

Luiss
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Mapping Italy: scenario and political risks

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Italian politics has always been an arcane subject. A handful of specialists and enthusiasts love to talk of its Machiavellian intricacies for hours on end, but most people, especially north of the Alps, not only do not understand it, but see no reason why they should bother to understand it. Today there are at least three reasons why they should. First, in Italy the crisis of the political establishment that is now evident in many advanced democracies began a quarter century ago. This means that the country is further down the road of the democratic malaise – it is a laboratory and a bellwether. Second, Italy is the first country from within the historical core of the European community to be governed by anti-establishment parties. Third, its politics represent the greatest threat to the stability, or possibly even the existence, of the common European currency.

Founded in 2010 in a University that has a very strong international vocation, the Luiss School of Government aims to facilitate the connection between Italy and the world outside of it. It aims to prepare the future Italian public elite for the complexities of an ever more integrated planet, and to provide first-class education to non-Italian students in Italy's capital city. SoG professors have often helped non-Italian journalists and newspaper readers understand Italian politics. Thus, it seems only natural to me that the Luiss SoG should offer a monthly report on Italy that provides an interpretation of the country's recent political events, and makes an educated guess about what happens next.

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1.Scenario and risks

1.1. Politics

For the moment, the total lockdown established by the government to contain the diffusion of the pandemic and the healthcare emergency are deploying a hood on the Italian political debate. However, in the midst of the Coronavirus crisis, underground movements are shaking Italian politics.

Matteo Salvini, Matteo Renzi and Luigi Di Maio, for three different reasons, aim to unsaddle Giuseppe Conte. Salvini is working to return to the polls in 2021 and he hinted he is ready to accept a few months of transitional government to achieve his objective; Matteo Renzi, from the benches of the majority, aims to remove Conte, seeing him as a competitor for the occupation of the political centre that Renzi has the ambition to command; Luigi Di Maio wants to keep his control over the Five Star Movement and to limit the political rise of the Prime Minister as a potential leader of the Movement. In this scenario, last month have showed parallel convergences among the three leaders. Despite the patriotic rhetoric to face the crisis, it seems instability is growing within the majority.

Moreover, **the government is under pressure and in the first weeks of the crisis it mismanaged the containment of the crisis**, approving probably too late severe measures to avoid mass-scale contagion. Moreover, Palazzo Chigi suffered different leaks to the media on government's containment plans, an event which increased the level of panic and uncertainty among the Italian citizens. In this condition, the socio-economic consequences might be devastating for morale and the already weakened Italian economy. Impacts on stock market, tourism, trade and industry are already important and they will probably get worse in the next weeks. **Recession is taken for granted now.** An event which might led to a further weakening of the government. Many analysts are wondering **who will pay the price for the economic slowdown due to the sanitary emergency. It seems very plausible that Conte might become the person to be targeted by his allies, particularly by Renzi.** It is likely that the Prime Minister will come under attack for not doing enough, particularly in terms of economic measures. Indeed, some ministers underestimated the impact of the virus and in recent weeks they downplayed the potential effects of the illness on the Italian healthcare system and economy. In coming weeks, we will see if there were repercussions in terms of consensus. **Certainly, the Conte 2 Government was set up to maintain the status quo, not to face an emergency.**

1.2. Scenario

The way forward is becoming more complicated for the Italian Government. The coronavirus outbreak showed significant deficits in the Government's containment strategy and it produced tensions with the northern regions in managing the emergency. In terms of communication, during the first weeks of crisis, there was a lack of coordination and a poor chain of command. In the last days, Palazzo Chigi seems to have found a better framework with the regions and public administration to manage the emergency.

Moreover, while Conte is trying to stem the panic, rumours on the future of Government are on the increase in Rome. **Matteo Salvini and Matteo Renzi ruthlessly exploited the event to carry on a "parallel convergence"**. Renzi, after having called into question the role of Conte and the main reforms designed by the executive, sent a signal to Salvini by calling for "national unity" in the face of the virus outbreak and messaging publicly with League's governor of Lombardy. The former PM seems ready to leave the majority and he is the main concern for Conte's premiership at a political level.

In the last weeks, **Salvini stated clearly his availability to participate in a "national unity government" for a few months to manage the economic and sanitary crisis and then go back to the polls.** The League's leader needs elections to confirm his 30% share of votes and his leadership of the right-wing coalition, which is contested by the rising star of Giorgia Meloni (now polling around 13%).

