

## Italy: Risk of a government crisis rapidly increasing

The approval of the Recovery and Resilience Plan by the government cabinet overnight could not iron out tensions between former Prime Minister Matteo Renzi and current PM Giuseppe Conte. Renzi, a coalition partner, might soon decide to withdraw support for the government, with no obvious new base case, at this stage



### Rising political tensions on crucial EU funds matters

Over the last few weeks, Matteo Renzi, the leader of Italia Viva, a coalition partner in the current ruling alliance, has been putting increasing pressure on PM Conte on a series of relevant issues. At first, criticisms focused on the proposed governance of the Next Generation EU funds (too centralised and with little involvement of affected ministries, in Renzi's view), but soon extended to the architecture of the draft Recovery and Resilience Plan (too little money on health, education and innovation, according to Renzi, and not enough drive to use it to fund only incremental investments) and on Conte's decision not to tap the Covid ESM facility (Renzi has long highlighted the opportunity to tap it). In addition, Renzi has been calling on PM Conte to delegate control of the Secret Services.

## Revised RRP was approved last night in a dedicated cabinet meeting

Renzi's requests have recently been accompanied by the threat to withdraw his support from the current government in the absence of a proper response from PM Conte. Among rising tensions, PM Conte's response materialised late on Monday in a revised RRP draft, incorporating a good deal of the amendments that Renzi (and, less vocally, the PD party) had solicited. The proposal, which does not tackle the tricky issue of the governance of Next Generation EU funds, nor that of the use of the Covid ESM facility, was examined last night by the government in a dedicated cabinet for approval. The scheduling was very likely chosen in order to isolate the trajectory of the Recovery and Resilience Plan from that of the government. The new draft RRP was approved by the government cabinet, but the two ministers from Italia Viva abstained. It will now need parliamentary approval, which is expected to come after a debate which will also have to deal with the accompanying reforms needed.

## Risk of a government crisis has now increased

Last night's developments suggest that the revised RRP offer was not enough to iron out the other points of contrast between Renzi and PM Conte and point to an increased risk of an imminent government crisis. True, the two Italia Viva ministers did not resign after the cabinet meeting, but they might very soon, possibly today. Last night, in a televised talk show, Renzi announced that the ministers would speak today during a press conference to be organised late in the afternoon at the House of Deputies.

## Simple cabinet reshuffle has become a very shaky base case...

The solution of a cabinet reshuffle after a coalition check-up remains a possibility, in our view, but it has become a very shaky base case. The residual viability of this orderly solution will crucially depend on whether Renzi would accept a continuation of the current (reshuffled) government led by Conte without passing through a flash resignation and a new mandate by President Sergio Mattarella. Based on yesterday's developments in the domestic political debate, this seems increasingly unlikely. Also, top officials from the 5SM and PM Conte's entourage stated yesterday that should Renzi withdraw his ministers, there would be no possibility of a future government alliance involving Renzi's party. This may have been a signal that an alternative majority was being sought in parliament.

## ...while a substitution of Renzi's support in the Parliament seems increasingly likely

Indeed, should Renzi decide to withdraw his support, PM Conte might be tempted to look for alternative backing, presumably from the ranks of the mixed parliamentary group or from centrists now in opposition. If successful, this attempt would likely yield at the Senate an extremely thin, and possibly even patchier majority. Would President Mattarella accept a solution offering scarce guarantees of stability? Definitely a possible solution, but hardly a reliable new base case, at this stage.

## National unity government also a possible solution

Should both the above mentioned possible outcomes fail to materialise, we would expect President

Mattarella to explore the possibility of having a “national unity” government (with ample parliamentary support) led by a technocrat with the core mission of implementing the reforms and the investment projects foreseen by the RRP until the end of the current legislature (expiring in the spring of 2023). The chances of this outcome are also going up, in our view.

## Early election remains unlikely, in our view

A last possible outcome for a government crisis could be an “early election by accident”. Markets have been dismissing this so far and we continue to believe that a snap election remains an unlikely outcome, but it cannot be ruled out. Based on current opinion polls, which show a clear lead for the right-centre block, we believe it would be political suicide for most members of the current majority to go for elections. As an additional disincentive, after the recent constitutional reform, the next election will install a downsized parliament and many current MPs would have a very small chance of re-election. Even those who in principle could benefit from an early vote, the League and Fratelli d'Italia, might be not so eager, as the vote would likely cause a late start with a handicap for the implementation of the Recovery plan.

In sum, the political picture has become very complicated. Over the next few hours we expect President Mattarella to exert his moral suasion and late this afternoon, we might know whether Renzi will indeed leave the coalition. Understanding which solution will eventually materialise might take some time.

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