



ITALY: ANNUAL REVIEW FOR 1982  
SUMMARY

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INDEX	PA	Action Taken
	<i>PA</i>	<i>JS</i>

1. 1982 a difficult year for Anglo-Italian relations, but a good one for Italo-American relations. (Para 1). *See*
2. The year saw the fall of the Spadolini government, the return of Fanfani as Prime Minister, and changes within several of the political parties. (Paras 2 - 4). *(5)*
3. The security forces did well but organised crime and drug traffic remain major problems. The Bulgarian connexion difficult to unravel. Italy active in foreign affairs, especially over the Middle East. (Paras 5 - 7)
4. Pessimism in economic circles, and prospects for 1983 gloomy. Externally, economic relations tougher for Italy. (Paras 8 - 9).
5. In Anglo-Italian relations, the Falklands crisis and the EC budget problem were the two contentious issues, plus a small brush over bilateral Summits. A busy year for visits. Two major cultural events. The Calvi, May and Kiss Maerth cases attracted much interest. (Paras 10 - 17).
6. Commercially, 1982 saw a drive to improve our balance of trade with Italy, with several new initiatives. Trade policy work increased. (Paras 18 - 19).
7. The way ahead difficult to predict. Possible elections this Spring, but real change unlikely. Economically, external factors will have more influence. (Paras 20 - 21).
8. Valedictory remarks. (Paras 22 - 24).



BRITISH EMBASSY,  
ROME.

20 January 1983

The Rt Hon Francis Pym MP, MC  
Secretary of State for Foreign  
and Commonwealth Affairs  
LONDON

Sir,

ITALY: ANNUAL REVIEW FOR 1982

#### INTRODUCTION

1. 1982 was for the Italians the year they won the World Cup; they joined in the row with the Americans over the Siberian gas pipeline; they were alarmed by the failure of the rest of the world to lead the way out of recession; economic indicators were by winter extremely sinister; the 17 month run of Spadolini's 'lay' government ended in November and the veteran Fanfani's prospects at year's end were not at all bright. For us it was a year in which the Italians failed us partially in the Falklands crisis, and were no longer key allies in the EC where divergent interests developed. But for the Americans the Italians won points for neatly releasing General Dozier from his kidnappers, for staunchness over Comiso (Cruise missile site) and for a ready contribution to international forces in Sinai and Beirut, topping it off at the end of the year by Alitalia electing to buy 30 DC9-80s from MacDonnell Douglas. The Communists (PCI) worsened in their relations with Moscow and at home looked no nearer power; and President Pertini proved a bit of a folk-hero as a visitor to the United States. So Italy's stock stood higher in Washington than in London. The year ended with an intriguing question mark as the 'Bulgarian connexion' (with the Pope's Turkish assailant) took the headlines.

#### POLITICAL - INTERNAL

2. Up to August it was Spadolini's year. He was popular and flourished at first; but deep divisions between the main coalition parties, Christian Democrats (DC) and Socialists (PSI), prevented /him from



him from carrying out vigorous economic remedies. His coalition became increasingly unmanageable and a crisis came in August. Pertini gave him another chance but the same divisions prevented real changes and the 'Spadolini bis' Government never got going. The DC and PSI put electoral considerations first - the Socialist leader Craxi being impatient for anticipated elections - and brusquely pushed Spadolini towards the door. For a man whose party had a mere 3% of the vote he had lasted long; he went with some bitterness and - perhaps wisely - declined to join the new coalition. He had cleaned up after the P2 (masonic lodge) scandal and had some successes against terrorism. He changed the style, if not the substance, of government for the better. He was basically pro-British.

3. The choice of an old DC war-horse, Senator Amintore Fanfani, to succeed him suggested that President Pertini did not want a mere caretaker government, playing out time until spring elections. With the PRI out, the coalition was now four-party (DC, PSI, PSDI, PLI). But Fanfani had inherited a worsening economic situation and the underlying political tensions (especially DC/PSI) remained. Craxi continued to behave more like an opposition leader than a coalition colleague. Some key Ministers of interest to us remained - Colombo at the MFA and Lagorio at Defence.

4. There were some changes affecting the parties during the year. The PCI fell out more sharply with Moscow after the imposition of martial rule in Poland. The party is disoriented and its spring Congress will be important. The clever Ciriaco De Mita replaced the drab Piccoli as Secretary of the DC and has already improved its fortunes, by embarrassing Craxi on some issues, and by bringing more unity to a faction-ridden party. The PSI tried in vain to force premature elections, and will not have escaped some opprobrium. They criticised the DC on several foreign policy questions (eg El Salvador, Falklands, Siberian pipeline and now the 'Bulgarian connexion'). The experiment of a 'lay' (non DC) Prime Minister, with some personal success, did not help the formation of a 'lay bloc'.

