

Italy has enough resources to relaunch its economy: The country urgently needs projects, not ideological wrangling

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National governments and European institutions have mobilized and will continue to mobilize huge financial resources to counter the economic consequences of the ongoing health pandemic and to avoid a serious depression. Although the confused national political confrontation hinders the understanding of what has been done so far in Italy and in Europe, Italy already has an unprecedented amount of funds to combat the crisis.

To allow the Italian economic system to get out of the current slump and gradually resume its business safely, it is not enough, however, that these funds be large and accessible in the short term. It is also important that there are conditions for their effective, efficient and efficacious use. These conditions require that the financing and spending decisions, taken at European and national level, are not blocked by administrative obstacles or by small-time political speculations and, in the medium-long term, by the absence of a vision on the changes to be made. In both the short and long term, it is therefore necessary to create programs and use the funds for the preparation and implementation of these changes.

In the euro area and especially in Italy, the effectiveness of the public response cannot be limited to restarting activities. It must trigger a process of economic restructuring that focuses in particular on digital transformation and environmental investments. This means that the restarting of the European economy must be inscribed in strategic investment plans that are the result of a thorough interaction between the varied set of players, public and private, that is essential for the concrete implementation of these plans.

In this perspective, it is appropriate to elaborate concrete proposals to use the available resources before even asking for further funding from the European institutions and the Italian Parliament. This is why, in the following, we will first try to verify which and how many resources are already available for Italy. Then we will inquire whether the initiatives taken at national level allow for an appropriate and adequate use of the available resources. Only after trying to answer these two questions will we address the issue of what negotiating position Italy should take with respect to the choices made in the recent Eurogroup meetings and with respect to the discussion to be held at the next European Council meeting.

1. An unprecedented amount of resources to use

In the last forty days, the Italian government has deliberated public expenses and public guarantees on bank loans which, in principle, seem capable of warding off the first blows suffered by the economy following the pandemic. Budget expenditure, announced by the government and partly approved, is close to 3% of gross domestic product (GDP).

In the first “Cure Italy” Decree of March 17, measures to strengthen health services and support the incomes of employees and self-employed workers were launched; in addition, moratoriums were approved on the financial commitments of businesses and families towards the public administration and the financial sector to the economy; finally, timid first steps were taken to strengthen public guarantees on bank loans by strengthening the Central Guarantee Fund (CGF). This set of interventions resulted in an expected increase in the Italian public deficit, close to 1%.

As pointed out by the government itself, the so-called March decree immediately proved insufficient for at least three reasons. First of all, it did not address the problem of new poverty triggered by the collapse of 'gray' activities and the associated loss of precarious family income. Secondly, it did not provide sufficient financial aid to the sectors of Italian industry structurally affected by the pandemic (tourism, transport, trade). Finally, unlike the other major Eurozone countries, it has not exploited the European Temporary Framework to offer adequate public guarantees on bank loans and thus avoid the fall in loans to the 'real' economy.

All three of these aspects deal with dramatic economic and social problems. The third aspect, however, risked producing the peculiar effect of preventing Italian companies from exploiting one of the most important European interventions to counter the pandemic shock: bank refinancing of up to three thousand billion euro, offered by the European Central Bank (ECB) between March 2020 and June 2021 through LTRO and T-LTRO transactions at negative interest rates (between -0.25% and -0.75%). Indeed, European banks are willing to use such refinancing only if national governments provide sufficient guarantees to absorb most of the possible defaults of the troubled borrowers.

The second decree-law, adopted by the Italian government on April 8, provided - in principle - a satisfactory response to the problem, designing public guarantees on bank loans potentially equal to 400 billion euro¹. Through the CGF, the decree has strengthened guarantees on bank loans up to 800,000 euro and up to a turnover of borrowers of no more than 3.2 million euro, reaching a - direct or indirect - coverage of 100%. In addition, it authorized concession procedures without ascertaining creditworthiness for the part not exceeding 25,000 euro. Although through a somewhat cumbersome procedure, it then set a limited maximum threshold for interest rates on loans thus guaranteed. Through SACE, public guarantees have been extended for exporting companies, especially with regard

¹ As already mentioned by Bassanini-De Vincenti-Messori (cf. *il Sole 24 Ore*, April 12, 2000)

to the riskiest sectors and countries; and public guarantees fluctuating between 70% and 90% of bank loans were granted to national companies not falling under CGF management.

