

Eurozone politics: A taste of what's to come

When it comes to politics this year, there are three countries to watch: Italy, the Netherlands and Germany. All three have dominated the headlines in the first weeks of the new year



The Statue Of David in the Piazza della Signoria In Italy Wearing Blue Protective Medical Face Mask

Source: Shutterstock

Politics, both at the national and European level, has always been an important factor for the eurozone economy, sometimes unexpectedly derailing an economic recovery but sometimes, as in 2020, actually supporting and accelerating it.

In the eyes of many international observers and financial market participants, the strong and relatively swift fiscal response to the pandemic was one of the positive developments of 2020. The agreement on a European Recovery fund, a departure from the previous principle of loans-based solidarity, has been a new milestone for eurozone integration.

However, experience has shown that new political obstacles are never far away. For 2021, the financial market's main focus will be on two national elections, in the Netherlands and Germany, while developments in Italy will also continue to attract attention. As long as the European Central Bank is fully exploiting its quantitative easing programme, there is very little risk of a severe calamity but European politics can always surprise. The first few weeks of the year have already

given some flavour of what's to come.

Italy: Centre stage again

In Italy, strong divisions over the management (and projected governance) of the forthcoming EU Recovery plan in the hands of Prime Minister Giuseppe Conte have created increasing tension within the government coalition alliance. Matteo Renzi, the leader of Italia Viva, a junior coalition party, has been by far the most vocal critic, focusing mainly on two key issues: the poor quality of the first draft of the Italian Recovery Plan and PM Conte's decision not to tap the available European Stability Mechanism's Covid facility in the midst of a health emergency. A revision to the Recovery Plan as suggested by critics and a late promise by PM Conte to begin a sanity check on the government's activity and consider a cabinet re-shuffle did not stop Renzi from withdrawing Italia Viva's parliamentary support for the government. PM Conte managed to avoid an outright crisis in parliament by winning confidence votes in both houses, but the thin simple majority obtained in the Senate left him in a weakened position.

PM Conte's attempt to find a sustainable majority, by looking to moderate pro-European MPs in the opposition ranks, proved unsuccessful. Faced with the growing risk of a parliamentary defeat, which would have severely reduced his chances of a new mandate, Conte decided to resign, a move endorsed by 5SM, the PD and Leu - the remaining partners in the government alliance after Renzi's departure. President Mattarella accepted his resignation, and asked him to stay on for ordinary business. President Mattarella will now run a round of consultations (possibly completed before the end of this week) before deciding if conditions exist for a new mandate.

We see three main options ahead.

- The first would be to seek a new mandate for a Conte 3.0 government with renewed support from Renzi's Italia Viva and the addition of some pro-European moderates from the opposition ranks.
- A possible alternative could be that of a national unity government with broader parliamentary support led by a technocrat. Moves in this direction have already been made by Silvio Berlusconi, the leader of Forza Italia, the pro-European moderate party in the opposition.
- The least likely option (but far from impossible) in our view, is that of snap elections "by accident", which would be hard to justify to the electorate during the height of a pandemic, and in view of the forthcoming Next Generation EU inflow of funds.

Germany: Slowly but surely preparing for the post-Merkel era

With federal elections scheduled for the end of September, the CDU is finally preparing for a post-Merkel era. After an often-postponed vote on the party leadership, Armin Laschet, currently minister-president of NorthRhine Westfalia, became chairman of the CDU in mid-January. While normally, the chairman of the CDU is also the designated candidate to lead the party into federal elections, this race has not yet been decided. In our view, it will either be Armin Laschet or the minister-president of the Bavarian CSU, Markus Soeder, who will take pole position. A date for this decision has not been announced, yet.

Two influential events on the road to the federal elections, and the CDU/CSU's ultimate leadership, are the regional state elections in Baden-Wuerttemberg and Rhineland Palatinate, both on 14 March. In Baden-Wuerttemberg, attention will focus on whether the incumbent minister-president

Winfried Kretschmann from the Green party remains in office, while in Rhineland Palatinate, the test will be whether the Labour Party can reconfirm its minister-president Malu Dreyer. These votes will be important barometers for whether the Greens are still strong candidates to join the next federal government and whether the Labour Party can stop its decline of recent years. They will also provide some insight into the popularity of the new CDU chairman, which will indirectly decide the CDU/CSU's candidacy for the federal elections. This would not be the first time that federal elections have already been largely decided by the regional elections in spring.

Netherlands: Stepping down but still in charge

On 15 January, the Dutch government resigned because of the so called “day-care allowance affair”, in which the government unjustly treated thousands of households as fraudulent. This led to the resignation of the minister of Economic Affairs and Climate, Eric Wiebes (member of VVD), who was the undersecretary of Finance in the earlier government. Two other major political parties, the Christian-democrats CDA and the Labour Party PvdA, have also seen unexpected changes in political leadership in recent weeks. The CDA will now be led into the elections by current finance minister Wobke Hoekstra and the PvdA will be led by Lilianne Ploumen, minister for Development Aid in a previous government.

Given that the next national elections had already been planned for 17 March, the Rutte government will continue as a caretaking government, with limited consequences for urgent policies and the economy. The ongoing business of the parliamentary commission on European Affairs for instance, including Brexit, has all been deemed “non-controversial” so far. Several opposition parties have already stated that they would allow the government ample room to continue to manage the Covid-19 crisis. Indeed, it is not altogether unusual for a government in the Netherlands to step down weeks ahead of planned elections. The House of Representatives has, however, deemed the opening of Lelystad Airport (intended for November 2021) to be one of the controversial policies, likely meaning that the opening will be postponed for a fifth time.

Speculative polls suggest that the early end of the Rutte III government has led to only minor shifts in support for the parties involved and that the coalition parties still have the support of the majority of the population. However, a lot can happen in Dutch politics in the final weeks of the campaign.

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