#### TERRORISM AND ORGANISED CRIME

5. The liberation of General Dozier gave a great fillip to the security forces. There have been continued confessions by repenting



terrorists and many arrests. Nearly 2,000 are now held, mostly from the left. The Red Brigades are weakened but not destroyed. Old-style Mafia killings have continued, and reached crisis proportions in Palermo and Naples. Drug traffic is a major problem in Sicily and drug addiction is a disquieting feature in many cities. The Bulgarian rôle in the Turkish assailant's attack on the Pope is under investigation and the PSI had criticised the government for failure to respond more vigorously. Colombo is taking it cautiously, and magistrates' work may go on for months. The trail from Sofia to Rome is one thing, but the possibility of a trail back to Moscow quite another.

POLITICAL - EXTERNAL

6. The Italians have been active particularly over the Middle East crisis. Arafat saw the Pope and President Pertini in Rome, and met Colombo twice. The Italians participate in MNF, UNIFIL and MFO. The Italians got kudos with the Americans; and are exploiting the commercial spin-off. But Italy's armed forces remain below par despite increasingly vocal efforts by the generals to get more money. The peace movement has so far caused surprisingly little trouble, because the PCI - while deeply involved - are restrained by fear of being seen as too pro-Soviet. The pipeline dispute with the Americans split the coalition, and Spadolini made an effort in Washington to get an 'exemption' for Italy to supply compressors from Nuovo Pignone; but the contract with the Soviet Union for gas supplies has still been held over. In general, the Italians asserted themselves more whenever domestic political infighting permitted.

7. As 1983 began, I found Colombo preoccupied over the international economic scene and the Soviet propaganda campaign on missiles etc. He deplores the lack of American leadership on trade/money matters, the disarray in the EC and the nationalistic tendencies members are showing, and the dangers of protectionism. He thinks a single united allied response to the Soviet Union is called for, otherwise we are in for trouble in 1983; our policies should be concerted in NATO.

/ECONOMIC





## ECONOMIC

8. Internal. The longer the world recession lasted the harder Italian industry found it to scramble through by improvisation. By the year's end pessimism was felt in usually resilient Milan and other productive centres. Industrial production is falling. Heavy industry is in particular trouble and the state sector seriously bloated. GDP will have increased only marginally. Inflation, though lower than 1981, is still running at some 16%. The strength of the dollar increased the fuel bill. The PSBR got out of hand. Huge trade and balance of payments deficits built up. Exports faltered. The cost of debt-servicing increased. The lira lost ground against other currencies, but has held steady within the EMS since the 2.75% realignment in June. Spadolini was foiled in his attempt to cut the public sector deficit by Socialist reluctance to cut spending. Similarly he made virtually no progress on the key problem of excessive labour costs. The unions naturally fight to keep a system in which indexed pay rises and contractual increases match or exceed inflation. The employers gave notice that indexation would cease on 20 January 1983. The chances of a voluntary agreement between employers and unions seem poor and Fanfani may have to intervene and try to succeed where Spadolini failed - a tough task in a deep recession. The fundamental problem of lack of indigenous energy supplies was not tackled. No final decisions have been taken on siting of nuclear power stations. The Algerians will supply gas at too high a price. Siberian supplies are not yet secured. Prospects for 1983 are bad and it began with a rash of demonstrations and strikes against Fanfani's economic reforms.

9. External. Life got tougher for Italy in the outside world. They strongly resisted pressure in the EC to cut back steel capacity. They greatly feared the agricultural effects of Spanish and Portuguese accession. They joined us in fighting the Americans over the Siberian gas pipeline, having a greater interest than ours (both in the gas and in equipment for the pipeline). They resent US attacks on the CAP. Like us they were alarmed by French protectionist symptoms.

/ANGLO-ITALIAN RELATIONS



## ANGLO-ITALIAN RELATIONS

10. 1982 was the only difficult year I have had here since I came in mid-1979. 1980 was a bonus year for Anglo-Italian relations. 1982 saw two sharp differences emerge.

11. The first was the Falklands crisis. This became entangled with real Italian interests and with party politics. There are huge numbers of Italian emigrants in Latin America, particularly Argentina. There are proposals for making it easier for Italians abroad to vote in elections here. 5% of Italian trade is with Latin America. Most major Italian companies have subsidiaries in eg Argentina, Brazil. The Argentines lobbied extensively here through delegations, parties, trade unions, commercial and even Rotarian links. The media tended to put the Argentine version first. So a major campaign was necessary by this Embassy, and I had arguments with many including Craxi, who for party politics, prevented Colombo and Spadolini from renewing economic sanctions - though they (and Pertini) were very apologetic, and Craxi has since tried to excuse himself.