The granting of these latter guarantees requires, however, often complex paths that can be severely hindered by bureaucratic inefficiencies. Furthermore, the regulation does not protect borrowing companies from opportunistic behavior manifested by banks; in fact, it encourages the fixing of excessive financial charges and does not contrast the possible replacement of the pre-existing unsecured loans with the new guaranteed loans. The decree of April 8 has a general aspect that is unresolved: it does not earmark sufficient funds in the national public budget to make the offer of guarantees equal to 400 billion credible. The government said that this problem will be addressed with a third decree, the so-called April decree, which will be promulgated after the Easter period and which will result in an additional public deficit assessable around two percentage points of GDP.

These considerations highlight a potential increase in the national public deficit of around 55 billion euro by the end of April. Given the high public debt/GDP ratio that existed in Italy before the pandemic shock (over 135% of GDP), it is reasonable to ask whether such a decision is compatible with the sustainability of Italy's public budget. From a short-term perspective (throughout the current year), our response is positive both because of the purchases of sovereign bonds by the ECB and in light of the huge mass of loans and the albeit smaller amount of transfers that are flowing in from the European institutions. Thereafter, the question of an excessive debt repayment plan cannot be avoided.

2. European financing and transfers

As already mentioned, the ECB has decided to use the banking channel to inject up to three thousand billion euro into the European economy by June 2021; the feasibility of this potential injection has been strengthened by the loosening of the rules with respect to the collateral that the ECB accepts from the banks to refinance them: also "junk paper" and loans to businesses. In addition, the European Banking Supervisory Authority further incentivized banks to transform these re-financings into loans for the Eurozone's 'real' economy, freeing up 120 billion euro of bank capital through suspension of additional requirements, which should allow for a further one trillion in bank loans.

With other decisions made last March, the ECB also approved new programs for the purchase of public securities (as well as private securities, and even commercial credit) of the euro area. If these programs are added to the restoration of 'quantitative easing' from the autumn of 2019, by the end of December 2020 the ECB will introduce liquidity for approximately 1,100 billion euro, equal to about 7.3% of the euro area's GDP. Based on the criteria envisaged, and the new flexibility allowed, the European system of central banks could purchase about 10% of Italian sovereign bonds (i.e. 180 billion euro) by the end of the year. This should allow for the coverage of the increased financing needs of Italy's government.

European interventions go beyond the action of the ECB. They involve a series of initiatives that allow resources to be transferred to Italy. In particular, the European Commission has adopted more flexible

rules regarding state aid and released the available remainder of the 2014-20 multi-year budget, allowing it to be used immediately for the Covid emergency, for an amount of around 11 billion euro. It also removed the national co-financing constraint for Cohesion Funds and renounced asking for the return of nearly one billion unspent funds for 2019. If these funds were used as national co-financing from the Structural Funds, 1.46 billion euro would be released for Covid expenses. Finally, the Commission has allowed for wide flexibility (not only among regions, but also between state and regions and among items of expenditure) with respect to the destination of the still unused structural funds - about 20 billion euro, of which half is not assigned to specific projects, therefore freely usable.

A second set of interventions concerns three initiatives, which will be submitted to the European Council for consideration on April 23, relating to possible sources of financing for the Member States or euro-area businesses. The first source of financing focuses on the use of a portion of the total residual loans (about 410 billion euro) which the European Stability Mechanism (ESM) could provide upon issuing new bonds thanks to its already paid-up capital. These loans would have, as the only conditionality, the direct or indirect support of the health systems. The use of the ESM would allow Italy to obtain around 36 billion euro (equal to two percentage points of its GDP) at a favorable interest rate. The second source of financing is provided by European funds (SURE) intended for the protection of euro-area workers in a temporary situation of reduced work activity or unemployment due to the pandemic emergency. SURE is designed to provide assistance to euro area member states through loans granted on favorable terms up to a maximum amount of 100 billion euro, which mainly cover the extension of national compensation schemes following the reduction in working hours. The third source of financing is the increase (up to 200 billion euro) of the loan potential of the European Investment Bank (EIB) to activate and strengthen national investments in health systems and infrastructures.

