



The Italian Political Crisis

On 1 August 2013, Italy's highest court of appeals confirmed a four-year custodial sentence that the lower courts imposed on former Prime Minister Silvio Berlusconi as a result of his conviction on charges of tax fraud dating back to the 1990s. The high court also instructed the lower courts to recalculate how long Mr Berlusconi should be barred from public office. This process should take approximate six to eight months. In the meantime, Mr Berlusconi may hold onto his seat in the Italian Senate and he may even stand for election as leader of the largest center-right political party, the People of Liberty (PdL). Nevertheless, he may lose his parliamentary immunity and he must choose to serve the one year that remains of his four-year custodial sentence either in house arrest or doing community service.

The high court's decision has thrown Italy into political turmoil. Berlusconi's supporters on the center-right charge that the judiciary is trying to undermine Italian democracy, they insist that Berlusconi is innocent of all charges, they have put pressure on Italian President Giorgio Napolitano to find some way to protect Berlusconi from the courts, and they have demanded that Italian Prime Minister Enrico Letta move judicial reform to the top of his legislative agenda. Berlusconi's critics from other parts of the spectrum insist that justice has been done, they point to the many other trials in which Berlusconi is involved – for bribery, corruption, and underage prostitution – that are working through the courts, and they argue that a politician facing similar charges in any other country would have stepped down long ago.

The problem is that Berlusconi's political party is an essential part of Prime Minister Letta's ruling coalition. Worse, that coalition brings Berlusconi's supporters together with their historic rivals on the center-left, many of whom are openly resentful of having to do business with Berlusconi and would rather face new elections instead. Alas, new elections are not a serious alternative because they are unlikely to result in a decisive outcome for any of the major political groups and because neither Italian financial markets nor the country's 'real' economy or manufacturing and services can withstand another bout of political uncertainty. Italian politics is at an impasse. It can neither engage in business as usual nor move decisively toward a superior alternative.

The purpose of this brief is to explain how this situation came about. The analysis has five parts. The first sets the stage by introducing the main political parties and institutions. The second looks at the impact of the economic and financial crisis. The third focuses on the current coalition. The fourth returns to the present and sketches possible outcomes.

Italian Democracy

Politics is complicated everywhere and Italy is no exception. Indeed, many observers complain that Italy is more complicated than most places. That may be true. But that does not mean analysts need to appreciate every complex element of Italian political life in order to explain the most important problems facing modern Italy. On the contrary, most of Italy's current problems revolve around three elements – the divided structure of Italian political institutions, the fragmented nature of the party system, and the perverse incentives created by Italian electoral laws.

Italy's political institutions are the best place to start because they are deceptively familiar. Italy emerged from the Second World War with deep divisions between different parts of the country (meaning north and south) and different ideological groups (communist and socialist left, fascist right, and Catholic center). Hence the Italian constitution gives equal importance to the representation of the country's historic regions in the Senate and its political traditions in the Chamber of Deputies. Where legislation is concerned, the two houses have equal power. This legislative structure mostly mirrors that of the United States. But there is one important difference: where the United States has a President who is independent of the legislative branch, Italy is a parliamentary democracy and the President of the Council of Ministers (or Prime Minister) must have the support of majorities in both houses. Barack Obama can govern (albeit with difficulty) despite a Republican majority in the House; Enrico Letta cannot remain Prime Minister if he loses the confidence of either the Senate or the Chamber of Deputies.

The confidence of the legislature requires a majority vote of the members of each chamber. According to the Italian constitution, these members should be allowed to vote according to their conscience. This is another historic legacy. It is related in part to the influence of both the Communist Party and the Catholic Church. The Italian Republic should not act at the command of Moscow or Rome. It is also a theory of representation. Italian legislators are not the delegates of the electorate; they are the trustees of the popular will. Members of Parliament should not wait to be told how to vote; they should vote for what is right. Most important, this notion that representatives should vote their conscience is a reflection of the many informal patron-client relationships that have long been a feature of Italian political life. Although political parties have played an important role in shaping Italian democracy, the currents or factions within political parties have been equally if not more influential.

