In the space of a few short months, discussion about Italy in the second half of 2011 swung from a country that could bring down the single currency and possibly the EU with it, to having the government that would “save” the Euro and the EU. It would be too easy to fall into the trap that depicts this dramatic transformation as the eclipse of a populist political leader by a technocrat cut in the mold favourable to EU officials and, more widely, political commentators. There were many features that made the Silvio Berlusconi government an outcome of primarily (and uniquely) Italian social and political conditions. However, these different faces of Italy in Europe – Italy as an unreliable European partner versus Italy at the heart of the EU - mask much deeper structural features that find expression in the ambiguities about the EU itself and the role it is to play in mediating exogenous pressures on Italy and, more generally, member states. These tensions rose to the surface and began to define politics in Italy, and elsewhere, with the economic crisis of the last decade.

One of the many fissures to emerge in the European Union since the start of the global economic crisis in 2007 has been between the states seen to have adjusted to the imperatives of a global economy and those who have yet to bring about structural reforms in social, political and economic relations. It has brought into relief an ambiguity that has been present for at least the last two decades. On the one hand, the convergence pressures of the single currency as well as the single market would force a rebalancing of state intervention so as to make economies more competitive. The “transformative power” of Europe would help to whip member states into shape to ensure that Europe’s economy could take on global challenges. On the other hand, there has been a constant reference to how EMU would ensure national diversity and the preservation of different models of economic and social governance. As much as the EU has transformative power, it also has been seen as the means to “rescue” the state in the different ways in which it governed society in the member states. The debate about Europeanization and the transformative power of Europe - that is, about the extent to which the EU can and should be the instrument to change social and political relations within and not only between states – is also about the extent to which exogenous pressures lead to some sort of convergence in the domestic politics and policies of member states in order to deal with the challenges of a global economy.

The Italian case in the period since the introduction of the euro provides a useful way to examine the extent to which the politics within member states have dealt with this tension between seeing exogenous pressures as vehicles for change versus looking to Europe as a way to guarantee existing social and political relations. Throughout the process of European integration, Europe has always represented two parallel and, possibly contrasting, tendencies within Italian politics and society. On the one hand, Europe was to be the motor for the completion of Italy’s modernization. Its political, economic and social structures remained incomplete projects, with a party system that lacked traditional center-left and center-right parties, a dichotomous (or more) economy and large parts of society still looking to remain immune from the competitive pressures of an increasingly interconnected world. Europe was to provide not necessarily the “vincolo esterno”, although at times necessary, but the transformation of norms and values for Italy to be a modern (liberal) society and state. Italy was to remain in the centre of Europe so that
Europe could become the centre of Italian political and social life. On the other hand, a second vision was that Europe was to be the bulwark against fundamental social, political and economic change. European integration would provide the umbrella under which national economies and societies could protect themselves from external pressures, whether these were in the forms of immigration or economic liberalization. The weight and strength of nearly 500 million people would ensure that the variants of the European social model would retain their essential elements. While this could mean opening up parts of the economy and other policy changes, the aim was to ensure that Europe, and more broadly globalization, did not become an engine of change within Italy. Italy was to be in the centre of Europe so that Europe not would become the centre of Italian political and social life. These two visions of Europe have not been translated into coherent political movements largely because Europe is not the underlying issue that drives them. Rather, they reflect underlying structural factors that continue to shape Italy’s policy responses to Europe more than European policies shaping Italian outcomes.

The aim of this paper is two-fold. First, it wants to illustrate that Italy has had, despite an official position that has been highly supportive of European integration and supranational arguments, an ambivalent relationship with Europe, looking to it as both a source of modernization and as bulwark against change. The second aim of the paper is to explore more closely the deeper political and economic factors that suggest that it is this “second Italy”, that which has resisted and feared modernization, which seems more widely diffused and deeply engrained. This part of the discussion will explore the extent and the limits to the “transformative” power of Europe.

**Transformative Europe, Transforming Italy**

Arguably, Italy provides one of the most attractive cases for trying to assess and demonstrate for the transformative power of Europe; that is, the extent to which being part of the process of European integration has been instrumental in bringing about fundamental changes (Börzel and Risse 2007; Cowles, Caporaso, and Risse 2001; Featherstone and Radaelli 2003). Long before scholars of European integration asked to what extent and how the European Union might change politics in the former Communist regimes of eastern and central Europe, Italy had looked to Europe as the means to consolidate a fragile liberal democratic regime and help in its postwar reconstruction (Willis 1971).

