COUNTRY SPOTLIGHT ITALY

A new dawn?

Will Italy's referendum lead to the sun setting on the current period of economic and political volatility?

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Italians will go to the polls on 4 December and vote on changes to their country's constitution, changes that seek a smoother running of government. Italy has a bi-cameral political structure in which two Chambers — the Senato (upper house) and the Camera (lower house) — wield equal power. If the referendum passes, the Senato will see the number of its members reduced from 315 to 100 and some of its power devolved to the Camera. The same reforms were proposed in 2014 and were passed but lacked the 66 per cent majority that would have rendered them into law. Prime Minister Matteo Renzi has since reintroduced them through a national referendum and, despite later backtracking, said he would resign in the wake of a 'no' vote.

Voting impact

The results of a Renzi departure could be stark. In September, *The Economist* said it could, "[...] pitch the country back into political disarray and spark a wider crisis in the EU economy. Italy is a weak link: it has debts of 132.7 per cent of GDP and a banking sector weighed down by bad debts after years of sluggish growth." Current polls put the 'no' vote in a 4 per cent lead. However, surveys have shown that 19 to 42 per cent of the population are yet to decide how they will vote.

HSBC recently listed possible outcomes for the referendum. As reported in the British media, the banking giant laid out two scenarios for a 'no' vote and single scenario for a 'yes' vote. If the vote is 'no' and Renzi does step down, the bank predicts that a caretaker government would be nominated by President Sergio Mattarella with possible early elections next year, a high risk of ungovernability in the new parliament and a slowdown in reform. A 'no' vote, followed by Renzi staying, said the bank, would either see the party divided — leading again to early elections next year — or united, sticking with the Prime Minister to guide reforms into legislation. In both 'no' scenarios, equities are most likely to be immediately effected, due to quantitative easing by the European Central Bank. A 'yes' vote on the other hand, would cause a 'relief rally' across all asset classes, Renzi would remain in power with internal opposition weakened, and a stable

government can 'keep the reform momentum'.

There are no immediate effects on the pensions industry in Italy if the referendum fails and Renzi leaves. Likewise, there are no immediate effects for a 'yes' vote. The proposals are about the make up of government and are not concerned with a growingly-disproportionate older population, an under-funded and late-starting younger generation, or the parlous state of the country's finances. But for a state that needs desperate reforms to its economy, the ability to pass legislation quickly is paramount.

The European Association of Paritarian Institutions of Social Protection (AEIP) CEO Francesco Briganti says that Italy desperately needs financial stability in its markets, adding: "A more stable government would probably mean that legislation would not change every other year. That's important because pension reforms should look at the medium to long term. It would be undermining if a new government came in every 11 months and changed the reforms made by their predecessors. A more stable government would mean more laws that focused on the long term."

Alternative investments

The country has also seen more movement in recent years towards alternative investments. In 2012, Eurofer, the €883 million pension scheme for the rail sector, entered the alternatives market by investing in a pan-European estate fund. This followed similar investments made by Laborfond, which invested in private debt by regional firms and aims for a target allocation of 10 per cent in alternatives; Priamo, which began looking for a private debt manager in January to invest €15 million, or just over 1 per cent of its AUM, in private debt; and Solidarieta Veneta, which has made similar investments in locals SMEs. These moves followed adjustments in investment limits that were issued in November 2014 and came into force in May.

Olivieri Associates' associate Laura Brusco says: "The possibility for institutional investors — including pensions funds and private pension funds for professionals — to make alternative investments has been expanded. They've also, in some way, been regulated at European level with the advent of the European AIFM Directive on alternative investments that came into force on 23 July 2013."

Brusco maintains that even prior to the AIFM Directive, the Supervisory Commission of Italian Pension Funds released a resolution in 2012 that recognised the strong role that pension funds using alternative investments could provide in supporting the Italian economy.

"It's reasonable," says Brusco, "to expect a growing appeal in

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alternative investments from pensions funds and welfare funds because of the major performance effect that alternatives can have, albeit with increased, liquidity, and lower management fees, especially for certain asset classes."

She adds: "It is possible that a negative outcome of the forthcoming constitutional referendum could lead to an increase in the spread and thus the need of the state to finance itself through government bonds at higher rates. This would lead to a renewed appeal of traditional investments that could again attract the attention of institutional investors at the expense of alternatives."

Economic decline

These changes are taking place against a background of long-term economic decline. The Italian economy is one of the worst in Europe, having shrunk by 10 per cent since 2007. And despite some positive development in the last year following a triple-dip recession, recent reports stated that Q2 2016 had seen no growth. The government had said it expected 1.2 per cent growth this year, but many economists now believe it will be closer to two-thirds of that. And last year, youth unemployment reached 42 per cent. And anecdotal evidence suggests that many of Italian's younger population are leaving the country for work abroad.

"It affects enormously the pension system," says Briganti. "If the economy is bad, you come back to the issue of unemployment. When you have a DC system and people are entering the labour market late, they will end up with a low pension benefit. And because we don't have economic growth, we have problems with indexing pensions in general because they're linked to that. If growth is zero or negative, index-linked inflation is completely frozen."

In April, finance minister Pier Carlo Padoan said he supported an overhaul of the Italian pensions system. Details on what that overhaul may be are scant, however, although the National Institute of Pensions and Welfare voiced its support, too, for an urgent review of the system.

Briganti says: "The government should focus on economic growth, reduce unemployment, boost GDP, and talk about migration. We need migrants to make the economy work. The younger generation don't want to work in factories after getting a degree. But if we don't have an intelligent policy, who is paying the pension if the young people are few and leaving the country, and the old people are getting older? Declared official migrants were, in 2015, 8.3 per cent of the population, and they produced almost the 9 per cent of the country's GDP. In other words, they funded the pensions of 640,000 Italians. Like it or not, from an economic perspective, migration is economically convenient."

Both Briganti and Brusco say that when it is their time in the ballot box, they will vote 'yes'. "I will vote 'yes'," says Briganti, "because I think that — even if the reform is far from being perfect — that it will give more political stability. Of course, I would not vote 'yes' just to support the survival of Renzi's government."

Brusco strikes a similar tone. "I will vote 'yes', not only because of the correctness of the reforms but, above all, because I believe in the need to provide confidence to this government and to maintain political, economic, and social stability in Italy." ■