Meanwhile, **the Five Star Movement is still in free fall in the polls (13-14%) and they are looking for new leadership.** Despite Luigi Di Maio stepping down as leader, he is always present at the Movement's public events, he is leading the campaign for the referendum to approve the constitutional amendment to reduce the number of parliamentary seats and, behind the scenes, he is trying to consolidate his control over a broad faction of the Five Star Movement. This is another element which might destabilize Conte, who is aspiring to lead a more moderate and centrist Movement.

The real stakes. Someone might wonder why Italian politics is always so frenetic. **The answer is that in a country with limited sovereignty, owing to its huge public debt, and strong external pressure due to EU rules and constraints, the role of the President of the Republic is essential.** The Presidential Palace on the Quirinal hill holds the residual national power, in terms of international relations, bargaining power with Brussels and safeguarding the Italian and European establishment. Mattarella will finish his mandate in two years and this deadline helps to explain the parliamentary turmoil of these months. Everybody wants to elect a President of the Republic who is sympathetic to their faction, because, as we saw with Napolitano and Mattarella, the Quirinale can really influence the composition of governments and foreign policy. Thus, for the right it is essential to overturn Conte and his majority, with a new government or with a snap election within the next year and a half (in the six months before the parliamentary election of the

new President a general election is forbidden by the Constitution). Renzi needs to consolidate his centrist position, without turning his back too much on the current government, exploiting the opportunity of being potentially fundamental for the election of the new President of the Republic in any case.

In this picture, **possible scenarios are becoming clearer:**

A) **Conte 2 goes on with the same majority.** It is difficult to predict how long, but the executive resists for the next months. The economic and healthcare crisis is too important to allow the overthrow of the government. Brussels allows enough new fiscal stimulus to overcome the crisis triggered by the outbreak and this flexibility is used to formulate new economic policies. Conte ties Renzi to the majority with some concessions on the Government's programme and the President of the Republic presses to maintain stability. Political parties, up to the next regional elections, choose to acquiesce. For now, this is the most likely scenario.

B) **Renzi-exit and the "responsabili".** Conte 2 survives but with a different majority. As soon as the entity of emergency decreased, Renzi's party leaves the Government and goes into opposition. The former PM might opt for opposition to gain more support in the polls. Meanwhile different groups of MPs unattached to parties (there are dozens in the Parliament) or without any possibility of getting re-elected join the majority and substitute Renzi and his MPs. This group of MPs in Italian political jargon are called "*responsabili*", responsible for keeping the legislature alive. In this case, the numbers of the majority would be very fragile and stability would be even weaker than today. The Government would be in limbo, without room for manoeuvre or to approve any significant reforms. The Government would not be dead, but in intensive therapy.

C) **Transitional government before snap elections.** In the next few months, majority collapses and the scenario moves toward a few months of transitional government. In this case there are two sub-options: **a) a national unity government**, with all the parties involved in it and led by a technical or impartial figure, it is formed to approve a new electoral law, particularly if the constitutional referendum of 29 March passes, and to draft the 2021 budget law; **b) a caretaker government** for a very few months in order to quickly return to the polls (e.g. from June to September), in this case the involvement of the President of the Republic will be stronger but shorter-lived. It would be a government with only one mission: bringing the legislature to an ordered end and going to snap elections. **We consider a) an implausible scenario for now**, too difficult to realise and to be used by Salvini to signal his sense of institutional responsibility in a crisis and a hook to seduce some Five Star MPs in the current majority, **while b) might be very likely** in case of a sudden collapse in order to reach snap elections in an organised way. However, **today this is not part of our baseline scenarios.**

1.3. Forecasts

Probability of snap elections:

Elections within 2020: **10%**

Elections within Q1 2021: **30%**

Elections after 2022: **60%**

The Conte 2 Government was set up to maintain the status quo, not to face an emergency. It was born for smooth sailing, not to weather a storm. However, **for now the most likely scenario remains the survival of the government and the legislature**. This does not imply that things might not change fast. For example, Renzi might force the precarious Five Star Movement to reshuffle the government as a condition for continuing the legislature. **He could lobby to increase his power in drafting a more centrist and pro-development (infrastructure and cutting labour taxes) agenda**. The PD as well, if the Five Star collapses at the regional elections in May (and it is probable), could push in this direction. **The balance of power within the government might change in favour of PD and Italia Viva**. This scenario is the most likely one and it might happen in the next months. Its realization will depend from the development of the pandemic.