However, even when there are letters from the European Central Bank listing policies to be adopted, identifying whether and to what extent Europe can transform a state and its politics remains a source of debate. There has been a great deal written about the extent to which Europeanization “hits home”; that is, as a process that transforms domestic politics, institutions and policies (Exadaktylos and Radaelli 2012). There are different interpretations of Europeanization; so much so that it has run the risk of conceptual stretching as it has been applied in a variety of ways and to explain very different processes (Olsen 2002; Radaelli 2000). There is a “top-down” view of Europeanization, which explores the extent to which decisions made at the European level are transmitted into domestic policy (Börzel 2002). The emphasis here is on Europe as a constraint on politics and policy. There is also a “bottom-up” view of Europeanization, which examines the ways in which domestic actors look to the European level as a way to shape policy outputs and outcomes. In this instance, Europe is an opportunity more than a constraint. Then there is a third view of Europeanization that explores the relationship between domestic actors and the European level as a dynamic one in which domestic actors are both constrained and enabled by politics and policies at the European level (Giuliani 2003).
While the debate about the actual dynamics of Europeanization will rage on for some time, there are some essential features found in all Europeanization arguments that have some bearing on a discussion about Europe and “salvation” or modernization. The first is the obvious point that Europeanization is essentially about change and that member states must engage in “reform” of their politiees, politics or policies; that is, being more “European” means that, in most cases, domestic conditions had to be recalibrated to merit the Europeanization tag (Graziano and Vink 2006; Knill 2001; Radaelli 2003). Second, there is an implicit assumption that if there is a problem with the Europeanization process – namely, the expected change does not come about or does so without respecting the intended effect – it rests with the member state. Indeed, the term used is “misfit”, in the sense of a lack of fit but clearly it is implied that the member state is the “mis-fit”; that is, is inadequate to be part of the group because it is unable to integrate what comes from Europe into the fabric of domestic politics or policy (Borzel and Risse 2000; Falkner 2001; Falkner 2003). In this sense, we see references to laggards, member states who drag their heels in becoming more Europeanized and, in doing so, possibly slowing down the whole European project.

Third, there is a positive evaluation given to change and “Europeanized” change. Every step in the integration process is seen as the result of either an intergovernmental bargain, which means that states have found a satisfactory decision that will promote their interests: by definition, then, a good change. Or it is the result of a supranational process, which reflects new phenomena, such as “multilevel governance” or the regulatory state in which politics gives way to practical problem solving in a post-national context. In both instances, the Europeanized change is a step in creating a more modern Europe that reflects and responds to the new dynamics of politics beyond the national state. Europeanized change is also, implicitly and most often explicitly, seen as responsible for most of the positive changes that took place in post-war Europe: the spread of liberal democracy, peace and security, economic growth, the dismantling of economic barriers, etc. (Rifkin 2004). Europeanization, then, has meant not only change but transformations that have made Europe a modern haven for liberal democracy and market capitalism; a model of change to be exported throughout the world. The fact that a great deal of compliance from member states relies on “blaming and shaming” the laggards, free riders and misfits, indicates the inherently positive connotation that is given to change that is inspired by Europe (Tallberg 2002). Indeed, the “vincolo esterno” would be less effective if there was not a widespread acceptance that the exogenous constraints were not inherently good or right.

As will become more apparent in the discussion below, these various features have been very much part of the discussion of the relationship between Italy and the European Union; and more generally between the “core” members of the Eurozone and its “periphery”. Moreover, in few member states have the dynamics of domestic political, institutional and policy change been embraced – both by political actors and observers – within the framework of the essential features of Europeanization. The view that Italy and Europe were bound by the same destiny claimed that the vincolo esterno was not only necessary, it was the right strategy to pursue to create help create a “normal country”. However, alongside this positive view of the transformative power of Europe there has always been a form of trasformismo; that is, that Europe would provide a shield to ensure that exogenous pressures of an increasingly global economy would be kept at bay. These two views co-existed comfortably so long as Europeanization did require political choices that had redistributive consequences and a re-structuring of state-society relations. The economic crisis which began in 2007 has laid bare the fissure between those who see transformation as necessary and right and those that look to use Europe to preserve existing social and political orders. What will be apparent below is that the transformative power of Europe is limited in its capacity to heal this rift between those who see change as necessary and right and those who look for ways to limit the impact of exogenous pressures.
Italy and Europe: between continuities and changes

Italy, as a founding member of the European project, has been often considered one of the supportive Member-States (MSs) of the EU. Eurobarometer and other polls consistently reported that Italian public opinion was among the most enthusiastic of European integration for much of the postwar period. This picture was not far from the reality. After a short period of contestation during the 1950s and the 1960s, when the two main parties, the Christian Democrats (DC) and Italian Communist Parties (PCI), mirrored the geopolitical divisions of the Cold War, Europe became the point of reference for political leaders of all political stripes and the citizens in general (Isernia 2005; Isernia and Amendola 2005). However, as we will see below, this almost monolithic and positive embrace of Europe has given way more recently to two opposing visions of Europe and its role in Italian political and social life (Bellucci 2005; Bellucci and Serricchio 2012).

