

Interview with Hermann Sileitsch-Parzer, *KURIER*, Austria, 07/15/19

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Hermann's questions are in bold fonts, followed by the answers I sent him on June 27, 2019.

Minibots: How serious are those plans to introduce a parallel currency? Or is that simply a means of piling political pressure upon ECB and European Commission?

The intellectual leaders of the no-euro movement who have been advising Salvini on economic policy have never made a mystery of their desire for Italy to leave the euro. Alberto Bagnai, now heading the Senate's Budget Committee, articulated his views in many posts in his very popular blog, and he coauthored research arguing that leaving the euro would cause nothing more than a 1992-93-like currency crisis. Claudio Borghi, now the head of the Chamber's Budget Committee, made his case for minibots in countless newspaper and TV interviews. He was very explicit on his vision of minibots as a parallel currency that would eventually facilitate leaving the euro. Even if both he and Bagnai claim that the government has no actual plan to leave the euro whenever faced with the question explicitly by the media, Borghi misses no opportunity to mention that minibots can be a useful tool to keep payments working "in case of trouble." Bagnai on one side claims that it would be suicidal for Italy to leave the euro unilaterally, on the other (even as candidate for the role of Minister for European Affairs) he openly pushes for collision with EU institutions. And Bagnai and Borghi are only the tip of the iceberg: Italy's no-euro movement includes a whole cast of characters of questionable economic competence who have become regulars in the media, and some of whom have just won seats in the EU Parliament. Interestingly, Mr. Giancarlo Giorgetti, the Undersecretary of State at the Presidency of the Council of Ministers, and thought by some to be a "voice of reason" is the Lega, explicitly discredited Mr. Borghi a few days ago by declaring to media "Is there still anyone who believes him?" But Giorgetti himself actually was quite supportive of Borghi's idea in the very recent past. It is as if the Lega establishment is playing a "bad cop-good cop" routine with the media, mainstream or social, presenting whatever face seems more convenient at each point in time to please its most extremist fans or the more moderate ones. But if there were no actual intention to push the country toward the "accident" that would cause it to crash outside the euro and the EU, why isn't Salvini getting rid of Bagnai and Borghi, removing them from their positions and marginalizing them?

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Some think it could be Italy's first step to prepare for an Euro exit. In official statements plans to ditch the euro are denied, in the past Lega politicians said different things. Is that credible or is there a hidden agenda? What's your perception?

This is tied to the previous issue: the best thing that can happen from the perspective of Salvini and the no-euro movement leaders is a crisis that they can blame on outside forces (the EU, Germany, finance...) and that leads to the collapse of the government with it being replaced by technocrats charged to take the painful steps to fix the mess. Salvini counts on riding this to massive electoral victory in the parliamentary election that would follow. And so much the better if leaving the euro and the EU ends up being part of the final outcome, as long as this can be blamed on outside forces in the eyes of the Italian electorate. Having Italexit pinned on them would be disastrous for the current government, but an “accident” followed by painful adjustment that can be blamed on the “evil EU, evil finance, etc.” would be ideal. Note also that besides Bagnai's and Borghi's views, a “plan B” for leaving the euro had been written and circulated already a few years ago by Mr. Paolo Savona, the current head of Italy's stock market watchdog, Consob, and this government's Minister for EU Affairs until he moved to the Consob. He proposed that Italy should act to exit the euro over a long weekend. For all these players, the game is to steer the country toward the “accident”, but positioning themselves to blame the counterpart if it finally happens.

Who are the driving forces behind those plans? Who is in the steering seat economically? Conte, Tria, Salvini?

I think I answered this question above. Salvini is clearly Lega's leader. The question he should be asked is the one above: If you really do not want to leave the euro and the EU, why don't you get rid of characters like Bagnai, Borghi, Savona—and others—who are only costing Italian taxpayers dearly with their shenanigans and their impact on the credibility of our commitment to the euro? As for Conte, there is an old Italian saying that I think is relevant: roughly translated, if you have a clay vase between two iron ones, when there is a tremor, it is the clay vase that gets shattered. Conte was put in place as PM to be the clay vase between those of iron, Salvini and Di Maio. Since the government was formed, Salvini has successfully cannibalized Five Star Movement votes also by presenting himself as tough on immigration (and the ongoing Sea-Watch crisis is helping him greatly). So, now Salvini is in a much stronger position than Di Maio, but that doesn't change the fact the Conte remains the weak player in that trio. Finally, Tria is a representative of an old-fashioned Italian economics academia that has zero or near-zero contact with the international academic world, and who was put in place after President Mattarella nixed Savona's candidacy as Minister of Economy and Finance. He is a voice of reason compared to Bagnai, Borghi, and Savona, but he is ultimately contributing to a disastrous management of Italian public finances and economic policy.

In economic terms: What would the minibots mean - could that elevate pressure on Italy's budget? Statistically it would add up to debt and deficit, wouldn't it?