The period when the Christian Democratic Party (DC) governed the country immediately after the Second World War is a good illustration. Although the often DC controlled both the Senate and the Chamber of Deputies, the government fell approximately once a year. The explanation lies in the competition between groups within the DC rather than conflict between the DC and other political parties. Moreover, the Christian Democrats were not alone in suffering from internal divisions. The difference for other parts of the political spectrum – like the non-communist left – is that these divisions crystallized in the

formation of smaller political parties that often centered on single individuals. This was true particularly as the decline of religious devotion sapped support from the Christian Democrats. Hence when the DC governed in the 1980s, it did so in coalition with four other parties.

The disgrace of the Italian political class in the corruption and mafia-related scandals of the early 1990s created an opportunity to bring more coherence to Italian democracy. The belief at the time was that the fragmentation of the party system was the result of the proportional electoral process. So long as political groups could gain representation in either the Senate or the Chamber of Deputies by capturing only a small share of the electorate, the incentives for large fractious political groups to break down into small parties dominated by individuals would remain a problem. By contrast, a first-past-the-post or plurality electoral system – where individuals gain representation by winning the most votes in a single district – would force politicians to organize into larger cohesive groups on the right and on the left. Individuals and individual conflicts might still play an important part in the political dynamics, but only large political parties would win elections.

This theory underpinned the introduction of a new electoral system in the early 1990s that relied primarily on plurality style elections in single-member districts but with some proportional representation at the margins. Three different kinds of political movements emerged as a consequence. There were smaller, regionally concentrated or ideologically motivated political groups that took advantage of the remaining proportional seats in order to remain active in parliamentary life. There was a populist political movement created by Silvio Berlusconi on the center right. And there was a coalition of diverse political groupings that ranged from former Christian Democrats at the center to former Communists on the left that was forged by Romano Prodi.

The smaller political groups represent the most continuity with the past – even when they formed around new issues, like the separatist Northern League. Berlusconi's populist movement was the greatest innovation because it combined Berlusconi's great wealth and media savvy to form a personalized political grouping on an unprecedented scale. Prodi's coalition falls somewhere in between because it included small political groups and diverse political factions in an overarching common framework.

In the contest between these groups, Berlusconi managed to show greater unity when he came to power and Prodi tended to suffer more from in-fighting within his coalition. By the same token, the center-right could not win without Berlusconi and yet the center-left could govern without Prodi. Meanwhile, the smaller groups could influence the balance of power between center-right and center-left – helping either Berlusconi or Prodi to come to power.

This alternation explains why Berlusconi decided to change the electoral rules in 2005. Berlusconi had been in power since 2001; he managed to sustain a single government throughout almost the entirety of his parliamentary mandate; yet, he faced conflict with

his coalition partners in the Northern League and he lost support among the electorate. To stem these losses, the Berlusconi government introduced a new electoral system that would replace single-member districts with proportional elections. He also introduced a majority bonus. Whichever political group wins the most votes at the national level gets 55 percent of the seats in the Chamber of Deputies; and, whichever political group wins the most votes at the regional level gets 55 percent of that region's representatives in the Senate.

This new electoral system placed emphasis on the divided nature of Italian political institutions by introducing different formulas for calculating the majority in the Chamber of Deputies and in the Senate. It reinforced the incentives to fracture the party system by returning to proportional representation. And, for Berlusconi at least, it had the desired effect of making it harder for Prodi to hold together a coalition on the center-left than it would be for Berlusconi to finance and mobilize a personal political movement of unprecedented size. In the 2006 elections, Prodi won an outright majority in the Chamber of Deputies by getting the largest vote share across the country; but he failed to win a majority in the Senate because his center-left coalition was edged out by Berlusconi and his allies on the center right in many of the most populous regions of the country. Prodi's control over the Senate finally collapsed in 2008 and Berlusconi pushed for new elections which he won outright in both Chambers.

Italy and the Crisis

The Berlusconi government that came into office in 2008 was more stable than the Prodi government that it replaced. Nevertheless, it suffered from significant divisions. Most of these related to the competition between those who wanted to inherit Berlusconi's mantle once he finally stepped down from office. Gianfranco Fini brought his once neo-Fascist national alliance party into Berlusconi's movement in order to put himself into the line of succession. Meanwhile, Finance Minister Giulio Tremonti tried to position himself as an intellectual leader and an essential bridge to Berlusconi's coalition partners in the Northern League. Both moves challenged Berlusconi's leadership implicitly even if neither Fini nor Tremonti was ready (nor able) to push Berlusconi out of office and take over the reins of power.