In the aftermath of the Second World War, the Treaty of Rome and the project of European integration had two important related and legitimizing roles for Italy. First, it provided Italy with the means to re-enter the family of nations at the international level and to firmly place itself as a member of the Atlantic alliance; second, Europe meant liberal democracy and market capitalism, two essential features that were highly contested in the immediate aftermath of the war. Moreover, the idea of Europe became inexorably entwined with the democratic Republic. In other words, Europe not only was a choice of Italian foreign policy, but, more in general, it was a “Weltanschauung”. The political elite considered anchoring Italy to Western democracies a necessity largely because of the presence of the most successful Communist party of Western Europe. The PCI’s electoral strength did not translate into executive power but it was large enough to shape the dynamics of the party and political syste. Italy became a consensual democracy, based on a conventio ad excludendum; that is, there was little possibility of an alternation in power and the exclusion of the leftist parties from the government coalition. Nonetheless, there was a high degree of elite accommodation on a number of fundamental issues and Europe became one of them.

Italian foreign policy in the decades immediately following the war was based on three different objectives which were considered a sort of obstacle to the legitimation of the PCI: participation in the process of European integration, the alliance with the US, and a friendly relationship with southern Mediterranean countries. The PCI relationship with the Soviet Union and its own history meant that its foreign policy position with respect to these three pillars would condemn it to an anti-system status. During the 1970s and the 1980s, the position of the PCI changed (Benedetto and Quaglia 2007), with the party becoming more pro-European (and, as a consequence, accepting with a more critical approach, even the Atlanticist choice). Europe, then, became a bipartisan issue, bridging the gap between the government and the seemingly permanent opposition.

Despite the consensus that emerged on the importance of Europe, Italy’s European policy was sometimes contradictory and not particularly successful. This might be explained partly by Italian policy styles. Italy has traditionally been characterised by fragmented decision-making structures, with numerous access point for societal interests, thus fostering a consensual approach to policy-making (Posner 1978; Ranci 1987). Additionally, a weak and divided executive, mapped onto an institutional and constitutional architecture that placed a premium on representation rather than system effectiveness has produced a policy-making style that assured “surviving without governing”. It was characterised by incrementalism, little consensus on major policy objectives and deep social divisions (Di Palma 1977) so that governments rarely anticipated policy challenges and even more rarely could define their preferences and the terms of
the political and policy debate. These factors made identification of the Italian interest (or preferences) very difficult, and the coordination mechanism in the European policy very weak. As a consequence, Italy often failed in promoting its positions in Brussels and had a very low record of national transposition of EU legislation. The result was that while there was strong support for Europe amongst political elites and in public opinion, Italy often found itself under scrutiny by European institutions and its EU partners. Amongst Italian political elites, Europe was the means to modernize the country; for Europe, Italy was the “sick man” that needed to be transformed.

While many areas of public policy would garner attention (for example, labour market policy), none would capture the attention of policy makers and European officials as the governing of the Italian economy, especially the state of public finances (Reviglio 1998; Spaventa and Chiorazzo 2000). The ink was not yet dry on the signatures of the Maastricht Treaty when Italy was forced to drop out of the Exchange Rate Mechanism (ERM) in the midst of a serious financial crisis in September 1992. The lira was allowed to devalue by as much as 25%, leading to further strains on public finances. The devaluation would prove to be a swan song, which would raise more serious challenges once Italy entered the single currency; that is, it helped generate an export boom that allowed policy-makers to put off making difficult decisions about productivity and competitiveness. The exit from the ERM and the devaluation also sparked fears that Italy was reverting back to the old practices of avoiding making difficult choices in the governing of its economy. Italy was once again the “sick man” of Europe (Graham 1996).

There are a number of reasons why the “health” of Italian public finances was the focal point for a broader discussion about the need to provide Italy with adequate policy responses in a rapidly changing world. The first, and most obvious, was the dimension of the problem. Italy’s long road to enter the single currency is well documented but it is worth remembering here that its public deficit level in 1991 was in double digits and Italian budgets had to service a debt level that exceeded 110% of GDP. It would have been hard for any kind of discussion about public policy to ignore these levels of public sector debt and deficit, even without the objective of bringing them within the parameters set by the convergence criteria. Any “healing” of Italian public policy would have to begin with public finances; and given already high tax levels, this meant having to make decisions about spending.

Second, public finances put into relief many of the problems endemic in Italian decision-making. A consensual policy style combined with a political stalemate ensured that weak governments would loosen purse strings to hold together wobbly coalitions as well as maintain social peace. Necessary for reform was not only a first order change in the policy instruments but also in the decision-making mechanisms themselves (Hall 1993). It is not a coincidence that Italy’s hyper-consensual politics ran into problems at the beginning of the 1990s, at precisely the same time that it was faced with difficult decisions about maintaining ERM commitments as well as beginning to take the steps necessary to meet the convergence criteria (Salvati 1997). This is not to argue that the “First Republic” collapsed because of public finances. It is simply to point out that Europe, by the 1990s, meant having to make difficult choices that constrained the ability of political parties to use public finances to mobilise support. Italian parties tried to avoid the day of reckoning as much as possible but the financial crisis has only highlighted that being part of the Euro meant it was harder to “transform” exogenous pressures rather than be transformed by them.

