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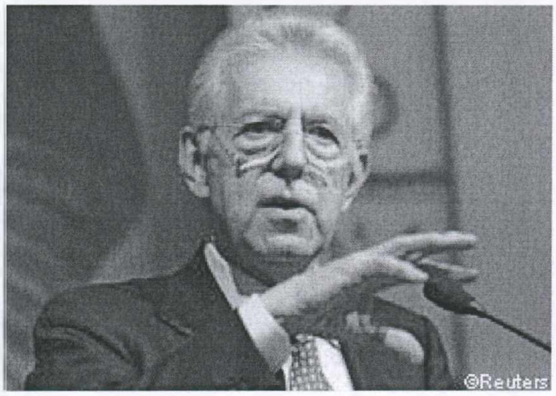
Italy's problems threaten to overwhelm

By Guy Dinmore in Rome


Mario Monti, Italy's prime minister

A squabbling cabinet, an entrenched bureaucracy and a prime minister focused on the international arena – Italy's domestic problems seem to be growing beyond the capability of its technocrat government to resolve even as the eurozone debt crisis deepens.

Officials conceded on Tuesday that a cabinet meeting to approve a package of relatively minor measures intended to promote growth and dig Italy out of its double-dip recession had been postponed for a second time, possibly until Friday.

To blame: Disagreements between Corrado Passera, minister for industry and author of the planned decree, and his cabinet colleagues, as well as opposition from civil servants wielding power behind the scenes.

"Today it is a bit of all fighting against each other," one official said. "I am afraid we are entering phase three in the story of this government – recriminations, after one, honeymoon and two, back to real life."

Mario Monti, the former European competition commissioner appointed technocrat prime minister, tried to knock heads together this week, calling for unity in his cabinet and a sense of purpose after a series of public spats, another official said.

But an adviser to the government, who asked not to be identified, said the real problem was that Mr Monti had lost interest in domestic issues while his attention was fixed on his growing role in co-ordinating policy responses to the eurozone debt crisis by the European Union and the Group of Seven industrialised nations.

"Italy is in the hand of bureaucrats who are fighting change and a prime minister who is not putting his foot down," the adviser said, lamenting that Italy was "missing the opportunity" to implement real reforms after the collapse of Silvio Berlusconi's scandal-plagued and dysfunctional government last November. "The markets will realise at some point that Italy has not done much [reform]."

The advisor is among those who credit Mr Monti for driving through effective pension reforms last December. But his critics charge the prime minister followed that by caving in to political pressures and diluting legislation intended to open up service industries.

Separate labour market reforms are still moving slowly through parliament. Officials are also concerned that as-yet-undefined plans to cut public spending to keep ambitious budget deficit targets on track will be stymied by the powerful state general accounting department, whose mandarins remained in office last year even as Mr Monti replaced the ministers above them.

The spending cuts are essential if the government is to avoid raising sales tax later this year. The treasury on Tuesday said tax revenues in the first four months were €3.5bn short of the government's target, in part due to a drop in consumer spending caused by tax increases.

Even the fates seem aligned against Italy. The government is struggling to find €2bn to help rebuild the industrial and agricultural heartland north of Bologna that was badly hit by earthquakes last month even as its export-driven economy was starting to take off.

Roubini Global Economics commented in a report last week: "The initial period of euphoria that followed the appointment of Mario Monti's technocratic government in November is now well and truly over." The report also noted that yields on Italian 10-year bonds had risen back above 6 per cent, while Mr Monti's approval ratings had fallen from unparalleled highs to the mid-30s as tax increases start to bite.

"As national elections scheduled for spring 2013 draw even closer, the government's capacity to push important, but unpopular, structural reforms through parliament will wane," the report added.

A growing sense that the technocrats have run out of steam while the economy sinks deeper into recession is exposing fractures within the two main parties supporting Mr Monti in parliament.

Stefano Fassina, economic spokesman for the centre-left Democratic party, has publicly suggested Italy should hold snap elections after the summer since in the current context Mr Monti no longer had the strength to push through reforms.

Mr Fassina was quickly slapped down by Pierluigi Bersani, the party leader who insisted elections should be held as scheduled early next year. But similar calls are emanating from the fringes of Mr Berlusconi's People of Liberty party.

Despite growing talk of elections, surveys suggest neither of those parties would win an effective mandate. A void on the centre-right is waiting to be filled, while the Democrats cannot decide whether to form an electoral alliance with smaller parties further to the left.

Hopes among some foreign investors that Mr Monti can remain in office even after elections do not appear well founded. As one aide noted, the unelected prime minister recently complained that these six months in office seemed like the 10 years he spent in Brussels, and perhaps that is where he really wants to be.

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