Artículo

Public sector

Populism in Italy

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Almost three months after the elections, populism has reached the government of Italy with the coalition between the 5 Star Movement (M5S) and the Northern League (LN). The M5S, a left-wing populist party, won a huge victory in the south of the country, while the LN, a right-wing populist party, won in the richest regions in the north. These are two parties that have little in common besides being, each in its own way, anti-establishment.

Their victory is probably a response to public frustration at the results produced by the «system». The truth is that they have been rather disastrous: Italy's GDP per capita in 2018 is the same as it was in 1999, while public debt exceeds 130% of GDP despite primary fiscal surpluses (which exclude interest payments) being generated for the past 20 years (with the sole exception of 2009). No other country in Europe has had a comparable history of surpluses.

For a long time, Italy has descended into a spiral of low economic growth and high public debt from which it has not managed to escape. Even when it joined the euro area, Italy already had debt in excess of 110% of GDP. Since then, an average economic growth of just 0.5% per annum in real terms has been insufficient to reduce the bulk of the debt. The fundamental problem with the Italian economy is its inability to grow, and the main reason for this is the absence of reforms. Italy is an economy which is running against the tide of bureaucracy, the slowness of its judicial system, the poor quality of its educational system and the rigidities of its labour market.

Some thought that joining the euro area would help the country to push through the necessary reforms to improve productivity, but this has not been the case. In addition, the euro has made it impossible for Italy to resort to currency devaluations, which had helped to compensate for the loss of competitiveness in the country in the past. The results clearly illustrate that the inability to carry out reforms has a higher price within the single currency.

So, what now? The new government has promised to fight corruption, but apart from this measure, it does not have an agenda of structural reforms to drive economic growth. On the contrary, its priorities include a series of measures, such as the introduction of a guaranteed minimum income and cuts to personal income tax, with a fiscal cost that could cast serious doubts over the sustainability of Italy's public debt. Added to this is the uncertainty surrounding the government's commitment to the European project and the single currency.

To avoid a loss of investor confidence, which would trigger a surge in the risk premium and could close the financing markets for the Italian government, the coalition will have to avoid implementing a programme of extremes and adjust its promises instead. This might happen from the outset, or when faced with a possible rise in the risk premium. In any case, it would be risky for the government to explore the limits to which it can take its policy.

There are several reasons to believe that the government will avoid implementing policies that could trigger a debt crisis. Firstly, it is unlikely to do so for its own survival, given the harm this would cause to the Italian economy and to debt holders, mostly Italians. Secondly, it has a very narrow majority in the Senate, which may be insufficient to approve its proposed policies, depending on what they involve. Thirdly, the President of the Republic can veto a budget that flagrantly violates the constitutional mandate to ensure debt sustainability. Fourthly, and most importantly of all, the majority of Italians want to stay in the euro area.

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