It is not surprising, then, that despite the enormity of the challenge at hand, Italian political leaders were undeterred in the quest to ensure that Italy did not miss entering the single currency in the first round. Public finances were the lightening rod around which debates about how Italy could and should adapt to new challenges in a global economy. As one commentator argued, “The euro was the path of a
solid currency, lower costs for energy and credit...It was an alternative to the traditional policies, and certainly a healthier and more modern one” (Cañagata 2005). They were the litmus test for a modern, efficient liberal democracy and it was Europe that would provide the answers. There was no debate as to whether Italy should strive to meet the convergence criteria; it was only a question of whether it could. Moreover, there clearly was little doubt that many felt that Italy had no choice but to try. The titles of books – for example, Condemned to Succeed? or Saved by Europe? – were graphic summaries not only of the challenges ahead but also the implications of the convergence process. Europe would “condemn” Italy to reform, and the price for resisting might be to lose Europe and the modernization of Italy.

Italy’s entry into the single currency did not create political cleavages in the 1990s. The consensus that Italy had to enter the euro was widespread and deeply rooted. However, Italy’s “success” was not met with a great deal of enthusiasm and Italy had no sooner entered into the single currency when it became apparent that rather than be an opportunity for solving Italy’s policy dilemmas, the euro itself was now becoming a problem. In fact, there was even nostalgia for the lira. Government ministers for the Northern League (LN) made public declarations in favour of the return of the old currency. The LN’s position was understandable. Its core constituency is in the industrial provincial cities of northern Italy, an area that benefited enormously from the export boom of the 1990s but which paid the cost once the cover of a devalued currency was lifted.

Nor did Italy’s entrance into the single currency mean the end of the concerns with the state of public finances. By 2005, it was subject to an excessive deficit procedure dictated by the terms of the Stability and Growth Pact; it would be subject to the EDP again in 2009. With the introduction of the single currency, it was no longer just fiscal policies that needed to be reformed under European inspiration but a whole range of related policy questions; and once again, the discussion about Europe and Italy’s modernization resurfaced. By the time Romano Prodi returned from his stint as EU Commission President to head a centre-left government in 2006, it was apparent that the requirements for being a “modern” European country had extended well-beyond simply reining in public finances. The upheaval in Italian domestic politics, from centre-left to centre-right in 2001 and then back again in 2006, did not produce the political and institutional changes that would have provided the kind of decision-making machinery that many felt was necessary to provide the timely policy responses needed in a rapidly changing and integrated global economy. But for many, Europe (and more of it) remained the beacon to follow. What was different by the middle of the 2000s was that there did not seem to be a consensus neither around the question that Italy needed major reforms nor around the direction if it did.

This lack of consensus was even more emphatic between 2008 and 2011, at the time of the fourth Berlusconi government. The impact of the international economic crisis that started in the US in 2007 on the national economy was seriously underestimated by the government, which kept insisting that the economy was doing well as late as the start of 2011. Berlusconi himself continued to claim that the was no “crisis” in Italy as late as November 2011, even as international financial markets were condemning his government. This only highlighted that the lack of the needed structural reforms (among which we can mention, as examples, those in fiscal policy, the welfare state, labour markets, and the liberalization of services) condemned the Italian economy to extremely low rates of growth if not recession. Confidence in Italy in international financial markets was undermined by the fact that these reforms were not carried out by the Berlusconi government despite having the largest majority in Italian parliamentary history. Berlusconi, his own credibility shaken by a string of personal scandals, presided over a fragile coalition that became more divided over the course of the legislature. Newspaper and media reports in the second half of 2011 were dominated by data of the “spread”, that is to say the difference between the interest rates of
the Italian Btp and the German Bund at 10. This came to be considered an indicator of the capacity of Italy to cope with the economic crisis and to adopt the inevitable reforms. It is not surprising that an unprecedented increase of the “spread” on 9 November 9 2011 (and the downgrading of the Italian debt by the main international rating agencies) forced Berlusconi to resign, making the birth of a government led by Mario Monti possible. Berlusconi’s position had become untenable both within Italy and at the European level after his government had reneged on carrying through on reforms that were promised in August in return for the ECB’s intervention in secondary debt markets.

