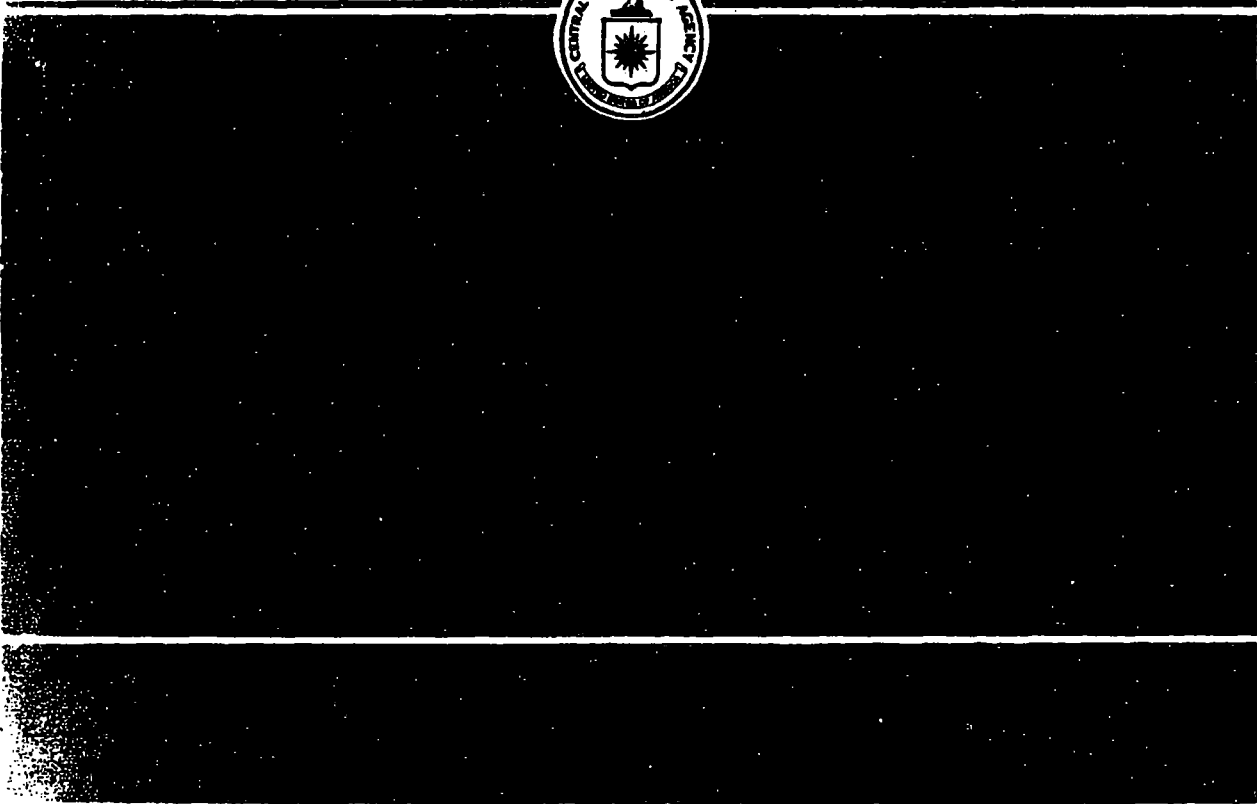


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Special Analyses

Italy: Political System Under Fire

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Special Analysis**ITALY: Political System Under Fire**

Scandal, economic necessity, and electoral declines are pushing the leaders of Italy's largest political parties toward reform. Although traditional politicians still shrink from serious change, anxiety about Italy's status in the EC will help Prime Minister Amato's reform agenda and make support for US policies less certain.

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Popular discontent with Italy's governing class continues to grow. Regional protest parties made dramatic gains in the national election last spring, and the political corruption scandal that began in Milan last February has spread nationwide. Well over 200 politicians, businessmen, and public officials have now been arrested or are under investigation for their part in a pervasive network of bribery and graft, much of it involving public funds.

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The scandal has dealt long-governing parties a mortal blow in prosperous and politically influential northern Italy. In local elections last month in Mantua, Northern League protest parties won 40 percent of the vote; the national coalition parties—the Christian Democrats, Socialists, Liberals, and Social Democrats—together got 23 percent. Local elections in December, which Rome had tried to delay, and a referendum expected next March on electoral reform are likely to deliver similar blows to Italy's traditional rulers.

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International markets fear that the enormous public debt will precipitate renewed attacks on the lira, similar to those that forced its withdrawal from the EC's exchange rate mechanism last month. Italian investors, worried that Rome will resort to controls on capital movement to save the currency, have been moving money abroad at an increasing rate. Foreign banks, embroiled in a dispute over the debts of a state-owned holding company, are refusing additional credit to Italy's largest public firms. The banks may even cut off short-term funds to the banking system and impound Alitalia's aircraft to force Rome to repay the loans.

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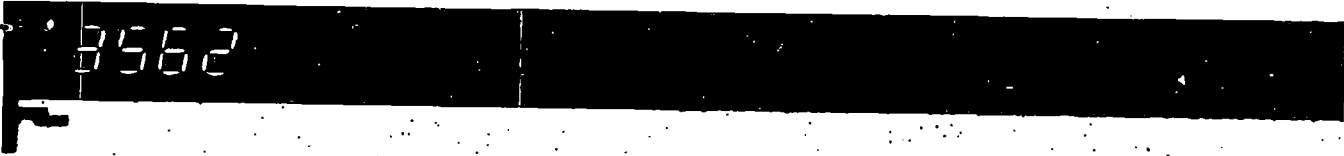
Crisis Management, Italian Style

Amato is trying to restore credibility to the old political process by showing that Rome is finally reining in public-sector spending. Undeterred by the largest display of labor unrest since the 1970s, the Prime Minister is forcing Parliament to accept an austere budget that includes unprecedented measures to dismantle pension and health

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benefits. He also is seeking an EC loan of roughly \$10 billion. He believes that Community preconditions for the loan will force Italy to adopt further controversial reforms and thus give him some cover from domestic critics. [Redacted]

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Public anger over the power of the Mafia—Italy's two top anti-Mafia prosecutors were murdered last summer—is forcing Rome to show surprising resolve against organized crime. The traditional parties have long enjoyed the benefits of votes controlled by the Mafia in southern Italy, but fear of further electoral gains by protest parties in the north may push Rome to keep up its anti-Mafia efforts. [Redacted]

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Implications for European Role

Against this backdrop of deep domestic trouble, changes in European political structures, and challenges from the Northern League, Italian leaders will be forced to make economic gains and continued inclusion in the EC core their main foreign policy goals. Such priorities will make Rome a less predictable and more troublesome ally for Washington. [Redacted]

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For example, Rome may look for economic benefits from closer ties to Iran or Libya, or it may become skittish about letting its bases be used for US out-of-area operations. The need for near-term economic assistance from the EC probably will make Rome less willing to make concessions on bilateral or GATT-related trade issues. Concern about arousing French or German ire probably will also constrain Italy's willingness to assert the primacy of NATO against any EC- or WEU-based security structure. [Redacted]

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