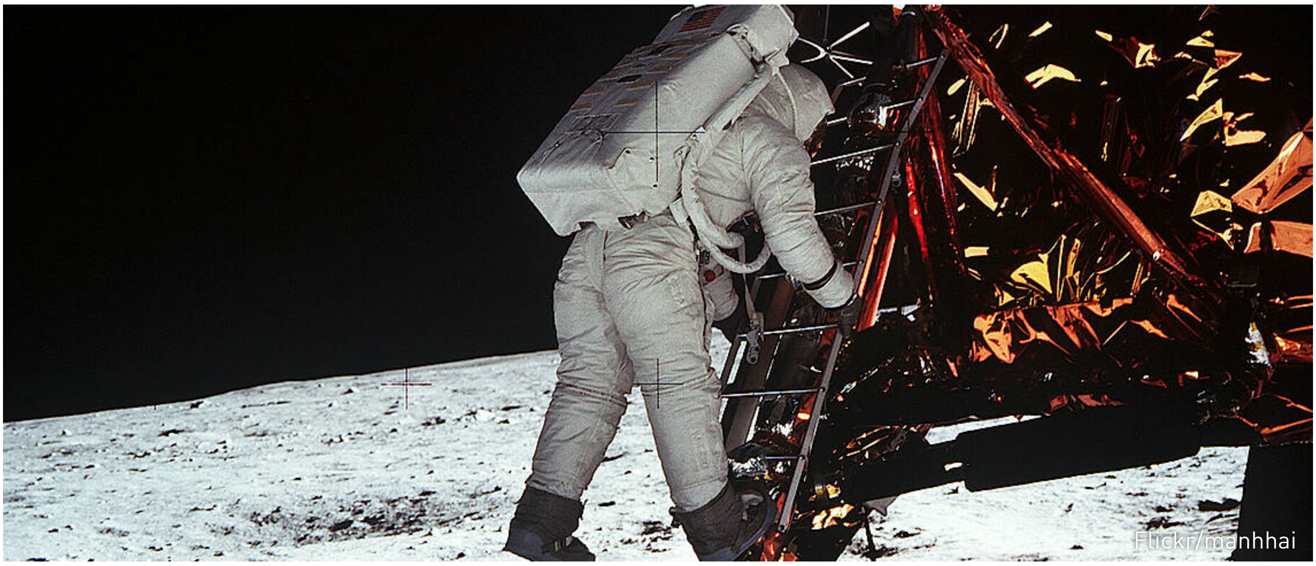
One giant leap for Europe...

...but one small step for Italy? While some celebrate the 'Mercron' reovery fund as a milestone, Rome's reaction is cautious

By Michael Braun | 22.05.2020



As giant a leap as Apollo 11 landing humans on the Moon?

Read this article in German.

'A bold and significant step toward a common European Union response to the pandemic that has devastated the continent.' In the very first sentence of his article on Politico, Italian Prime Minister Giuseppe Conte heaps praise on the Macron-Merkel proposal for a €500bn European recovery fund. In the second sentence, however, Conte adds the words: 'But it's also only just that: a step.'

The following question may be not as important for any other EU country as it is for Italy: What solutions will the EU find in the coming weeks to contain the economic and social consequences of the corona crisis? It was the first country to be hit by the pandemic with full force and the first to move to a lockdown – including the closure of large parts of its industry for six weeks. All forecasts predict a slump in GDP of around 10 per cent this year, while the recovery in 2021 could be slower than in other EU countries.

The outlook for Italy's government debt is correspondingly gloomy. Before the crisis it was already at 135 per cent of GDP and by the end of the year it will be around 160 per cent. The Italian government has so far launched two aid packages for the economy, the employed and the unemployed amounting to €80bn. But to get the country back on its feet, far greater resources are needed. Resources that the country alone cannot mobilise.

Against this background, the packages adopted so far in Brussels – the use of the European Stability Mechanism (ESM), the SURE programme for unemployment benefits and the funds of the European Investment Bank – were considered insufficient by Rome.

Prime Minister Conte and Finance Minister Roberto Gualtieri did indeed participate intensively in the negotiations on the design of the ESM intervention. Together with France and other countries, they achieved the renunciation of 'conditionality': the only condition is that the resources (for Italy about €37bn) must be allocated to the health sector. Nevertheless, Italy's government has so far shown little inclination to call on the ESM funds, even though the loans carry extremely low interest rates of 0.1 per cent.

How does a real recovery look like?

Above all, the Five Star Movement, which governs in coalition with the Partito Democratico (PD), is allergic to the European Stability Mechanism. Luigi Di Maio, Foreign Minister of the Five Stars, explained that the ESM is 'an antiquated instrument', an instrument of 'austerity, which has cut public spending'.

The PD sees a possible use of ESM funds in a more pragmatic light. But beyond the symbolism, beyond the memories of the Greek crisis and the Troika, the ESM does indeed have a big catch for Italy: The resources provided by the ESM are loans to the requesting country, thus further increasing its national debt – and in the long term, reducing its creditworthiness on the financial markets.

That's why Italy, together with France, Spain and six other EU states, pushed for a genuine European solution, the creation of a European Recovery Fund, financed by loans taken out by the European Commission. The fact that Merkel and Macron are now launching a proposal along these lines is seen by Italian Commissioner Paolo Gentiloni as 'extremely useful' and a recognition of the fact that 'we are in an exceptional situation that calls for an extraordinary response'.

In particular, the fact that the money from the fund – Italy is expected to receive €100bn – comes in the form of grants – and not as loans that in turn would put pressure on the national debt – is in line with Rome's approach.

When Prime Minister Conte welcomes the 'Mercron Initiative' on the one hand, while at the same time downgrading it to a mere 'step', then that's not because of the design of the proposed instrument. Conte's accusation goes in a different direction. He argues that the budget for all the European crisis responses that have been initiated so far is 'too low'; indeed, in recent weeks Rome has been talking about a European recovery fund of one trillion euros. Conte therefore concludes that it is now up to Commission President Ursula von der Leyen to present 'an ambitious proposal for the recovery fund and the Multiannual Financial Framework' in the next few days – and to 'remember that no European economy will recover on its own'.