If the numerous pressures on the Italian government coming from the EU institutions requiring more incisive economic reforms did not succeed, this was also due to the fact that Europe was no longer seen singularly as the “answer” to Italian problems; becoming, instead, one of the sources of these Italian “problems” (Brunazzo and Della Sala 2011). For many politicians (mainly on the centre-right but also on the extremes wings of the political spectrum) and for a growing part of the public opinion, the EU (and, more specifically, the Euro) was not able to guarantee modernization nor protect Italian society from broader global pressures.

The fact that there is no longer a consensus around the narrative about the EU is evident looking at the discourse of some leading political figures. Among those maintaining a high level of confidence in the EU we can mention the President of the Republic, Giorgio Napolitano, and former prime minister, Mario Monti. As an example of these positions supporting the EU project and strictly linking the Italian to the European destiny we can mention a brief passage of the address by the President Napolitano on the occasion of the exchange of greetings with the Diplomatic Corps on December 2011: “Today, Italy is called to tackle new challenges, in a period of radical and unceasing change on the global stage. These are common challenges that we must be prepared to grasp and win together. Well, Italy will play its part in advancing the cause of peace, human rights and democracy in the world, and of balanced, just and sustainable economic and social development at the global level. It will do so in multilateral fora; it will do so in a spirit of loyalty to its commitments and alliances; it will do so in military peace missions; it will do so in the process of European unity and integration”1. Napolitano, and Monti, are emblematic of a part of the political elite that continues to see in Europe the way to transform Italy and to see Italy’s definition of itself inexorably bound to the process of Europe.

Whereas in the first decades of the European project, this positive view of Europe’s role in Italy’s transformation would have been largely unchallenged, Monti’s government had to deal with a very different landscape. Since mid-1990s, critical voices on the role of the EU in national economies and on the limit posed by the Euro to national sovereignty have become louder and louder (Bellucci and Conti 2012). The party manifestoes and the discourse of the political leaders are now much more diversified and politicized than in the past in defining the relation between Italy and the EU. A book like the one published in 2008 by Giulio Tremonti, the Minister of Economy during the Berlusconi governments, entitled *La paura e la speranza* (Fear and Hope) criticized the role of Europe in managing the pressures generated by the globalization process in a way that would have been unthinkable in Italy only a few years earlier. In his book, Tremonti tries to answer the following question: “Why is Europe no longer the master of history and risks exclusion from history, reduced to a geographical agglomeration?”. His conclusions are that Europe has lost its identity and is no longer able to provide the right answers to the difficulties of national and international economies. Tremonti is an important figure not just for the central role that he played in governing the Italian economy for most of the period since the introduction of the Euro. He was the

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lynchpin of the different strands in the Berlusconi coalition, close to both the Northern League and to Berlusconi. He was at the same time skeptical of many aspects of economic integration yet a proponent of Eurobonds. He saw in Europe not an engine of change but a bulwark against global pressures. In this way, he captured the position of the Italian government for most of the last decade.

The arrival of Mario Monti was supposed to represent a return to “salvation” through transformation. His government was met with an initial sigh of relief as the drama surrounding the figure of Silvio Berlusconi was replaced with a serious concern with restoring credibility in international markets and with European partners. However, relief quickly gave way to frustration amongst the electorate as the social and economic consequences of the crisis only worsened in 2012. More importantly, it was clear that not only was the esteem and credibility of the Monti government not an asset, in many ways it was a liability. It represented the transformative power of Europe but underestimated the extent to which Italian politics is still very much constrained by the dynamics of trasformismo. The success of the Movimento 5 Stelle (M5S) in the 2013 election suggests that what the electorate was looking for was not political leadership that would gain favour in Europe but one that would ensure that a central place in Europe would guarantee that the impact of Europe on basic policies and politics would be limited.

The 2013 election is striking in that the only political force that defended the importance of the transformative power of Europe, Monti’s Scelta Civica, was soundly defeated. More importantly, not a single major political party, including the centre-left PD, sent out unambiguous signals of support for the need to use Europe to modernize Italian society. The M5S has been dismissed as a protest and populist party which will in all likelihood fade away. However, it sent out clear messages about how the Euro compromised sovereignty and was transforming Italian society and institutions. It clearly touched a nerve with a part of the electorate that was feeling increasingly threatened by changes it saw as out of the control of its institutions and political leaders. It is not a coincidence that amongst the many targets of the M5S’s leader, Beppe Grillo, are not only the European institutions but international financial institutions, immigration and economic liberalization. Grillo has consistently said that he is not opposed to the EU but that he wants a Union which protects Italy from these elements of globalization. His success has not been lost on other parties. Indeed, the refrain that we want a different Europe was sung by the major parties of the centre-left and centre-right in the election campaign. Monti’s Scelta Civica, which argued that there was no alternative to European commitments, has paid the price.