12. We had more trouble when Colombo (advised by his Ambassador in New York) seemed set in October to vote on the Argentine side at the UN. He had a fixation that Europe's relations with Latin America must be repaired and voting against the Latin Americans must be avoided. We had to get Spadolini, aided by Pertini, to restrain him and we secured an Italian abstention. Britain won a lot of admirers here for a brilliant military operation but the general feeling was that it was an 'absurd war' which put the Italians in a very awkward spot. The MFA believe that in the long run there will have to be an arrangement which will save us from having to keep the islands as a fortress. The Italians have their own problems over the 'desaparecidos' of Italian origin, whose cause the PSI have shamelessly been exploiting.

13. Colombo also had to differ with us over the EC budget problem where again he had an obsession. It was that he could not be seen to be paying any part of a German bill with Italian money. So we were in 1982 far from the happy situation of 1980 when Cossiga and Colombo worked hard to help the Prime Minister. In a more difficult economic climate the Italians have also had to fight their corner

/more strongly



more strongly and Colombo has been less able to ignore the views of the other parties. Italy's interests differ from ours over eg enlargement, Mediterranean products, farm prices, steel, energy policy, 1% limit. Colombo has also become disillusioned about lack of progress in consolidating the EC. He wants a strong cohesive Community to deal firmly with the United States and stand up to the Soviet Union.

14. We had a little brush over the frequency of Summit meetings. In the Cossiga hey-day it was agreed to promote this to a twice-a-year basis. In 1982 London wanted to revert to a once-a-year pattern. This would have humiliated the Italians and it was agreed to seek the desired result by slippage. Spadolini desperately wanted to visit London before the end of 1982, just as he visited the US, and was upset at our response. Fanfani has been invited to visit London early in the New Year.

15. It has been a busy year for visits, mainly in this direction. You came in July with the Prime Minister and Sir Geoffrey Howe. Other Ministerial visitors have included Mr Nott in February, and Mr Prior and Mr Tebbit in October. Prince Philip was here several times, and there were visits by Captain Phillips, Princess Margaret and the Duke and Duchess of Gloucester.

16. Crime. No Italian believes that banker Calvi enacted an elaborate suicide under Blackfriars Bridge. The SUNDAY TIMES does not believe that Jeanette May and her companion died a natural death. Miss Gaby Kiss Maerth was released by kidnappers but only after payment of a (modest) ransom. Miss Carol Compton is still in custody charged with burning cradles and not, as the British press have it, with witchcraft.

17. There were two major cultural achievements. First a successful visit by the Royal Ballet to Venice and Rome, coupled in Venice with fund-raising galas graced by Princess Margaret. There were innumerable administrative obstacles in both cities, causing us and the British Council much travail. But it was the sort of major British event which I have been trying to get staged here. Secondly, on 16 November Fanfani, the Prime Minister-designate, unveiled at

/Porta Pia



Porta Pia a major Henry Moore sculpture set in the ornamental pool in front of Basil Spence's modern building. This gives a finishing touch which was lacking and the two men's work complement each other well. The sculptor was particularly moved by the thought that his statue is juxtaposed to the monumental gate of Michelangelo, who has long inspired Moore. I am deeply grateful to the Henry Moore Foundation for this generous loan.

18. Commercial. Britain's exports to Italy in the first ten months of 1982 were worth £111 million more than the same period in 1980. (1981 figures not available). We were Italy's fifth biggest supplier (apart from oil) but the balance of trade remained in her favour. We have sought to prepare for an eventual upturn by various initiatives. There have been a series of technical seminars yielding good results (those in Rome listed at annex A). We have continued to attack important markets where we have no consular or trade offices (this year Modena and Bari) by 'saturation exercises', ie concentrated industrial visits by commodity experts, promotions of consumer goods and 'invisibles', technical presentations, and a concerted drive with other British interests. The technique pays off and will be repeated. British firms are sometimes afraid of conditions in Italy but such firms as eg Unilever, Rank Xerox and Glaxo prosper and Italy is now BL's second biggest overseas market, selling over 32,000 cars here in 1982. Those in problem sectors have difficulties, eg Cucirini Cantoni Coats, especially in sacking staff.

19. We had to battle hard to get the Triumph Acclaim admitted as the Italians thought it basically Japanese and so a threat to circumvent their quota arrangement which virtually excludes Japanese cars. We have some hopes of selling Land-Rovers to the Italian forces, which would be a big breakthrough. We ganged up with other Western countries having major airlines to seek better conditions at chaotic Rome airport. The EH-101 collaborative (helicopter) project has run into difficulties in both countries, but I hope it will go through. Protectionism is on the increase in Italy. Trade policy work, ie in defending our interests, has much increased.

