

Europe



Italy and the G8 summit

A cavalier preparing to host the world

ROME
The host of the G8 summit, Silvio Berlusconi, faces many lurid scandals at home. But the biggest should be his refusal to accept the extent of Italy's economic woes

WHEN the leaders of the world's largest economies meet on July 8th near the Italian city of L'Aquila for this year's G8 summit, they will find themselves in an apposite setting. Three months ago L'Aquila was hit by an earthquake that left 300 people dead and much of the city centre in ruins. The area is still experiencing powerful aftershocks: on June 22nd there was yet another one.

It might be imagined that none of the assembled leaders would deny that their economies have also been shaken to their foundations. But one does: the host. Italy's prime minister, Silvio Berlusconi, has from the outset insisted that in Italy the recession will be neither as severe nor as prolonged as elsewhere.

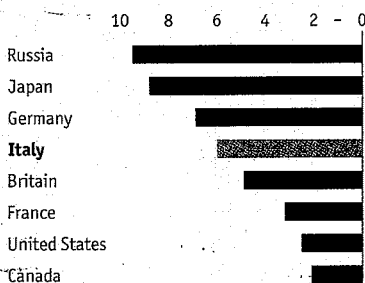
At first, this view had some credibility. With a banking system leery of derivatives and relatively isolated from the rest of the world, Italy did not suffer disaster of the sort that brought financial institutions crashing to the ground in America and Britain. But analysts have since given progressively greater weight to other considerations. The Italian economy is highly dependent on exports (partly because of weak domestic demand) and so exposed to a decline in world trade. What is more, the public debt is huge (worth well over 100% of GDP), so the government has little scope to copy others in borrowing for costly stimulus measures. An "anti-crisis" package unveiled by Mr Berlusconi on June 26th was unhelpfully modest: its

main provision was a 12-month, 50% tax break on reinvested profits.

In recent weeks, respected organisations inside and outside Italy have lowered expectations for the economy, predicting not merely a savage recession, but at best a fragile recovery in 2010. The European Commission and the International Monetary Fund both now estimate that in 2009 Italy's GDP will shrink by 4.4%. The Bank of Italy and the employers' association, Confindustria, have plumped for 4.9%. And in the most recent gloomy analysis, the OECD on June 24th put the likely shrinkage of the economy this year at 5.5%. True, three other G8 countries are doing worse still (see chart). But the notion that Italy, which has a 20-year history of under-performance, will miss the full impact of

Hard times

GDP, Q1 2009, % fall on previous year



Source: Thomson Datastream

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the recession is fanciful.

The OECD survey, in particular, clearly embarrassed Mr Berlusconi. He responded this week angrily that it was time to "shut the mouths" of those who spoke of "crisis here and crisis there". He also suggested that companies should withdraw advertising from newspapers that spread gloom (even though his own finance ministry had in May quietly altered its own estimate of the fall in GDP to 4.2%).

In Italy appearance and reality seldom coincide. Many economists and businesspeople assume that, as so often, Mr Berlusconi's provocative rhetoric masks a subtler purpose. "I think that [Berlusconi and his finance minister, Giulio Tremonti] are most afraid of a drop in internal consumption and are trying to drive it up," says Michele Tronconi, president of the fashion industry's trade body, Sistema Moda Italia. Mr Berlusconi has all but admitted as much. "We need to try to revive consumption. People should go back to their previous lifestyles," he declared recently.

Yet if the plan is indeed to compensate for the loss of exports by hoodwinking the Italian consumer into spending more, it is a risky one, for both Italy's government and for the country. Mr Berlusconi already has a credibility problem at home over his private life, having refused to make good his pledge to explain to parliament his relationship with an 18-year-old aspiring model. He is now having to put up with a raft of stories about call-girls being entertained at his home in Rome. He can ill afford to have his claims about the health of the economy contradicted by the evidence of voters' own eyes and ears.

Mr Tronconi, who backs the government's optimism offensive, acknowledges that "my experience is of a crisis that is biting very hard". He heads a small, family-owned textile finishing company and output in his sector was down "nearly 30%" ▶▶

▷ compared with 12 months ago.

Fabio Pammolli of CERM, an economics think-tank, notes that "being a country with a very fragmented economy, made up of small businesses, the moment at which the recession becomes visible is delayed. The collapse of thousands of micro-enterprises does not make the front pages in the same way as the bankruptcy of a Chrysler or General Motors." But it does show up in the figures. Istat, the government statistical office, says that 204,000 jobs were lost in the first quarter of 2009. In April industrial production was down

by 22% and orders by 32% on a year earlier.

By insisting that nothing is amiss, Mr Berlusconi and Mr Tremonti are also passing up an opportunity to embark on reforms that would not only speed the economy's recovery but actually improve Italy's productivity and public finances. Confindustria is pressing the government for more reform of the unsustainable pension system (Italy spends 13% of GDP on the elderly, almost four percentage points more than the average for the EU 15 richer economies). And it wants a programme of liberalisation and privatisation to promote

competition, increase productivity and cut consumer-price inflation. A recent Bank of Italy study concluded that in three years such a programme could boost Italy's GDP by as much as 5%.

Since it returned to office last year, however, the Berlusconi government has become wary of free-market ideas. Guided by Mr Tremonti, author of a book foreshadowing the credit crunch, the government has embraced Sarkozyite ambiguity. It has no programme for deregulation or asset sales. It is not prepared even to raise the retirement age for women. Ministers have hinted that they fear courting unpopularity at an already delicate juncture.

It might be possible to steer through pension reforms and take on the vested interests opposed to liberalisation and privatisation if it were done in the name of national belt-tightening. Italians responded heroically in the mid-1990s when the then prime minister, Romano Prodi, called for sacrifices to clean up the national accounts to prepare for euro membership.

Yet although Mr Berlusconi may survive the scandals that have engulfed him, he can scarcely appeal to voters for blood, sweat and tears so long as he insists that Italy has emerged almost unscathed from the world's economic meltdown—rather as the barracks in which the G8 summit is being held weathered the earthquake. ■