**Italy, A Difficult Transformation**

It would be hard not to find a period in the 150 year history of unified Italy when there was not a discussion of the need for major reforms to complete the process of modernization and to meet the challenges of the contemporary period. However, arguably, the last twenty years may stand out as they have been characterised by, on the one hand, a great deal of political ferment and even convulsions while, on the other, yet another period when forces of resistance to change prevailed. Since the signing of the Maastricht treaty, Italy has had, amongst other important political developments, at least two major reforms of its electoral laws, changes to the distribution of powers between the central and regional governments, the disappearance of all the major parties that dominated politics in the postwar period and then many of those that replaced them, two distinct phases in which the country was governed by technocrats and the emergence of a nascent bipolar party system. Yet, despite the volatility of the period, politics and policies have stayed remarkably consistent; and some basic social and economic structures have proven to be remarkably resilient.
One way to measure the limited impact that European pressure has had on Italy in the last two decades is to examine the letter sent by the then President of the European Central Bank, Jean-Claude Trichet, and his successor and Governor of the Bank of Italy at the time, Mario Draghi, to Italian Prime Minister Silvio Berlusconi on 5 August 2011. The letter is remarkable both for what it represents and for its content. Written just as Italy entered into the sovereign debt storm in July 2011, it set out quite clearly what the Italian government had to do if it wanted to benefit from the ECB’s intervention in the secondary debt markets. It was a form of conditionality that one would not expect to find applied to a member of the G8 and the third largest economy of the eurozone.

The August letter to the Berlusconi government set off an exchange of missives between the European institutions and the Italian government in October and November 2011. They were supplemented by reports from the IMF and the OECD, not to mention assessments by financial market operators. The missives from the EU institutions have two striking features. First, there was nothing new in the reforms that were being solicited. More than a list of conditions to be met in return for help on financial markets, they were an admonition of the inability of Italian governments of all political stripes in the period since the Maastricht treaty to carry out basic structural changes that should have been part of being in the single currency. Second, it is hard not to read the letters from both sides and not notice an underlying lack of faith that there is the political will to carry out reforms. The Berlusconi letter was full of vague references and promises that were not so different from those presented by Italian governments for the last twenty years. On the other hand, Commissioner Olli Rehn’s punctilious note asking for clarifications contained 39 sets of questions and requests that no government, let alone a fragile one on its last legs, could have responded to with a clear set of answer and commitments.

The exchange, then, provides an interesting lens through which to examine some of the structural problems that Italy continues to face and which seem resistant to attempts, mostly feeble, by governments to address. The Commission’s and the ECB’s concerns fall into two categories: public finances and obstacles to economic growth. In many ways, the case of public finances has been the easier story for Italian governments to tell. In a letter to the Presidents of the European Council and Commission on 26 October, Prime Minister Berlusconi could claim that Italy’s recent performance in maintaining a healthy balance sheet was parallel to Germany’s. He pointed to measures to bring a balanced budget to Parliament by 2013 (a year earlier than originally agreed to) and one with a primary surplus of 5.7% of GDP by 2014. This would serve to bring down Italy’s public debt from 120% of GDP to 112%. While the figures and projections were entirely wildly optimistic, Berlusconi was right to point out that Italy’s public finances in recent years have been relatively healthier than some of its Eurozone partners.

However, the major problem with Italian public finances, apart from the rather obvious point that there is an exceptionally high level of public debt, is its structure. Public sector spending, as a percentage of GDP, has remained fairly constant over the last two decades as has its distribution: from 50.2% in 1997 to 50.5% in 2010 after a slight drop in the intervening period (OECD 2011c). Yet Italy continues to spend a disproportionate amount on income maintenance for protected sectors such as pensioners while lagging in areas such as education and research. On the revenue side, tax revenue as a percentage of GDP has crept up from 40.1% in 1995 to 43% in 2010 (OECD 2011b).

There may be a number of ways to explain this relative consistency in public finances but what emerges is a political system that has been unwilling and/or unable to address redistributive questions. Fragile governments, even with electoral majorities, have not mobilised the political capital to change the basic structures of taxation and government spending. Moreover, governments, from the Prodi coalitions
that brought Italy into the single currency to the Monti technocratic administration, have met public finance targets largely through tax increases rather than spending cuts. For instance, the Berlusconi government introduced measures that have raised VAT rates from 20% to 21%, with another scheduled increase to 23% in October 2012. The Monti government has not only not reversed these changes, it has introduced new charges such as a property tax on first homes. Monti, like his predecessor, has discovered that there is no major political force that can be mobilised to address some of the structural problems of Italian public finances. The centre-left has proposed very little in terms of changes to public spending and has focused on revenue measures aimed at high income earners and cracking down on tax evasion. The centre-right, on the other hand, is more fractured on the question and at the end of the day has supported tax measures rather than address spending questions especially those that affect local and sectoral electoral constituencies. The best example of this has been the Northern League, whose identity as an anti-politics movement is betrayed by its opposition to structural reforms such as eliminating provincial governments (equivalent to counties) which would have brought yearly savings of over €1 billion.