This scenario, along with the emergencies of the coronavirus and the global economic slowdown, will determine a new government programme. The government is now under pressure and it has asked (and obtained) more flexibility from Brussels on its budget deficit. An emergency situation requires an extraordinary solution and next months will tell us if the combination between deficit spending and ECB loosened policy will be enough for the Italian economy. If not, a government crisis or a standoff with Bruxelles might come back at the center of the Italian political stage in the next months. How Conte manages the emergency in coming weeks will be fundamental for the future of the majority.

1.4. Mapping risks

There are three major risks at this moment concerning the Italian political system:

- **Coronavirus and recession**. It is evident that the Government mismanaged the healthcare system in facing the spread of the virus. In coming days, the price of this mismanagement will become clear, both in political and economic terms. According to experts, the virus' diffusion might continue for months. It could be a disaster for some sectors, such as tourism and agri-food. For the first time since the end of 2010 financial crisis, GDP will decline.
- **Rising probability of an "accident" within the majority**. The tension between Renzi and Conte is shaking the majority. By now, the most likely scenario is that the Government will go on with some adjustments. However, in the long run political stability is at risk. What will happen after the important vote of May in the regional elections if the Five Star has bad results (far below the ally of the PD)? The duration of the government should not be taken for granted. In this case, it is implausible that the Conte 2 Government will continue unchanged up to July 2021 (when the "*semestre*

bianco", 6 months in which it is not possible to vote because the Parliament has to elect a new President of the Republic, starts).

2. Public Opinion trends

2.1. Polls

The polls of February confirm the slight electoral decline of the League. Compared to January, the party led by Matteo Salvini lost one percentage point, now polling around 30.4%. Although this is just a slight decline over one month, it is worth noticing that the figure is consistent with a negative trend that started after the European Parliament elections of May 2019. **On that occasion the party got 34.3% of the votes and in the aftermath of the EP election (June 2019), the League polled around 36.2%. From June 2019, the performance of the party has steadily declined, a clue that the party performance might be going to stabilize around 30%.**

	Polls February	Polls January (2020)	Polls December	Polls October	Polls September	Polls June	EP elections (2019)	Polls March	Polls December	March 4 elections (2018)
League	30.4%	31.4%	32.4%	32.5%	32.4%	36.2%	34.3%	33.1%	32.9%	17.3%
Five Star	14.4%	15.5%	16.2%	18.7%	19.7%	18.0%	17.1%	21.3%	26.3%	32.7%
PD	20.8%	18.9%	18.6%	19.6%	20.9%	23.4%	22.7%	21.0%	17.6%	18.7%
FI	6.1%	6.7%	6.3%	6.8%	6.7%	7.4%	8.8%	9.6%	8.7%	13.9%
FDI	12.0%	11.1%	10.3%	8.0%	7.2%	6.7%	6.5%	4.5%	3.8%	4.4%
+EU	2.0%	2.1%	1.7%	1.9%	2.3%	2.8%	3.1%	2.9%	2.5%	2.6%
Italy Alive	3.9%	4.0%	4.9%	4.8%	4.6%					
Action	2.1%	2.2%	2.2%							
Left	2.7%									

Table 1: Electoral trends in recent surveys

The electoral trends observed in recent months are confirmed also for the other parties of the centre-right camp. The decline of Go Italy (FI) is by now a matter of fact: compared to January, the party lost other 0.6 percentage points.

On the contrary, **Brothers of Italy (FdI) continues to grow in the polls. Compared to the last month, the party gained one percentage point, polling now around 12%.** The positive trend for Giorgia Meloni's party confirms the attractiveness of FdI, which is by now the most direct challenger to Matteo Salvini in the race for the leadership of the centre-right coalition. The latter, despite the downward trend of FI and the League, would get 48.4% of the votes if elections were held today -a slightly lower result than that recorded in January, when the coalition polled around 49.2%.

As for the governing parties, only the Democratic Party (PD) recorded a positive electoral performance: an increase of almost two percentage points compared to last month, with overall 20.8% of the votes. This is an important result in the centre-left camp which confirms the significant attractiveness of the PD, potentially making the party the pivot of a possible coalition extending to other political parties.

