IN FOCUS

Investment Insights into Current Events

DiMeo Schneider & Associates, L.L.C.

Italy's Parliamentary Election

March 2018

Stephen Proffer, CFA
Institutional Consultant

Populist politics are back in focus after neither a single party nor a coalition obtained 40% of votes cast in Italy's Parliamentary election over the weekend. Early counts predict the anti-establishment Five Star Movement will gain about 32% of votes and the center-right coalition will gain 35% of votes. The two largest parties that make up the center-right coalition, Forza Italia and Northern League, are each projected to gain about 15% of votes. Either of these parties may attempt to form a government with the Five Start Movement. This would require the parties to reach an agreement on key issues such as fiscal and immigration policies as well as whether to remain in the European Union (EU). No doubt global investors and leaders of the EU will watch closely as this unfolds in the coming weeks (or months). In the EU's third-largest economy, only political uncertainty is certain for now.

Key Points:

- **Italy is likely to remain in the EU**. The Five Star Movement largely favored leaving the EU but reversed course leading up to the election. It is possible they renew exit-rhetoric to gain leverage in talks with the EU. However, leaving the union seems a low probability event. Center-left and Center-right political campaigns generally favor remaining in the EU, but also seek increased government deficits to spur economic growth. Although increases in deficit spending would be at odds with existing EU fiscal constraints, Real GDP in Italy remains 6% **below** 2008 levels and patience is wearing thin among voters.

- **Italian Bond yields were a mixed bag** following the election**.** The spread between German and Italian ten-year sovereign bonds yields rose 0.07% to 1.48% following the election results – modestly above its three-year average of 1.40%. Despite near-term uncertainty, the spread reflects investor confidence that the election outcome will not result in renewed talks of Italy leaving the EU. Furthermore, following last week's disappointing inflation data, political gridlock will give ECB President Mario Draghi cover to maintain monetary stimulus while Italy's leaders work toward political stability.

- **Italian equities, representing about 2% of the MSCI EAFE Index are modestly lower post-election.** Fueled by a chorus of campaign promises for fiscal stimulus and an uptick in economic growth momentum, they have been the best performing developed economy stock in the EU over the 12-months leading up to the election. Looking ahead, equity prices will adjust as elected officials attempt to coalesce key government issues. In the interim, we believe existing monetary policy and global growth trends will support Italian equity prices.

For information and assistance, please contact any of the professionals at DiMeo Schneider & Associates, L.L.C.

About the Author:

Stephen Proffer, CFA, Institutional Consultant

Steve provides investment consulting services to institutional clients and nonprofit organizations. He services clients by providing advice and expertise on asset allocation, portfolio design, investment policy statements, manager search process, fiduciary stewardship, and overall investment management. Prior to joining the firm in 2017, Steve was an Associate Client Investment Officer with Northern Trust Asset Management where he provided comprehensive investment management services to discretionary institutional client portfolios. Steve earned a BA in Economics and Finance from the University of Illinois Urbana-Champaign and expects to earn a Masters of Analytics from the University of Chicago in June 2018. He is a CFA Charterholder and a member of the CFA Institute, CFA Society of Chicago, and The Chicago Council on Global Affairs. Steve enjoys outdoor activities and spending time with family.