While there can be no doubt that the communications from the European institutions sought to put pressure on the Berlusconi government to maintain fiscal discipline, they were more concerned with Italy’s poor record on economic growth since the introduction of the Euro. For instance, only 6 of the 39 sets of issues raised by Rehn dealt with public finances while questions about structural reform to promote growth occupied 32. They essentially concurred with the assessment of the IMF, whose country report on Italy in July 2011 stated that fiscal consolidation was essential, “But only sustained growth will reduce the burden of public debt. Increasing potential growth should be the main policy goal. Comprehensive structural reforms in the areas of labor and product markets and public administration should be promptly implemented” (IMF 2011). Structural changes to public finances were needed but these would be of limited use and politically difficult to sustain if they were not accompanied by measures to sustain economic growth.

A close reading of the EU missives, as well as the IMF documents, presents a list of areas that represent the spectrum of social and political life. There are the usual references to the burden of an inefficient public administration and excessive regulation. But there are also queries about reform of the judicial system, universities, teacher training, evaluation of schools and transportation. Rehn also was concerned with measures taken to increase the capitalization of Italian firms. The assessment of external actors, especially the EU institutions, seemed to imply that it was the Berlusconi government that had become the obstacle to these reforms seen as essential for growth. And while it is true that the centre-right was in power for most of the period since the introduction of the euro, there are deeper structural factors at play. For instance, the poor capitalisation of Italian firms (and banks) reflects a model of capitalism that has relied on close (often familial) networks deeply embedded in social and political life, from the local to the national level. Attempts to create new ownership structures that would subject firms to control based on return on equity rather than the more complex relationships in Italian capitalism have and would continue to run into fierce resistance.

Both the EU and the IMF highlight the need to introduce greater competition in Italian product (including services) and labour markets. Greater competition in the provision of goods and services is seen as essential not only to stimulate domestic demand in Italy but to help address some of the issues at the root of declining competitiveness in global markets. The IMF identified the obstacles to product competition as essentially the high levels of public ownership, administrative barriers to entry and excessive regulation. What the reports do not mention explicitly is that the lack of competition, especially in services, is rooted in a guild-like protection for many services and products. For instance, when the
Berlusconi government in July 2011 proposed minor reforms of the legal profession, such as liberalising fee structures, close to 90 parliamentarians from his own coalition threatened to vote against the emergency budget measures. Needless to say, given the fragile state of the coalition, the government backed down. The Monti government’s liberalization package, introduced in January 2012, is still working its way through the legislative process but it does little to address the lack of productivity below in the largest sector of the economy (Weisenthal 2012). The ECB letter as well as Rehn’s was especially concerned with the limited competition for many services at the local level. Despite controlling the purse strings, national governments have failed over the last two decades to liberalise the delivery of most local services, which remain an important resource for political parties at all levels.

The picture that emerges from the assessment of the European and international institutions is an economy that continues to resist opening up parts of society to competitive pressures. There is nothing new in this conclusion and it is something that successive governments have acknowledged but have been reluctant or unable to address. A 1994 report by the state agency for social and economic policy research, CENSIS, laid out a blueprint for how to respond to the challenges of the economic and monetary union as well as broader global pressures. Titled, “How to Create a Competitive Society”, it called for the overhaul of everything from capital markets to education by reducing the role of the state and, perhaps more importantly, dismantling protected interests (Censis 1994). The policy challenges laid out in the CENSIS report have formed the rhetoric of government policy pronouncements for the last twenty years but, as the statements made by European and international institutions in 2011 suggest, there have been few concrete developments.

The one area that is the subject of a great deal of attention is the structure and regulation of Italian labour markets, seen to be a major obstacle to enhancing competitiveness in the single currency. There are two issues that stand out with respect to labour markets and Italy’s relationship with the EU: the growing divide in unit labour costs and employment participation rates. The data in Figure 1 illustrate how labour costs have crept up in Italy since the introduction of the Euro. The nominal unit labour costs in Italy had increased by 30% between 2000 and 2010, while the increase for the entire Eurozone was 20% and 14% for the entire EU (Eurostat 2011b). It is this data that is often pointed to as evidence that the adjustments required as a consequence of the loss of the instruments of monetary policy were largely not carried out. It is important to note that the steady increase in labour costs has not meant that Italian salaries, especially in manufacturing, have surpassed those of its Eurozone partners; in fact, salaries remain below Eurozone averages despite larger relative salary increases in the last decade. What the figures show, in the Italian case, is that social contributions remain high along with other labour costs.
The second feature of Italian labour markets is that it remains one that has a high degree of protection for those in permanent, unionised jobs and a large sectors that are either excluded or in precarious forms of employment. When Italy agreed in 2000 to the objectives laid out in the Lisbon strategy, it had a labour market participation rate of 53.7%; by 2010, that figure had crept up to 56.9% helped largely by the increase in female participation rates which increased from just about 39.6% to 46.1% (Eurofound 2011; Eurostat 2011b). Labour market statistics paint a clear picture, with some groups – namely women and young workers - maintaining a precarious position and struggling to enter. Moreover, the dualistic labour market also had a regional dimension to it, with Italy showing the largest regional disparity with respect to employment and unemployment rates. While regions in central and northern Italy met or came close to meeting all the Lisbon targets in 2010, not a single region south of Rome came close (Eurostat 2011a). Moreover, Italy had the widest regional variation of all the EU member states. Its coefficient of variance in 2010 was 17.4, nearly twice as much as Spain (8.8), the next placed member state; and this disparity was growing rather than shrinking (Eurostat 2011a). Yet the gap between north and south decreases dramatically when it comes to salary differentials.

