



Holger Schmieding, Chief Economist | [Holger.schmieding@berenberg.com](mailto:Holger.schmieding@berenberg.com) | +44 20 3207 7889

## EUROPEAN POLITICAL UPDATE

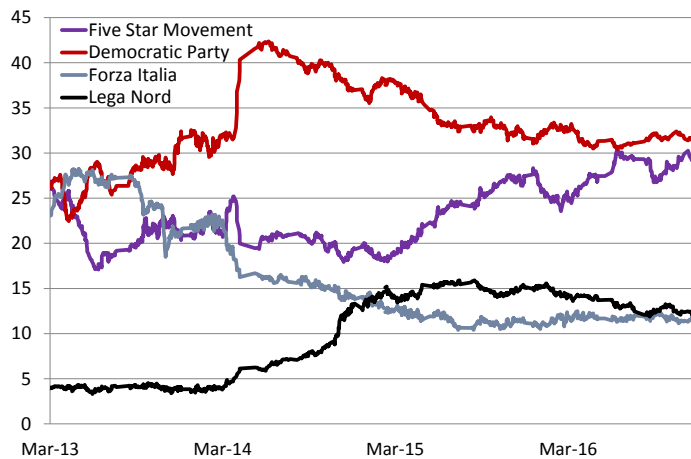
### Berenberg Macro Flash

Germany remains stable, France presents an opportunity, Italy poses a risk. The evidence so far this year strengthens some key conclusions of our [Global outlook 2017: more growth, more risks](#). The economic outlook seems to be almost boringly reassuring in the Eurozone, with the current concerns about a sudden snap-back in inflation as exaggerated as the deflation mania of early last year: oil price effects and not much beyond that. Instead, we need to keep our eyes on the politics.

#### ITALY: ANOTHER REFERENDUM?

Of the major Eurozone members, Italy poses the most significant political risk in 2017, as it did in 2016. Since the rise and fall of Berlusconi, Italy no longer has a strong and reliably responsible centre-right as an alternative to the governing centre-left. That makes the country more vulnerable to political risks than most other countries. In Italian opinion polls, the populist Five Stars are running a close second to the centre-left Democrats (see chart 1). After pro-reform prime minister Matteo Renzi stepped down in December when he lost a constitutional reform referendum, the risk that Italy may go to the polls ahead of the regular date in May 2018 has risen.

**Chart 1: Italian opinion polls**



Voting intentions in %. Source: various Italian opinion polls

Tomorrow, Italy's constitutional court could further complicate the political mix. After CGIL labour union had collected 3.3 million signatures for its demand to hold a referendum on Renzi's 2015 signature labour market reform, the court is scheduled to rule on 11 January whether such a referendum will have to be held, and when. The labour market reform introduced a sensible new labour contract with rising dismissal protection over time, removing one of the biggest obstacles to new hirings in Italy. If that reform was rejected in a referendum, it would undo the most important reform achievement of Renzi. It would dash hopes for firmer growth in Italy and further raise the risk of early new elections.

Italy is still far away from getting a Five Star-led government, in our view. The Five Stars are in serious disarray, as their weird attempt to join the staunchly pro-European liberal group ALDE in the European parliament has just demonstrated again. Also, the Italian constitution would not allow to hold a referen-



## MACRO NEWS

dum on an international treaty such as the one establishing the euro. The risk that Italy could vote itself out of the euro in the foreseeable future probably does not exceed 5%. But we need to watch Italian politics closely.

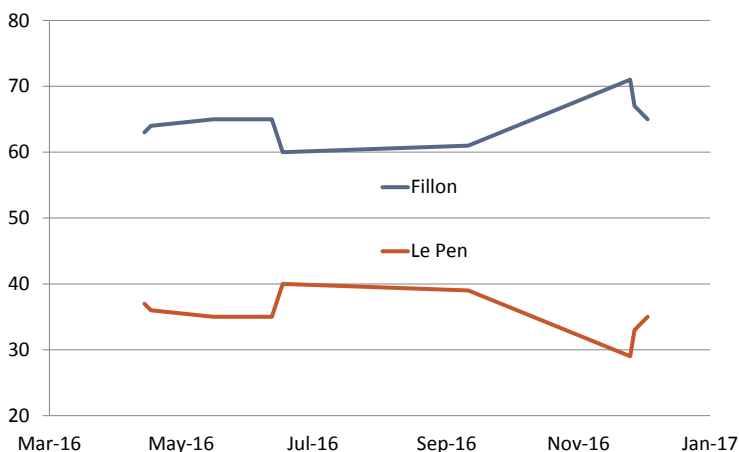
### FRANCE: AN OPPORTUNITY MORE THAN A RISK

After Brexit and Trump, the world worries about the tail risk of an upset victory for ultra-right Marine Le Pen in France. Rightly so, in a way. If she really took power with her plan to take France out of the euro, it could spell the end of the euro and the European Union as we know them. But that risk looks remote. The Trump comparison is somewhat misleading. Unlike Trump with his surprise novelty factor, she is more of a staid old politician who has been around for many years. In recent French elections, opinion polls did not systematically understate support for her Front National. Also, she would have to win the popular vote on 7 May 2017 – something which Trump did not in the US last November. And to do real damage, she would also have to get a majority in parliament for her Front National in the separate parliamentary elections on 11 and 18 June 2017. Never say never – but that really seems highly unlikely, with her party's support below 30% in the polls.

