

New Italian Government to be Formed — Again

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Contentious policy-making views between Italy's two coalition parties — right-wing, anti-immigration League and left-leaning Five Star Movement (M5S) — have persisted since the populist government formed over a year ago. League Deputy Prime Minister Matteo Salvini's move to quit the coalition in a bid to become Italy's new leader will be challenged by M5S co-Deputy PM Luigi Di Maio, wanting the same. With the resignation of Prime Minister Conte, President Mattarella has the sole authority to choose a new coalition or interim government. He can also call a snap election.

Mr. Salvini is advocating for the election process based on his rising popularity in Italy. If successful, he and coalition partners, right-centered Forza Italia and the Brothers of Italy, would establish right-wing leadership. A Salvini administration would most likely include a plan of aggressive tax cuts along with more public spending, counter to strict EU budget rules. We believe that more spending to lift the economy would not surmount the problem of Italy's ballooning debt and budget deficits.

The League is the overwhelming favorite in the polls, but Mr. Salvini could be opposed by a formidable coalition of M5S and the center-left Democratic party PD, which poses less drama. In addition, the M5S may propose to decrease spending. Along with a tax hike scheduled in January 2020, such a fiscal initiative could maintain the budget deficit at an acceptable level. This may be appealing to the president.

Italy's perennially divisive politics and sluggish economy have been a drag on the rest of Europe. Mr. Mattarella needs to ensure a 2020 budget is passed this year, though neither party may be the answer, especially for economic growth and government stability.

Italy's political morass will be fluid, as will the sovereign's standing in the world. Successful fiscal initiatives, through yet another government, continue to be a long-standing challenge for Italy and the EU. Italian volatility should not materially impact European financials fundamentals.

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