Such fissures are normal in any large political movement where individuals are constantly jockeying for power and influence. In themselves, they were nothing Berlusconi could not handle. If anything, Berlusconi was his own worst enemy. His relationships with younger women became a minor scandal in 2009 that ended his marriage. Berlusconi's team was able to contain the initial revelations but Berlusconi was slow to change his behavior and to recognize the potential political danger that such liaisons entailed. This gave Fini the opening to pull his group out of Berlusconi's movement in 2010. Fini was only partly successful and Berlusconi was able to hold onto some of Fini's loyalists but the defections weakened Berlusconi's parliamentary majority and also his control over the legislative agenda.

Meanwhile the economic crisis continued to grind away in Europe, forcing Greece, Ireland, and Portugal to seek bailouts. This caused financial markets to focus ever more closely on Italy. Although the Berlusconi government did not borrow excessively year-on-year, the Italian state is saddled with huge debts. The markets did not initially view this as a problem. However, when Greece entered into negotiations for a second bailout in 2010 and 2011, the huge indebtedness of the Italian state emerged as a cause for concern.

International investors started selling Italian bonds in early July 2011; by August, the Italian bond market threatened to go into a rout. The European Central Bank offered to shore up demand for Italian government obligations, but only if Berlusconi could achieve a coherent reform agenda. This is when the poor relations between Berlusconi and Tremonti became important. Although Berlusconi had a majority in both chambers, his support was not strong enough to undertake necessary reforms and at times Tremonti appeared to be working against the government's agenda. The pressure in financial markets only intensified as a consequence until the President of the Republic, Giorgio Napolitano, intervened to demand decisive action. Berlusconi was unable to deliver enough to satisfy either Napolitano or the markets and so in November 2011 he had to step down in favor of a technical government headed by Mario Monti.

The purpose of the Monti government was to undertake the reforms that Berlusconi could not implement. It was also to hold the Parliament together until the next scheduled elections could be held in the spring of 2013. To do so, however, Monti had to retain the confidence of both chambers in the Italian Parliament. Even a technical government appointed by the President of the Republic is not exempt from this requirement. Such majorities could attain only if Berlusconi and the center-left agreed to work together.

By this point, Berlusconi appeared to have lost much of his stature and the Northern League all but imploded. Meanwhile, the center left had not yet recovered from the divisions that brought down the Prodi government in 2008. The center-left coalition had rebranded itself as a single 'Democratic Party' (PD) already in 2007, but this did not contain the strong and conflicting currents surrounding powerful individuals prior to the collapse of the Prodi government and it only became weaker during the years that Berlusconi was in power.

The simultaneous weakness of the center-right and center-left made it possible for Monti to dominate the first months of the crisis. It also made it likely that Monti would lose authority as the center-right and center-left attempted to reassert themselves during the run-up to the 2013 elections.

The divisions on the right and the left created opportunities outside the political system as well as within the institutions of the Italian state. A new populist political grouping centered on the political satirist Beppe Grillo grew in the vacuum created as the center-right and center-left focused on regrouping. Moreover, the growth and strength of this 'Five Star Movement' was hard to track using traditional public opinion polling methods.

The main force keeping the Monti government together was the threat that political turmoil would give rise to economic catastrophe. That threat abated in the summer of 2012 when European Central Bank President Mario Draghi promised to do whatever it takes to safeguard the euro. Draghi fleshed out this commitment in September 2012 and the interest rate charged on Italian sovereign debt responded almost immediately. In turn, this relaxation of market pressures made it possible for Berlusconi to begin reasserting his authority. It made it easier for the center-left to try and forge a more coherent Democratic Party. It sapped much of Prime Minister Mario Monti's legislative initiative, which depended upon the active support of the two largest parties, but it also allowed Monti the luxury of imagining a life in electoral politics (rather than as an apolitical, technical appointment). Finally, this flurry of economic activity allowed Grillo to highlight the cynicism of the two main political parties and to ridicule the 'objectivity' or 'impartiality' of Monti's technical government. In short, the relaxation of the crisis ushered in a period of unprecedented electoral volatility.

From Bad to Worse?