If the electoral performance of the PD is encouraging, the **Five Star Movement (M5S) is struggling. Indeed, the negative trend of the last few months is confirmed. Compared to January, the M5S lost over one percentage point, stopping at 14.4% and remaining well below the electoral performance of the PD.** This is the lowest result for the Movement since the 2018 general elections. Finally, Matteo Renzi, leader of Italy Alive, falls below 4%. Despite the former prime minister's attempt to create a space of visibility for himself and his party, the party has so far failed to obtain an encouraging electoral performance in the polls.

2.2. The 2020 Constitutional Referendum and the optimal number of representatives

The confirmatory referendum on the constitutional law which modifies the Constitution to reduce the number of Italian parliamentarians from 945 to 600 will be held in the next months (it was programmed for 29th March but postponed for coronavirus emergency). Were the reform confirmed, the number of deputies in the lower house (i.e. the Chamber of Deputies) would decrease from 630 to 400, while the number of senators from 315 to 200 (with an overall number of Member of Parliament that will be equal to 400 deputies + 200 senators).

The reform has been at the centre of extensive discussions and many now believe that a reduction in the number of representatives in Parliament may negatively affect the quality of representation.

The problem of the optimal size of a representative assembly is not new and one of the most interesting contributions came from the political scientist Rein Taagepera. Taagepera approached the problem of the optimal dimensions of a representative assembly starting from a very simple point of view. The daily work of the parliamentarians mainly revolves around two functions: 1) to effectively represent the opinions of the citizens who have elected them; and 2) to work together with the other parliamentarians to reach policy outputs.

The two tasks become problematic when the number of social relationships to manage increases. Representing a district of 10,000 voters is easier than representing a district of one million voters. Therefore, on the basis of this criterion, the number of parliamentarians should be relatively high. However, making decisions in a 10-person assembly is undoubtedly faster and more efficient than in an assembly made up of 80 people; therefore, based on this criterion, we should have a low number of parliamentarians. As happens almost always in politics, there are two conflicting needs.

Taagepera addressed this problem in simple mathematical terms, looking for - given a population of a certain size- what number of parliamentarians offers the optimal level of representation, that is the one that minimizes (and therefore facilitates) the total number of social relationships (with both their voters and colleagues) that every parliamentarian has to manage. The solution he came up with is what is known as the cubic law of assembly size: if a population has dimension X , the optimal number of parliamentarians corresponds to the cubic root of X . This result, only apparently abstract, corresponds (net of an obvious margin of error, due to the specific characteristics of each country) to the actual size of representative assemblies in most countries of the world. Figure 1 shows it well.