Thanks to the interventions of this second set, Italy can benefit from additional European financing of approximately 80 billion euro. Added to the more than 32 billion euro of transfers available, the total amount adds up to more than 110 billion euro. This would allow to fully cover the greater public deficit already decided or planned by the Italian government. However, political decisions or intentions do not necessarily translate into concrete results.

At European level, the Italian government does not seem willing to use the funds disbursed by the ESM, to which the country is entitled, having itself contributed to the fund's capital, despite the fact that any conditionality has been virtually eliminated. We think that the Italian government should, if anything, commit itself to asking for the extension of the deadlines, well beyond the envisaged two years (30-40 years). The excuse to reject the ESM, whose initial treaty was approved in 2011 with the consent of the parties that are now in opposition, is that it would impose draconian conditionalities. This motivation is disproved not only by the experience of countries such as Spain that have resorted to the ESM for a specific purpose, but also by the availability of new precautionary credit lines that other European countries may also need. In fact, Italy's contrary position to the ESM appears isolated also with respect to the other countries of Southern Europe.

3. Will Italy know how to spend so many resources well?

In Italy, however, the political discussion is not focusing on how to use European transfers and financing. Instead, it is concentrating on the indispensability of a new European source of financing: Eurobonds.

In late April the European Council will discuss the establishment of the Recovery Fund that has just been drafted by the last Eurogroup meeting. In the French proposal, this fund should become a tool for centralizing investment and other expenditure at European level - very useful, but certainly not allocated to member countries. On the other hand, in clear synergy with this possibility, the European Commission is working on a new proposal on the multiannual budget of the European Union (EU) which would open the possibility of issuing European securities for a significant amount (up to 0.8% of EU's GDP); and these issuances could be destined precisely to finance the centralized expenses of the Recovery Fund. With respect to this proposal, it is not at all clear whether the Italian government is aware that this constitutes a shift of fiscal policy decisions at European level; and that the *funds obtained from the issuance of Eurobonds cannot be used to finance the Italian public budget*.

At national level, it would in any case be important to also focus government efforts on three crucial aspects relating to resources already potentially available:

- the effectiveness of the mechanisms for mobilizing these resources, so as to ensure their timely use;
- their destination for the most appropriate purposes to allow the resumption of production activities;
- the overall design, on the basis of which these resources can also be used to guide Italian economic reconstruction over the longer horizon.

With reference to the first aspect, it is necessary to avoid delays in providing loans to businesses and families. As mentioned above, the "Liquidity Decree" specifies the methods of granting, directly and indirectly, public guarantees on bank loans to businesses. Even if the dimensions are adequate for the needs of companies, some complications risk slowing down the procedures for granting guarantees. This is especially true for the guarantees provided by SACE, which include at least four different verification steps. It is also important that families also have quick access to low-cost financial aid to meet deadlines related to commitments entered into prior to the health emergency. A protocol for these credits, drawn up by banks through the Italian Banking Association, should be made operational quickly.

Again with reference to the first aspect, it is essential that the Italian government coordinate the national expenses for social safety nets with the European financing obtainable thanks to the SURE program. Furthermore, the Italian government should define, as soon as possible, a strategy for the use of European funds which have been made available to Italy through the residuals of the multi-year budget and through cohesion expenditure not yet implemented or decided; and it should encourage businesses, starting from those under its proprietary control, to prepare projects to access the new forms

of support provided by the EIB. Finally, the Italian government should transparently indicate its position regarding ESM funding. Any uncertainty, which would imply Italy's inability to use the resources already available, would undermine the country's credibility and its room for negotiation.

With reference to the second aspect, it is a question of defining an adequate infrastructure to allow for the relaunch of the Italian economy. In this regard, an "infrastructure" of interventions for the management of the infection is needed. It would include a) a "test and trace" system capable of identifying the infected people in the population; b) procedures for the safe reopening of the most relevant production activities and the logistical systems that support them; c) an articulated program of gradual recovery of the other activities for geographical generations-sectors-areas that allows to accelerate the relaunch.