When the electoral campaigning started in December 2012, the Democratic Party was in the strongest position. Silvio Berlusconi was a spent force. Mario Monti was well-respected and yet politically inexperienced. And Beppe Grillo was an unknown, dark horse. The only challenge for the PD was to win a majority in the Senate – which is much the same challenge that Prodi faced in 2006. By early January, however, the situation began to change. The PD was less unified and effective, Berlusconi was more attractive, and Grillo was more worrying. The only constant was the performance of Mario Monti, and yet his entry into politics began to chip away at his technocratic authority and so reinforce Grillo's accusations that Monti is just another member of the Italian ruling class.

These tendencies only strengthened in the weeks that preceded the February 2013 elections. Nevertheless, the magnitude of the changes was startling to virtually everyone. By the time the Italians went to the polls, Berlusconi's center-right coalition was virtually tied with the center-left coalition headed by the PD. Beppe Grillo's Five Star Movement came in a close third in comparison with these two electoral coalitions and yet it emerged as the largest single political party in the Chamber of Deputies and the second largest party in the Senate. For his part, Mario Monti did much worse than expected and his centrist coalition received fewer than 10 per cent of the electorate.

Under the prevailing electoral laws, the center-left coalition received 55 percent of the seats in the Chamber of deputies because it received 29.55 percent of the popular vote against the 29.18 percent garnered by Berlusconi's coalition on the center-right. In the Senate, the gap between center-left and center-right was slightly larger – 31.60 percent to 30.72 percent. However, Berlusconi's center-right coalition actually won slightly more seats – 116 to 113 – because it prevailed in larger regions where the majority bonus was correspondingly more generous. Without the support of Beppe Grillo, however neither

center-right nor center-left could command a majority in the Senate. Only by working together could the center-right and center-left form a government at all.

The full implications of this situation took several weeks to sink in. Democratic Party leader Pierluigi Bersani tried to form a coalition able to command a majority in the Senate and failed. Meanwhile the Italian Parliament had to elect a new President of the Republic. That proved equally challenging and so eventually Giorgio Napolitano had to stand for reelection – on the eve of his 82nd birthday. Bersani resigned as leader of the Democratic Party in the meantime.

Napolitano's conditions for resuming office were that the center-right and center-left agree to form a government and that this government reform the electoral system so that Italy does not find itself in the same situation once there is an opportunity to hold new elections. That is the reason Enrico Letta is Prime Minister and it is also why Letta's broad coalition government depends so crucially on Silvio Berlusconi.

The problem for Letta is that without Berlusconi there will be nothing to hold the center right together. Italian politics has always rested on informal, personal relations. But Berlusconi's center-right movement takes this dependency to a new level. Should Berlusconi be barred from holding public office, Letta risks losing his support in the Senate from the center-right. Letta's government will collapse without having reformed the Italian electoral system and new elections could result in further chaos.

The center-right is not Letta's only problem. He also has to face the divisions on the center-left, including both a resurgent Pierluigi Bersani and his most prominent challenger for leadership, the mayor of Florence, Matteo Renzi. Both Bersani and Renzi are pushing for a break with Berlusconi's center-right party and the opportunity to form a new government. Each is willing to accept the risks associated with new elections.

Looking to the Future

There is much that is not new in the current Italian crisis. The main drivers are the divided political institutions, the fragmented political parties, and the adverse incentives created by the electoral process. Italy has faced all of these problems before. The difficulty is that each of these problems is so exaggerated. Italy's political institutions more precariously balanced, its political parties more dependent upon personal influences, and its electoral system much more distorted than in the past.

The only good news is that so far market participants have not taken much notice. They are aware of the problems that Italy is facing but they have not priced them into their trading on Italian sovereign debt. In this sense, while the current crisis is politically intractable, the 2011 crisis that brought down the last Berlusconi government was worse. The only question is how long the market's indifference will last. The answer is 'not forever'. Should the Letta government fail to reform Italy's electoral institutions, should the broad coalition break down and result in new elections, and should Giorgio

Napolitano step down from office, the situation in the markets will deteriorate sharply. Moreover these things are all interconnected. The PD will support the broad coalition only so long as it works toward electoral reform; Napolitano will stay in office only so long as the broad coalition holds together.

The linchpin in all this is Silvio Berlusconi. The sentence against him has been confirmed. The question is how he will respond.

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