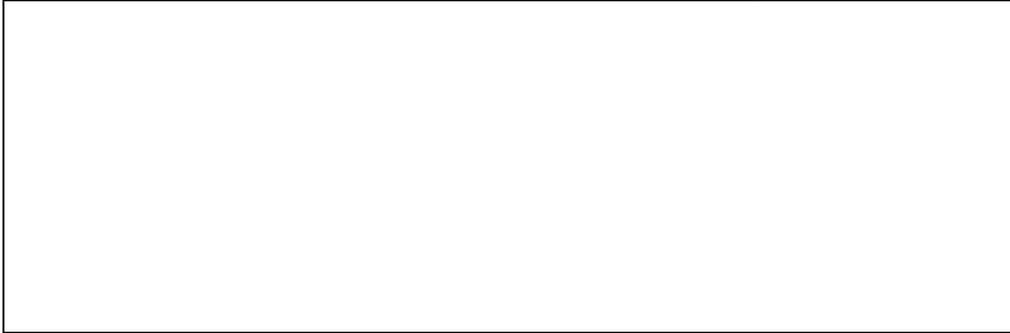


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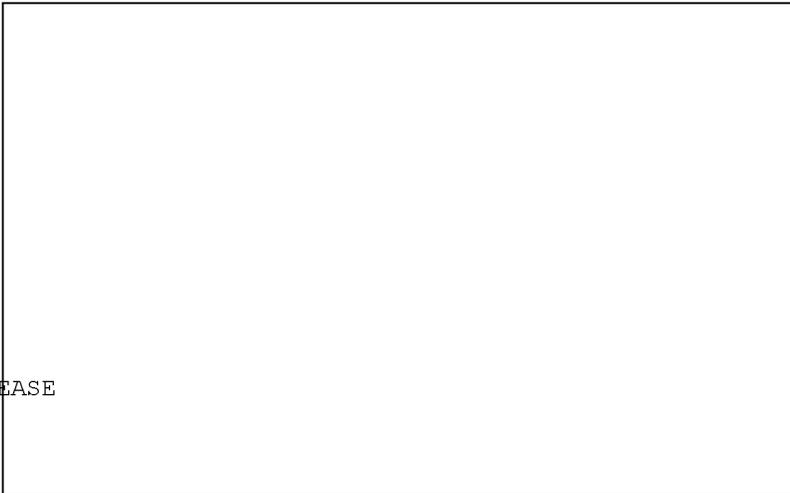


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Central Intelligence Agency



Washington, D.C. 20505

DIRECTORATE OF INTELLIGENCE

Italy: The Political and Economic Scene

SUMMARY

Socialist maneuvering to secure the prime minister's post has dominated the political scene for the last 18 months. With Socialist ambitions pitting them against the two largest political parties (Christian Democrat and Communist), the Italian talent for compromise has been severely taxed. Sparring over fiscal policy has been the most visible sign of friction within the coalitions that have included both the Socialists and Christian Democrats. On the other hand, the two Spadolini governments (June 1981-November 1982) had a fairly impressive record on terrorism and foreign policy. We believe this mix of failure in the economic policymaking arena and relative success elsewhere will probably persist, at least until national elections are held.

Political Situation

The Socialists expect healthy gains in parliamentary elections. The party's spring 1981 congress paved the way for the next campaign by strengthening the grip of party chief Bettino Craxi and by adopting a pragmatic platform. While the Socialists (PSI) want early national elections, they have had to be careful not to push too hard for fear of provoking collaboration between the Christian Democrats (DC) and the Communists (PCI). This would relegate the PSI to the sidelines.

An election -- early or on schedule in June 1984 -- is unlikely to alter the balance of power enough to end coalition instability and frequent policy immobilism that has plagued the country in the postwar era. Even if Craxi's party increases its electoral strength from roughly 10 percent (in 1979) to the hoped-for 15 percent, the Socialists will still be dwarfed by the Christian Democrats (38 percent in 1979) and the Communists (30 percent). Unless united with the other lay parties by means of a programmatic accord, the Socialists would be unable to challenge DC hegemony. No such accord now appears on the horizon. Thus, a Socialist-led government would depend on DC -- or perhaps PCI -- goodwill for its longevity and success.

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Institutional reform is being touted as another way to improve the government's policymaking capabilities. But here again, change will not come quickly. While all the parties are giving lip service to various reform proposals, only the Socialists seem serious about securing these reforms. Frequently mentioned reforms include: streamlining the cabinet, increasing the prime minister's power, and more strictly limiting parliamentary recourse to secret votes. [redacted]

Economic Outlook

All the major parties seem convinced that the next election will be won or lost over economic policy. This conviction led to a nasty and time-consuming budget battle last year, when early elections were also a possibility. The same battle lines have already been drawn over 1983 fiscal policy -- and contributed to the resignation of the second Spadolini government on 13 November. The Christian Democrats continue to press for austerity in the form of tax hikes and limited welfare spending cuts. The Socialists are rebelling at the cost of austerity in terms of jobs and economic growth. [redacted]

If pre-election jitters prevent adoption of austerity measures, the budget deficit could, according to Spadolini's budget minister, top 17 percent of GDP in 1983. It will be around 15 percent of GDP this year. Journalists at home and abroad have questioned whether even Italy's extraordinarily elastic system can swallow this increase. We believe it can, barring another external economic shock to the system. Our confidence stems primarily from the Bank of Italy's well-deserved reputation for keeping a close watch on the country's external finances. [redacted]

Although later and slower than other industrialized countries, Italy is now adjusting to the oil price hikes of 1979-80. Tight monetary policy is helping narrow the current account deficit, which hit a high of \$9.8 billion in 1980. Inflation declined throughout most of 1982 but began to climb again in late summer. As elsewhere, adjustment to higher oil prices has taken a toll on jobs and growth. We believe the evolution of the economy in 1983 will be similar to this year's record. The dim prospects are conditioned more by the inhospitable international setting than by domestic policy choices. [redacted]

Foreign Policy Priorities

New activism in Italian foreign policy contrasts sharply with inertia in economic policy. Involvement in the Lebanon multinational force, government willingness to deploy GLCMs at Comiso, and stepped-up foreign aid expenditures all attest to the new activism. We suspect a variety of factors accounts for this changed attitude to foreign affairs: desire to be included in high-level Atlantic Summits, fading memories of overseas misadventures during the Fascist era, concerns about the health of the Atlantic alliance. [redacted]

[redacted] the desire of the major parties to enhance their reputation as champions of Third World causes, and the de facto acquiescence of the Communists to these foreign policy initiatives. [redacted]

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