Opinion polls for the first round of presidential elections on 23 April show a three-way race between centre-right reformer Francois Fillon (around 25%), ultra-right Le Pen (around 23%) and centre-left reformer Emmanuel Macron (around 20%), who has the novelty factor on his side. It would take only a small swing in votes towards Macron to deny Le Pen a place in the second round of the presidential vote. Not our base case, but we won't rule it out. Although Macron is running as an independent, his chances to push out Le Pen in the first round will depend partly on whom the centre-left Socialists choose as their candidate in their primaries on 22 and 29 January. If pro-reform Manuel Valls wins, the chances of Macron would drop as Valls and Macron would compete for roughly the same voters in the first round.

For what remains the most likely pairing for the second round of the French presidential elections on 7 May, Fillon versus Le Pen, opinion polls still give a clear verdict (see chart 2). If Fillon or Macron win the presidency, they would have a mandate to finally overhaul the French labour market and turn France from Europe's biggest growth laggard into a German-style engine of growth. That would be the big opportunity for France – and Europe – this year.

**Chart 2: French opinion polls for second round of presidential elections**



Voting intentions in % for a Fillon-Le Pen run-off. Source: Various French opinion polls

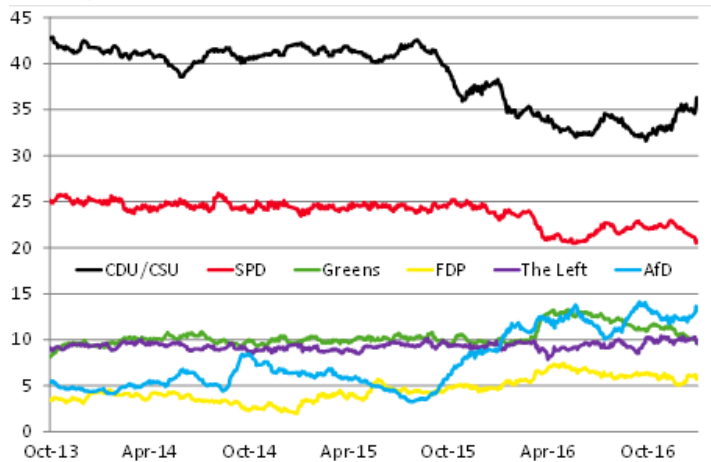


## MACRO NEWS

### GERMANY: ONE MORE TIME FOR MERKEL LIKELY

The only half-realistic alternative to a Merkel led-government after the German election - likely to be held on 24 September - would be a red-red-green alliance between centre-left SPD, ultra-left Left Party and Greens. On top of overcoming their serious policy differences, these three parties would jointly have to garner roughly 48% of the vote to win a majority of seats. Currently, they are trailing at 40.5% in the polls, with 21% for the SPD, and just below 10% each for the Greens and the Left Party (see chart 3). Of course, opinion polls are unreliable and events may still change the popular mood. But for these three groups to get up to 48% together would be a severe stretch. Note that the occasionally mentioned event risk – hypothetical terrorist atrocities – would probably not change that. Like migration policies, internal security issues are typically not strong points for left-of-centre parties. Recent opinion polls show that, in response to the horrific terror attack in Berlin on 19 December, a few voters apparently shifted to Merkel's centre-right CDU/CSU and to the ultra-right AfD instead. That would make it even more difficult for a hypothetical left-ist alliance to get the votes needed to unseat Merkel. Most likely, the real political question in Germany will be which kind of coalition Merkel will lead after the election, continuing with the SPD or teaming up with the Greens and/or the liberal FDP instead.

Chart 3: German opinion polls



Voting intentions in %. Average of last six polls. Source: Emnid, Forsa, GMS, Infratest Dimap, Allensbach, FGW

This message has been produced for information purposes for institutional investors or market professionals, it is not a financial analysis within the meaning of § 34b or § 31 of the German Securities Trading Act (Wertpapierhandelsgesetz), no investment advice or recommendation to buy financial instruments. The message does not claim completeness regarding the information on the developments referred to in it. On no account should it be regarded as a substitute for the recipient's procuring information for himself or exercising his own judgements. The message may include certain descriptions, statements, estimates, and conclusions underlining potential development based on assumptions, which may turn out to be incorrect. Berenberg and/or its employees accept no liability whatsoever for any direct or consequential loss or damages of any kind arising out of the use of this message or any part of its content. -- For full economics reports please visit our website or contact [capitalmarkets@berenberg.de](mailto:capitalmarkets@berenberg.de).

Joh. Berenberg, Gossler & Co. KG  
60 Threadneedle Street  
London EC2R 8HP  
Phone +44 20 3207 7878  
[www.berenberg.com](http://www.berenberg.com)  
[holger.schmieding@berenberg.com](mailto:holger.schmieding@berenberg.com)



**BERENBERG**

PARTNERSHIP SINCE 1590

# MACRO NEWS