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ITALY: HEADING FOR NEW ELECTIONS?

Berenberg Macro Flash

A new vote in 2019 - or 2018? Since the hung parliament election result on 4th March 2018, the leaders of Italy's major parties have been in talks to try to form a government. After President Sergio Mattarella's last ditch talks with party leaders failed to break the political stalemate on Monday, he proposed that a 'neutral' government should pass the 2019 budget and reform the election law this year, followed by new elections in early 2019. Anti-establishment 5Stars and right-wing Lega immediately rejected the proposal for a temporary-neutral government. As a result, the risk of new elections as early as 8th July now looms large.

What do the latest opinion polls show? The most recent data project further gains for Lega, in line with the Molise/Veneto regional vote in late April, but not enough for the centre-right/right alliance to win the majority of seats in both chambers of the parliament. The latest (average of the last 15 days) opinion polls – see chart - indicate:

- 1) Around 22.4% support for Lega, up 5 percentage points (ppt) compared to the March 4th election result - further increasing the lead over Silvio Berlusconi's centre-right Forza Italia (FI) party. FI would likely lose c. 2 ppt (to 12%). And overall, including the latest polls of the smaller alliance partners, the centre-right/right alliance would gain 2 ppt to 39%.
- 2) 5Stars performed well in the election compared to expectations, receiving 32.6% of the votes vs. 27.4% in the opinion polls ahead of the election. The party continued to gain momentum directly after the election, peaking at 34% support in mid-April, but has now slightly declined to 33%.
- 3) The centre-left Democratic party (PD) continues to lose support due to internal quarrels, declining by 1 ppt since the election to 17.7%. But opinion polls have to be taken with a pinch of salt, the March vote showed that polls were unreliable, underestimating the support for the radical parties.

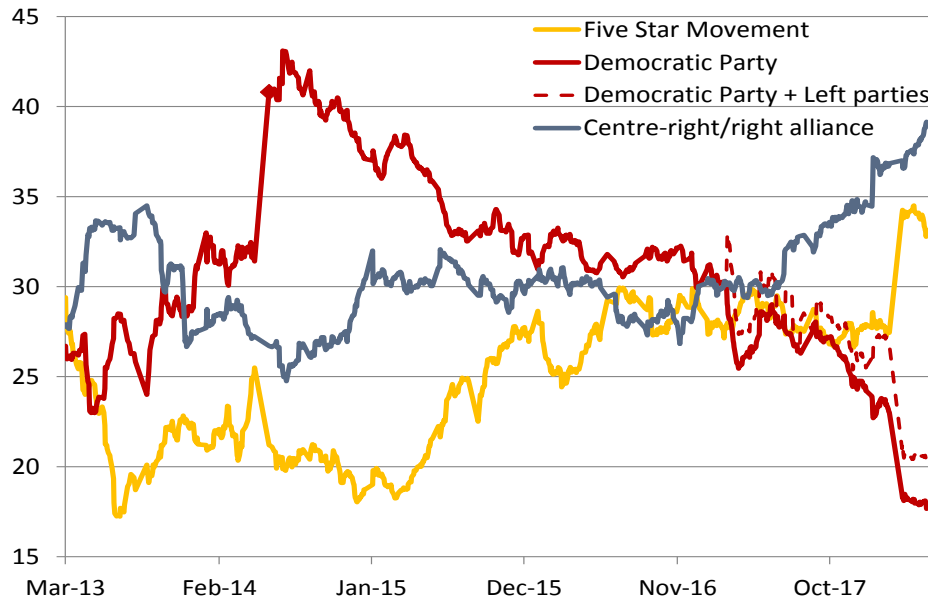
Key risks: Political uncertainty remains a drag on Italian investment and consumption growth. In Q1 2018, Italian GDP rose only by 0.3% qoq, one of the weakest results in the Eurozone. Meanwhile, the PMI Manufacturing index declined to 53.5 in April from 55.1 in March, the lowest level since January 2017. Furthermore, without a credible government, Italy will lose influence in the on-going discussion on [European reforms](#). A new election could further strengthen the radical parties that promised to reverse some of the recent [pro-growth reforms](#) - such as the 2011 pension and 2015 labour market reform.

Italian politics used to be our top risk in Europe before Trump's trade war threats turned into the new big risk. Although the tail risk of an Italian exit from the euro is not acute as before - radical parties have backed away from it - it is not zero. A lack of fiscal discipline and some reform reversals could sow the seeds of a new Italian crisis once the current cyclical upswing is over.



MACRO NEWS

Chart 1: Italy's centre-right/right alliance is gaining momentum



Centre-left Democratic Party (PD), Left parties include Popular Civic List (CP), More Europe (+E), PaP and Together (I), radical left Five Star Movement (Grillo), centre-right – right alliance includes Forza Italia (Berlusconi), ultra-right Lega Nord, Fratelli D'Italia and Us with Italy (Nci), average of polls over the last 15 days. Sources: National opinion polls, Wikipedia, Berenberg calculation.

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