

Italy: Confidence still soft in February

Soft confidence looks consistent with another contraction in GDP in 1Q19. The (lack of) growth theme looks set to become increasingly important in the local political debate, currently still dominated by the consequences of the poor performance of the 5SM in two recent regional elections



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Confidence data consistent with recession in 1Q19

February confidence data, released earlier today by Istat, points to a continuation of the Italian economic recession. Consumer confidence fell to 112.4 (from 113.9), an 18-month low, and the composite business confidence was down to 98.3 (from 99.1 in January), the lowest level since March 2015. The sector split shows that confidence fell slightly in manufacturing and services, and much more heavily in construction, while it rebounded substantially among retailers. A quick look at the forward-looking part of the report in the manufacturing domain shows that order books remain under pressure, more markedly in the intermediate and the investment goods sectors, and that judgments on inventories are picking up. This is not the best omen for a production recovery in the short run. In the service domain, the steep fall in both confidence and orders in the transport and stocking sector is in stark contrast with a strong recovery in the tourism sector.

All in all, today's release points to a continuation of the soft patch for the Italian economy, supporting our view that 1Q19 will see another quarterly contraction for Italian GDP (we anticipate a -0.1% quarter-on-quarter). The recession theme will likely become more central in the domestic

political debate, which is currently concentrating on the impact of recent local elections.

Poor regional election score puts pressure on 5SM

The recent regional election rounds in Abruzzo and Sardinia highlighted once more the peculiarity of the current political scene in Italy, where the current government alliance is not replicated at the local level. In both cases, the League was running in coalition with the rest of the centre right and with so-called “civic lists”, while the 5SM was running in isolation. In both cases, the League-driven centre right scored a neat victory and the 5SM a dramatic fall compared to the national legislative election of March 2018. In both regional votes, a united centre-left scored decently, at least managing to stem the decline.

In the aftermath of the votes, tensions rose in the 5SM, with the leadership of Luigi Di Maio under attack from the leftist part of the movement. It might well be that the 5SM has paid a price for having reneged on many of its hallmark pledges to align with the League and keep alive the contract-based alliance in the national government.

Growth-related issues are expected to take centre stage soon

We do not believe that growing tensions within the 5SM will increase the risk of a government crisis before the European elections. In the very short run, it seems likely that, for the sake of the alliance, Salvini will give more visibility (and parliamentary leeway) to some of the themes that are important to the historic 5SM strongholds. However, given the poor economic backdrop, a re-focusing on growth related issues will soon become essential, the obvious starting point being the starting of frozen infrastructure investment plans. Prime Minister Giuseppe Conte is taking initiatives in this direction, possibly to include at least part of this in the Economic and Financial Document (the DEF, which sets the macro framework for the next budget), to be disclosed in April. The controversial issue of the TAV project, temporarily swept under the rug, could be suddenly resurrected, eventually complicating things.

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