The exact answer would depend on the specifics of the design (and therefore nature) of the minibots, if ever created. As Draghi put it, as of now, we can say that they would either be debt (and this would cause Italian government debt to increase to 135% of GDP) or money—a

parallel currency—and therefore illegal.

How is public opinion in Italy, could there be public support for an euro-exit? Surveys say a majority is still in favor of the euro (57 percent € is good thing for Italy, 30 percent bad thing, Eurobarometer Flash 473).

The majority of Italians are indeed still in favor of the euro, and this explains why it would be a disaster for Salvini and company of an eventual euro-exit were clearly pinned on them. Yet, a significant portion of Salvini voters wants Italexit and is strongly anti-EU. Salvini has successfully stoked anti-EU sentiment by exploiting the immigration issue, which Europe has been handling very poorly for a long time. Unfortunately, the latest, still ongoing crisis, in this area—the Sea-Watch 3 situation—is playing into his hands. The more Italians become skeptic about the EU, and the longer Salvini delays pushing the no-euro leaders to the margins, the higher the risk of the “accident.”

What is your guess, what would the consequences be: how would financial markets react, savers, capital flows, rating agencies, the ECB, the Commission?

Italy crashing out of the euro would be a major shock (based on existing treaties, it would also mean Italy leaving the EU). So far, we haven't seen significant contagion from Italy to other sovereign bond yields as a consequence of the current Italian government's shenanigans. The institutional setup of the euro area, and the arsenal of policy instruments currently available to the ECB and national governments, to respond to the effects of an Italian crisis is different from 2010-2012, when, for instance, the ECB'S OMT program was launched, and even from much of 2015, when the European Court of Justice confirmed its legality. If an Italian crisis had happened between 2010 and 2015, I think it would have meant the end of the euro and probably the EU. Now, I think it would be a major shock, but the euro and the EU would survive and move forward, with Italy the major loser (in a situation of capital controls and financial autarky probably for a significant amount of time). Given how long the Italian problem has been simmering, I suspect the ECB, European Commission, and national governments have plans in place for how to activate all the tools and facilities that would contribute to reducing the spillovers from the crisis. I cannot predict quantitatively how large these would end up being, but I am confident that the euro and the EU would survive.

In more general terms: It's hard to deny that for two decades Italy was (and is) having a hard time as a member of eurozone. GDP per capita has (at best) stagnated. Who's responsible—is it the euro? Is it something else?

The Italian economy has been stagnating along some key dimensions, and it has been building up its debt problem, since long before the euro. Dismal productivity performance began in the early 1990s, if not before. Government debt ballooned in the 1980s. Feeble or zero productivity growth is the number 1 source of Italy's stagnation, and this has nothing to do with the euro. It has its roots in a culture and an economic policy management that favors rent-seeking, lack of competition, and current government consumption rather than flexibility of the economy and investment in the country's future by putting resources into education, R&D, even infrastructure. In the past, devaluation was the drug that masked this problem, but condemned Italy to inflation

and high interest rates. The changes in the structure of international trade since the 1990s and the fact that recourse to devaluation would most likely lead to trade policy retaliation once Italy is no longer in the Single Market would drastically reduce the temporary beneficial effects of the drug now. Reality is that Italy must address its problems of real nature, as these would continue to hamstring the Italian economy regardless of the exchange rate regime. Sequences of governments since the 1980s, and especially since the early 1990s, and cultural characteristics are responsible for the current situation. Missing the window of opportunity created by the low interest rate environment of the first decade of the euro was a major mistake.

What would be the most important political measures for Italy to enhance growth ? What could/should the rest of the EU/eurozone do to help?

Focusing on debt reduction by reducing government spending should be a priority. Being serious about spending cuts would make it possible then to reduce the burden of taxation, which is objectively absurd. But you cannot cut taxes without first being committed to reigning in spending. Italian governments should move forward with structural reforms that facilitate business creation and dynamism, and that enhance competition. Lack of competition in provision of services is a major problem. Market exit and resource reallocation from dying entities to more productive, growing ones or newly created ones must become easier. We need to continue with labor market reform by facilitating female labor force participation. We need reform of the judiciary to streamline civil litigation, which currently takes ridiculous amounts of time. We need to stop thinking that government engagement in the economy is always the solution (and I say this as an economist who is far from being any kind of “market fundamentalist”). We need to stop wasting limited government resources on counterproductive subsidies like this government’s “Citizenship Income” (a payout to mostly Southern Italian Five-Star-Movement voters) or this government’s rollback of pension reform (a payout to elderly Lega voters). These measures—or the deficit-financed pseudo-flat tax that Salvini is spearheading—do nothing for growth. If the government wants to support growth from the demand side of the economy, it should do it by investing in human capital, research, infrastructure. I am convinced that other eurozone governments and the EU institutions would be ready to show flexibility if Italy were really committed to the reforms it needs. Sadly, I do not see any evidence of such commitment manifesting itself any time soon. And it is impossible to stop worrying about the “accident” as long as certain characters remain in their positions.

Thank you for the opportunity.