A detailed discussion of the causes of these structural features of Italian labour markets would require more space than available here. Both European and international institutions have pointed to a number of structural features that have remained largely intact for the last two decades. For instance, Italy’s system of national labour contracts has helped ensure that salary differentials between north and south have been limited, especially in the public sector. The Trichet-Draghi letter stated specifically that, “There is also a need to further reform the collective bargaining system allowing firm-level agreements to tailor wages and working conditions to firms’ specific needs and increasing their relevance with respect to other layers of negotiations.” While collective bargaining at the level of the firm would have some impact on regional pay differences, this will be minimised if it does not include public sector employment as well.

As stark as the regional divide is in Italian labour markets, the central issue that has been at the centre of political and policy debates for two decades is the issue of liberalisation of entry and exit. The
consensus amongst economic observers, both internal and external to Italy, is that Italian labour policy provides a great deal of protection, both in terms of benefits and from dismissal, for those in employment. This comes at the cost of making it (perhaps excessively) expensive for firms to hire new workers. The debate has focused on Article 18 of the Italian labour code, which has given a great deal of discretionary power to judges to reinstate workers who have lost their jobs as well as to award damages. Faced with the prospect of having to pay workers even through lean times, it is argued, employers will put off hiring as much as possible. The result is that labour markets remain stagnant and those excluded are largely confined to short-term contracts that provide little protection. Trichet and Draghi pointed out that relaxing Italian labour laws so that it would be easier for employers to dismiss workers when demand declines is made more difficult by the absence of any comprehensive unemployment insurance scheme and active labour market policies.

Despite the obvious gender, generational and gender imbalances in Italian labour markets, with their attendant consequences for the long-term viability of the Italian welfare state, reform has been slow and difficult to achieve. Italian employers, through its national association Confindustria, has long wanted to dismantle Article 18 along with introducing more flexible forms of collective bargaining. However, they have been less ready to accept that this be accompanied by a major reform of labour and social policies that would see the introduction of more active policies with some of the costs for training and reintegration transferred to firms. Moreover, faced with an expensive and inefficient state, their primary concern with any labour market reform is to bring down labour costs as quickly and as dramatically as possible. Trade unions, on the other hand, have been reluctant to consider any weakening of “acquired rights” for workers. The Monti government had expressed a desire for a major overhaul of Article 18 but as the proposal works its way through the legislative process, it has been watered down so that judges will retain a great deal of discretionary power over decisions about re-instating workers let go by employers. As in the case of the liberalization of services, it is much easier to marshal a majority to resist change rather than one to bring about reforms aimed at addressing needs of those excluded from labour markets.

Despite ten years of national action plans on employment and participation in European initiatives through the Open Method of Coordination, Italian labour markets remain largely the same as they did at the start of the Lisbon process. The only major change of note has been the increase, especially with the onset of the economic crisis, in the number of workers on short-term contracts and those excluded from employment. The Monti government discovered, as centre-left and centre-right governments before it, that even the pressure of a major financial and sovereign debt crisis were not enough to mobilise forces to bring about fundamental change. The Italian economy and society remains wary of measures that will introduce elements of competition. Commitments and promises made at the European level were not translated into concrete measures largely because they were perceived as upsetting patterns of social relations seen as essential for social and political stability. For large parts of Italian society, from trade unions to parts of Italian capitalism, Europe was supposed to provide a measure of protection precisely against the kinds of changes that were now being asked by EU institutions.

Conclusion

The Monti government was presented as Italy’s last opportunity to complete its modernization and return to the table of the great powers of Europe. It presented its policies not as political choices but the only available alternatives if Italy was to be saved. It even called its major package of reforms the “Save Italy” decree. However, after a brief period in which politics was seemingly suspended, it too had to come to
address basic social and political relations. The transformative power of Europe has only scratched the surface in Italy because it has not, and cannot, address basic social and political relations.

References


