United States continues to be not only Italy's first market outside Europe but also the country where the greatest share of new purchasing power was "spent" on Italian imports. In 2013-2015,[7] imports of goods and services "Made in Italy" increased by 1.3 percent for each percentage point of growth in US purchasing power (see Table 2). Furthermore, the US is set to enjoy a stable growth rate in the short-to-medium term, it is a generally open market, and it can be expected that the US dollar will continue to remain a strong currency against the euro. The tapering of the Federal Reserve Quantitative Easing programme over the medium term will push the dollar to strengthen further, thus increasing its purchasing power vis-à-vis the euro.

[7] Figures calculated on data up to July 2015.

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Table 2 | Purchasing power (GDP in current €) and exports of main trading partners

Trade partner	Import from Italy (€ bln)	Annual average export growth (%) 2013-2015*	Annual average GDP growth (%) 2013-2015*	Ratio import/GDP variation
Germany	52.0	8.6	3.6	2.4
France	43.4	1.3	1.4	1.0
US	37.1	17.2	13.4	1.3
UK	22.5	7.3	13.0	0.6
Spain	20.1	8.2	2.2	3.6
Switzerland	19.9	-1.1	8.6	0.1
Belgium	14.6	12.9	2.1	6.2
Poland	11.1	8.6	4.4	1.9
China	10.7	4.1	19.6	0.2
Turkey	10.5	1.9	2.3	0.8
Netherlands	9.6	2.8	1.8	1.6
Austria	8.6	0.8	1.8	0.5
Russia	6.8	-20.7	-15.8	1.3
Romania	6.7	5.8	4.4	1.3
UAE	6.1	5.3	2.2	2.4
Hong Kong	6.0	12.8	15.4	0.8
Brazil	4.2	-9.5	-5.3	1.8

* Estimates on the basis of January-July 2015.
Source: authors' elaboration on ISTAT, IMF and ECB data.

3. The US is Italy's first strategic partner in international trade

The question today is whether Italian export can continue to grow in the face of the emerging economies' current slowdown, and what actions can be undertaken by companies and the government to this purpose. The IMF expects a decline in the purchasing power of emerging countries in the next few years due to lower growth and possible devaluations. As the global economic outlook deteriorates, Italian companies will face a contraction of foreign demand.

The Italian government announced in March 2015 a "special export promotion plan" and committed 260 million euros to this end.[8] In order for the implementation to be successful, the following considerations should be taken into account in defining target markets:

- resources should be focused on the countries that already attract the largest share of Italy's export;

[8] Italian Ministry of Economic Development, *Piano per la promozione straordinaria dell'export*, March 2015, http://www.sviluppoeconomico.gov.it/images/stories/commercio_internazionale/piano_straordinario_made_italy/piano_promozione_straordinaria.pdf.

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- export agencies and companies should try to identify in advance new markets with high long-term potential; and
- trade risks should be factored in when developing a national export strategy (notably possible fluctuations in exchange rates in the short-to-medium term).

In 2013, the Italian Government selected the US as a key target market. This decision proved correct in view of that country's sustained level of import. The latest figures confirm that the European single market and the US will continue to be the two main destination markets for Italian exporters. For this reason, the Transatlantic Trade and Investment Partnership (TTIP) currently being negotiated between the EU and the United States has an essential strategic value for Italy (and is more significant than the much-debated sanctions against Russia). Italy's export to the US has increased by almost a quarter since 2011 and the IMF forecasts that the US economy will continue to grow by about 5 percent per year in 2015-2018. Furthermore, export "quality" is as important as quantity. Europe and Italy's export to the US embodies a higher share of added value compared to export to other emerging economies.[9]

Among the BRICS, China is still a market with a high potential for Italy but it is more internal-demand oriented than in the past. Furthermore, the recent devaluation did not compensate for the long-term appreciation of the euro vis-à-vis the renminbi. Russia and Brazil remain important but strategically weak and volatile. Finally India seems to be a continent yet to be explored and understood.

4. The importance of TTIP for the future of Italian trade

In June 2013, US President Barack Obama and EU Commission President José Barroso announced the launching of formal negotiation for the TTIP. The treaty is set to transform commercial relations between Italy and its first non-European partner, and is thus of paramount relevance for Italy's international trade agenda. The TTIP is a comprehensive commercial partnership that addresses three key aspects: market access (tariffs and public procurement), regulation (non-tariff barriers to trade: health and safety, environmental standards, financial regulation, etc.) and trade rules (custom policy, provisions for state-owned enterprises, geographic indications, oil and gas export restrictions, etc.).

Some studies have indicated that the TTIP can have positive impact on Italy's growth performance and competitiveness.[10] In a very optimistic scenario the agreement could boost GDP by up to 0.48 percent (vs. only +0.02 percent in the most

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[9] Alessandro Giovannini and Umberto Marengo, "Boosting TTIP Negotiations: A Value Chain Approach", in *IAI Working Papers*, No. 15|18 (May 2015), http://www.iai.it/en/node/4226.

[10] E.g. Prometeia, *Stima degli impatti sull'economia italiana derivanti dall'accordo di libero scambio USA-UE*, June 2013, http://www.sviluppoeconomico.gov.it/images/stories/Articoli/TTIP%20Prometeia_rapporto_impatti%20economia%20italiana.pdf.

conservative scenario), increase export by 1.6 percent, and increase investments by 1.4 percent within three years of signing. The actual effects, however, will depend on the nitty-gritty of the deal, and the regulatory implications are difficult to forecast as they may vary significantly by sector.

The importance of the TTIP goes beyond the immediate effects of the agreement, though. The US is set to remain Italy's first strategic trade partner for the medium term. It is the largest, fastest growing and most open country of destination for Italian exports. Furthermore, as a global power, the US wields a significant influence on international trade negotiations at global and regional levels. Italy's value chains are already deeply interconnected with the US. As our country is already linked to (and interdependent with) the US, securing an agreement through the negotiating power of the EU will support Italian producers in setting the standards for the key bulk of products and services they export outside the EU.

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