A) As far as the "test and trace" is concerned, an ideal objective should be to apply the swabs to at least 100,000 citizens per day identified by activity, age, location (calculating the repetition of the tests every 20 days and about 40 million active Italians, the figure of security swabs should be twenty times higher). This exercise must give rise to the tracing, also through already available electronic applications, of citizens who have come into contact with those who have tested positive and to isolate people who can infect others. Ministerial and administrative structures, starting with the Ministries of Health, the Interior and the Regions, which must immediately prepare the necessary safeguards, must be provided with all the necessary resources, whether Italy wishes to use the approximately 36 billion euro made available for this purpose by the MES or to take the necessary funds from the state budget. A privacy-guaranteeing structure should be entrusted ex-ante to provide a data preservation platform and only ex-post to the protection-deletion of private data used by public institutions in the emergency phase.

B) For the resumption of the most relevant production activities it is essential that work environments be equipped in a way as to guarantee the necessary social distancing and, where this is more difficult, be equipped with safety devices for air circulation and filtering, protective clothing, including eye protection and filter masks. Space suitable for dressing and disinfection must be prepared. The production of the devices must be supported in the shortest possible time. Indications on production standards for the necessary controls must be provided immediately by the government also borrowing international examples. In this way, it will be possible to prevent the lack of government regulations from stopping producers for fear of legal disputes. To facilitate companies in directing their production to the necessary medical devices - from masks, to tests, to medical equipment - it is urgent that the State indicate the quantities of the necessary devices and coordinate their demand.

The provision of transport infrastructures that do not facilitate contagion is also part of the measures necessary for the relaunch of production. Bike paths and electric bicycles should be made available where possible. Subways and commuter trains must be multiplied in order to facilitate non-promiscuous transport.

C) A breakdown of the other activities by sectors and geographical areas can facilitate the test and trace operations related to the relaunch. It is therefore appropriate to define a form of geographical and selection graduality by sectors - production chains - and age of workers.

The tasks required of administrations are complex and interconnected. Therefore, the announced establishment of a 'technical' coordination committee at Palazzo Chigi (the Prime Minister's Office) is welcome, provided that it does not again translate into an oversized structure without powers. Its tasks must concern the concrete management of the programs described above. But Phase Two of the relaunch of activities must be followed by a subsequent phase that orients the abundant financial resources available today towards productions and specializations suitable for the future. In the coming months and years, European industry will likely want to bring numerous companies closer together, especially the "strategic" ones, companies that had left the European Union. The Italian economy must seize the opportunities that derive from this. Without a convincing horizon, the current difficulties may discourage many workers and producers to the point of dropping the level of the country's potential growth, and thus jeopardizing its well-being and stability.

In this regard, it is necessary to avoid the delay in the reopening of economic activities. Relaunching the country is essential to avoid discouragement and to keep businesses alive, businesses that would otherwise fail or be absorbed by foreign competitors. In this decisive step, everything possible must be done to prevent the relaunch from bringing new health risks. The lessons of the first wave of contagion must be recognized without hypocrisy: errors were made in the management of the health emergency and in the coordination between State and Regions. Now the priority is to orient the State-Regions dialogue in the best possible way to immediately make the investments that would allow for a safe relaunch without a restart of the infections.

4. Conclusions

Italy can dispose of adequate resources to face the emergency, set up the relaunch of economic activity and implement the 'transformative' investments necessary in the new post-crisis world provided that it abandons the spurious polemics that weaken its position in Europe and prevent it from using the resources available in the country itself.

The health and economic emergencies caused by the Covid-19 viral epidemic are likely to affect the institutional stability of the country and therefore its ability to respond to emergencies. It is a phenomenon that was already experienced in the past when economic and financial instability aggravated political instability and this in turn caused steep falls in investments, leading to a process that zeroed the country's growth. Now, faced with an unprecedented and possibly double-digit economic recession, the Italian "economic instability-political instability" vicious circle is likely to reappear with more dramatic effects and to make recovery, for which sufficient Italian and European financial resources are available, impossible.

The Italians' first reaction to the health emergency was an orderly response. In the months of February and March, even the tones of the political confrontation were contained. However, things have changed in the past few weeks. Two fault lines have opened up, recreating a breakdown of the common response and revealing serious uncertainty about the country's political development. The two fault lines are

represented by the State-Regions relationship and by the State-Europe relationship. In both cases, an ideological and personal antagonism has been reconstructed on these two lines, and has now taken on contrasting tones that are so strong as to appear difficult to reconcile. If this were the case, besides the serious effects of institutional uncertainty on Italy's economy, both the unity of the country and its permanence within the framework of the European institutions would be in doubt.