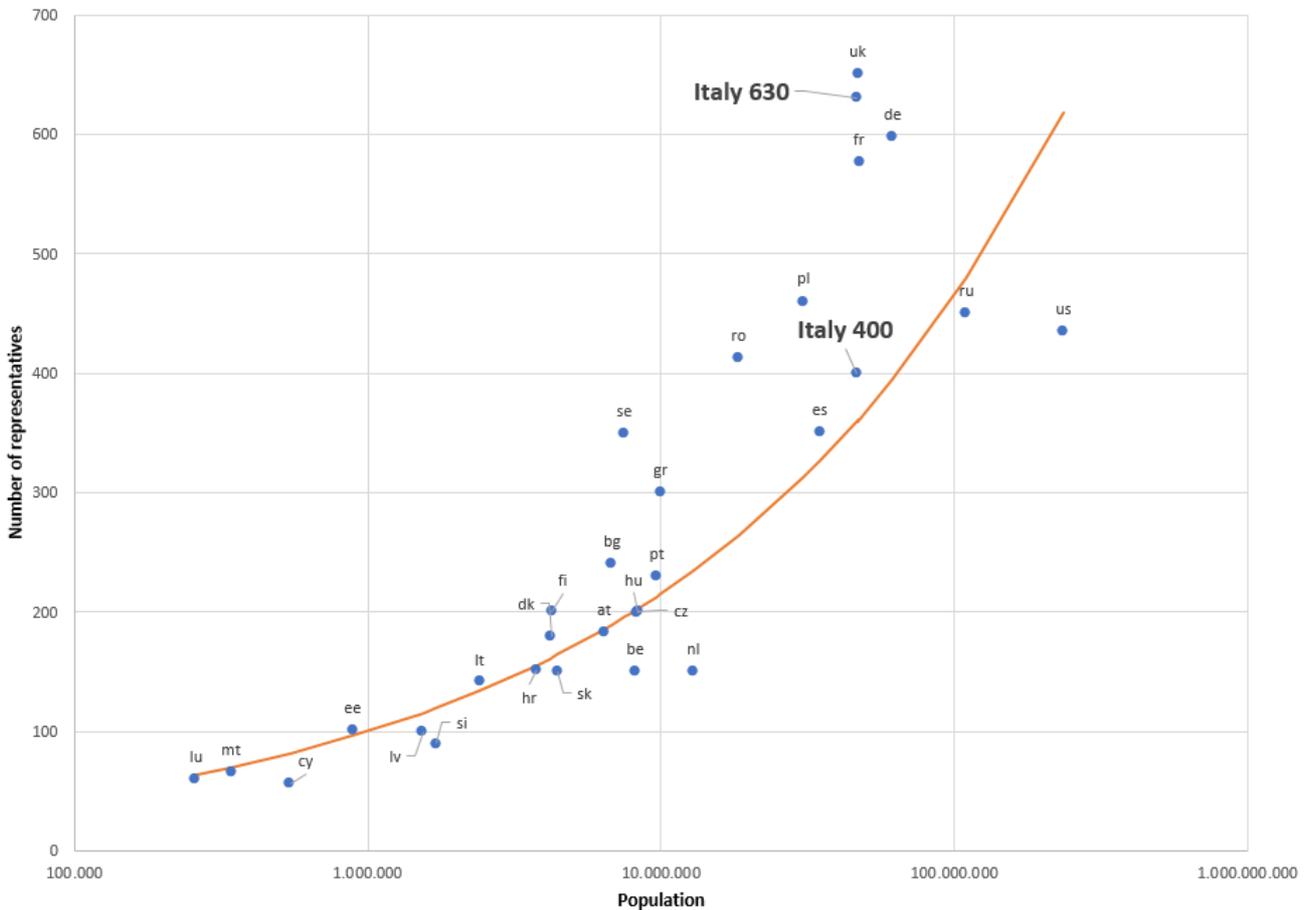


Figure 1: The Cube Root Law for Assembly Size

In particular, the figure shows the correspondence between the curve (the theoretical predicted size of assemblies according to the "cubic law") and the dots which represent the actual size of lower houses of the several countries.

Let's now try to see the application of the cubic law with a specific focus on Italy. We take as the reference population the overall number of voters, which in the 2018 Italian general elections was 46,505,350 (individuals aged under 18 are excluded). The cube root of this number is around 360 (that is, the ideal size of the assembly, according to the cubic law). Thus, the figure suggests that the constitutional reform goes in the right direction. In fact, if we consider the lower house alone, the number of 400 (envisioned by the reform) is clearly

closer to the cubic curve compared to the actual number of 630 (which is considerably higher, compared to the prediction based on the cubic law).

However, each country has its own historical, geographical, and social peculiarities, which lead some countries to deviate significantly from the "cubic law". Italy is a good case in point: basically, a heterogeneous country, whose unification occurred relatively late, in which there are still huge differences between different regions. If we take into account this diversity, the application of the cubic law produces different results.

For the sake of simplicity, we split the country in two halves (the North and the South) each made up *not* of 46,000,000 voters, but of 23 million each (a rough but effective way to incorporate the idea of a heterogeneous country). The cubic root of 23 million is 285. This means that if a "half country" of 23 million is optimally represented by 285 parliamentarians, the whole country (made up of two very different halves) would be optimally represented by 570 representatives, which is fairly close to the actual composition of the Chamber of Deputies (i.e. 630 deputies). Without taking this result as written in stone (however heterogeneous Italy is, it would be clearly absurd to argue that Italy is made up of two separate countries!), **what emerges from the analysis is that in the case of a particularly heterogeneous country, the optimal number of representatives could be higher than that predicted by the cubic law. Therefore, the real question is not whether 400 + 200 are too many or few, but instead: how heterogeneous Italy is.**

