

Conte 2.0, under the 5SM/PD flag

President Mattarella has mandated Giuseppe Conte to form a new government, backed by the 5SM/PD coalition. Formidable challenges lie ahead, but we expect less hostility towards Europe and a more constructive approach towards the budget. Growth policies, however, could potentially lead to conflict



Italian Prime Minister Giuseppe Conte (R) and Italian President Sergio Mattarella (L) during their meeting at the Quirinal Palace in Rome.

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The government crisis which ended the unconventional populist alliance between the anti-establishment Five Star Movement and the far-right League has seemingly found a solution after the centre-left Democratic Party and 5SM agreed to build a new government coalition led, again, by Giuseppe Conte, the outgoing prime minister.

But unlike in Spring 2018, it will be Conte himself managing the division of power between the two stakeholders and will try and strike a balance for a common programme.

President Mattarella will now give PM Conte a few days to work on the government programme and submit the proposed list of ministers. The new government will then have to undergo confidence votes in both branches of the parliament within ten days.

A common incentive to avoid early elections

The solution to the government crisis built on a common incentive for the 5SM and the PD party to avoid a snap election. The genesis of the 5SM/PD new coalition shows that this was contemplated on the PD front only under the assumption that the new government would aim at completing the legislature (which will end in March 2023). Incidentally, this time horizon would encompass the all-important election of the new Italian president in February 2022 when Mattarella's mandate ends.

Only time will tell if such a long time horizon would be possible.

A different role for PM Conte

In the new political setting, PM Conte is likely to play a different role in comparison to what he did in the outgoing League/5SM government.

If formerly he took office with an unprecedented notarial role, executing the inputs coming from the leaders of the League and of the 5SM, both acting as vice-PM, this time round he is likely to play a more conventional role of a prime minister. As the PM has been indicated by the 5SM, we don't think the scheme of the twin vice-PMs will be re-proposed.

Political divergences exist, but attitude towards Europe should be more constructive

The degree of cohesion of the new coalition is still unknown as both parties had fiercely opposed each other during the last campaign, and their differences remain. But where we do see ample room for improvement is in the relationship with European institutions.

Salvini's confrontational approach would have progressively isolated Italy in Europe, but the new political mix is likely to have a more constructive approach. The 5SM has progressively reneged on its anti-euro calls over the last year and voted in favour of Ursula Von der Leyen as the new president of the EU Commission, like the Democrats. The perceived risk of Italexit threats should clearly reduce under the Conte 2.0 government.

Less disruptive potential in the upcoming budget

But all of this will be tested quite soon in the budget season. Without an official government programme, it is very hard to draw any firm conclusions. However, the conciliatory approach adopted by Conte to European budgetary recommendations during his time in the former government, we believe this would be confirmed.

Cross-checking the lists of priorities spelt out by the 5SM leader Luigi Di Maio and PD leader Nicola Zingaretti, are quite vague, but nevertheless we see less scope for short-term budgetary disruption. There is no mention of costly tax cut exercises such as the introduction of a flat tax system, therefore we think it would be easier to craft a budget, not in collision with European budgetary rules. The lower cost of debt servicing associated with a reduced risk of 'Italexit' should in principle help subside the adjustment required.

Big challenges remain, particularly on growth

Having said that, the new government will still face formidable challenges, the first of which

will be to agree on pro-growth policies.

The Five Star Movement has so far failed to take a clear stance on this and recently reiterated their inclination to oppose big infrastructural projects, which may lead to conflict with the pro-growth Democrats. It will be up to PM Conte to distil a viable synthesis, as failing to do so could possibly widen the gap between the North and the South of the country.

To better decipher how difficult this will be, we will have to wait for the agreed government programme and, more practically the discussions over the next budget.

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