3. Economic Scenario

Due to increasing tensions brought by Covid-19 risks, **several policymakers have showed to be ready in supporting the economy. At the EU level, the European Central Bank has made clear that is ready to take ‘targeted’ action to address the economic impact of outbreak of coronavirus disease, whereas at the national level, the Italian government will soon ask the EU Commission a temporary deviation from the target deficit.** It consists of an additional 3.6 billion (0.2% of GDP) to cover extraordinary measures to support the sectors that suffer the most from the diffusion of the virus. In particular, the Italian government plan to increase the target deficit over GDP to 2.4% from the expected 2.2% for the current year. Moreover, at the beginning of March, ISTAT communicated the actual data on general government net borrowing, highlighting that in 2019 the deficit over GDP went down at 1.6%, with respect to the 2.2% of the budgetary plan, from the 2.2% of 2018. This was possible to higher tax revenues. **Concerning GDP growth for 2019, ISTAT revised the preliminary estimation of 0.2% to 0.3%, that does not change the slowdown with respect to the 0.8% of economic growth in 2018.**

For the current year, GDP forecasts accuracy will be strongly under scrutiny; in fact, the accuracy of macroeconomic dynamic forecasts is dubious since the virus trajectory is unknowable. **Notwithstanding, despite the positive, albeit small, forecasts for the current year economic growth, Covid-19 risks has furtherly pushed down the Italian outlook, with a resulting zero growth for 2020 as the best-case scenario.**

In January, in comparison with December, employment goes down by 0.2%, inactivity rose to, and unemployed people slightly grew (0.2%), whereas unemployment rate remains unchanged. Same dynamics are valid for cyclical variations (quarter on quarter), with employment that decreases by 0.1% and the number of unemployed increased by 0.3%, whereas the trend in the labour market reflects massive improvements, with employment that goes up by 0.3%, inactivity decreased by 0.4% and, more importantly, the number of unemployed that goes down by 6.2% with respect to the previous year.

The industrial production index shows high fluctuations for the first two months of the year. In fact, after the monthly increase of 1.9% in January, in February slipped by 0.5%. The negative outlook for future dynamics of the index are due to the drop in the demand for the tertiary sector and to Covid-19 risks.

Exports, after the negative performance at the end of 2019, maintains a positive trend (4.2% in December - yoy), with a greater contribution from extra-EU sales (5.9%). Despite a beginning of the new year with new trade uncertainty, the share of extra-EU sales continues

to contribute intensely (4.4% - yoy). Import continues to fall, especially for extra-EU countries.

Positive signals are coming from a decreasing spread, with yields on the BTP that went below 1%. This trend is common also to other countries in the Eurozone, with yields on government bonds that went down, but less than in Italy.

In general, **the conditions of the Italian economy will remain weak and, as confirmed by the confidence indicator, expectations of the operators are still geared to a widespread pessimism, with the aggregate consumer confidence index that goes down to 111.4 in February from 111.8 in January.** In detail, in decreasing order of intensity, the future climate goes down by 1.9 points, from 114.6 in January to 112.7 in February. The personal climate goes down by 0.6 points, from 108.4 to 107.8. The economic climate, with a drop of 0.4 points, flexes from 123.8 to 123.4. Finally, the current climate goes down by 0.1%, from 110.7 to 110.6.

With regard to the utilization of the economy's production factors, we report an increase of the business confidence climate index, from 99.2 in January to 99.8 in February. In detail, the confidence index increased marginally in the manufacturing sector, from 100 to 100.6, and rose from 106.6 to 107.6 in the retail trade sector. On the contrary, in market services the index is stabilizing at the previous month's value (99.4), while it dropped from 142.7 to 142.3 in construction. The scenario outlined by the PMI indices (Purchasing Managers Index) tends to reflect Italy's very fragile economic context. The manufacturing sector experienced new reductions in output and new orders. Overall, operating conditions in the sector deteriorated for a seventeenth consecutive month during February, with the PMI index that dropped from 48.9 in January to 48.7 in February. **According to the PMI index, the tertial sector is again expanding in February, with the quickest increase in business activity since last October. This was due to an increase in order book volumes at the fastest rate for four months, with the result of having higher job creation in the sector, and the PMI index that rose to 52.1 in February from 51.4 in January. Finally, with new orders expanded for the first time in four months, Italy's construction sector PMI index rose to 50.5 in February from 49 in January.**

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