LOOKING FORWARD

20. This is rash in unpredictable Italy. I did not suppose that Spadolini could survive so long. I thought Fanfani would not accept

/the job





the job unless he were confident of staying a while and making a success of it. Yet who could in the present economic climate? Few expect him to last very long. There may have to be elections in the spring. But they will change little. The DC may, under De Mita, do better than expected - before his advent they feared a slight decline. The PSI may, after Craxi's recent clumsy overbid for power, not gain as much as they hoped. The PCI, liable to lose another few points, may yet avoid doing so if unemployment is worse and austerity measures bear hard on the workers. The 'lay bloc' is still wishful thinking, the 'historic compromise' unlikely to come back into play. Marginal changes are the likely result, and more unstable coalitions, or fragile minority administrations.

21. One might say that in an era of economic growth the less interference by government the better, so that the Italian mercantile genius may flourish. But in recession firm government measures, especially of austerity, are required and it is hard to see Italy producing governments capable of this. I have seen five different Prime Ministers here, but not much sign of real change. What happens here in 1983 will depend more on Germany, the United States, Japan and other leading economies. Colombo remains at the MFA, and that is to our advantage. On major issue of the day he will be likeminded - a fervent European but well aware of where Europe must work with the US. On INF basing Italy remains firm, but backsliding in Germany could cause trouble, especially if the PCI decided to back the peace movement more strongly. They can get workers out in the streets when they want.

#### LOOKING BACK

22. To avoid burdening you with a valedictory despatch I will append here a few retiring remarks. I pay a warm tribute to the staff all over Italy for their support, and indeed to all those with whom I have worked in London and abroad since 1947. And to my wife who has devoted herself wholeheartedly to the Service since we set out for Turkey two days after we married. I belonged to the post-war entry now leaving the Service. It is only in this, my last post, that my war service has been of direct relevance; the Italians are generous still in regarding one as a 'liberator'.

23. Serving abroad in posts which attract many visitors one is

/struck by



struck by the high prestige of Britons from many walks of life; also by the affection for Britain which many foreigners retain, and perpetuate by sending their young to learn English. The Italians in particular have an admiration for our institutions and sturdier qualities. Unfortunately the media highlight our racial, social and economic problems, and foreign correspondents in London are often uncharitable, and some foreign Ambassadors cynical. We are regarded here as worldlywise and experienced, and yet apt to be insular and 'un-European'. It is good to see nowadays a new generation of young Britons coming to work in Europe who do learn the local language and do not remain exclusively in the 'British community'.

24. Our friends, and there are many of them in Italy, would like to see us play a bigger part in world affairs, fearing undue dependence on the United States. They are nervous when they see signs of Little England-ism. My successor will be working in a favourable environment, despite the difficulty of deciphering Italian politics and understanding precisely how a country which has so many imperfections can enjoy life so much.

25. I am sending copies of this despatch to representatives of all other EC capitals, to Washington, Moscow, UKDEL NATO and to the UKREP EC, and to the Holy See.

I am Sir

Yours faithfully

A handwritten signature in blue ink, appearing to read 'R Arculus', with a horizontal line underneath.

R Arculus

TECHNICAL PRESENTATIONS ETC AT HM EMBASSY ROME IN 1982

Date	Company	Event	Results
17 February	Group 4 Security Ltd	Presentation to Italian Minister for Posts & Telecommunications and Government Security Equipment Commission on Group 4 services and equipment	Group 4 currently tendering for substantial Government contracts
19 April	Rank Wharfedale Ltd	Presentation and demonstration of hi-fi equipment	Presentation marked the 50th anniversary of the UK company. Good press coverage and audience turnout.
11 May	Galt Glass Laminates Ltd	Presentation to Carabinieri of bomb-disposal equipment and protective clothing	Immediate order placed
14 June	British business community in Rome	Presentation by Embassy staff on Falklands crisis	
17 June	Marconi Ltd	Electronic measuring equipment	Orders placed immediately after presentation. Enormous interest shown in the test-equipment displayed.
24 June	Mangood Ltd	Electronic traffic equipment	The Italian agent reported the negotiations in course with a*
14 July	Rolls Royce Ltd Aero Division	Presentation to Italian Ministry of Industry officials on past, present and potential aero engine supplies to Italy	Rolls Royce in discussions on possible further collaboration for supplying engine to EH 101 helicopter

\* a number of the organisations invited to the presentation.

Date	Company	Event	Results
15 July	ICL Ltd	Presentation of mini-computers	ICL following up contacts established during the presentation with ENEL, the University of Rome and the CNR.
28/30 September	Bevan Funnell Ltd	Display of high quality furniture at Villa Wolkonsky	Entire display sold to local furniture shop and potential orders from various Embassies
6 October	British Tourist Authority	Display and reception to mark their 50th anniversary	
13 October	Mangood Ltd	Presentation to Ministry of Transport, State Railways, etc of railway weighing equipment	Negotiations continuing
15 November	Land Rover Ltd	Presentation and demonstration to Italian Armed Forces	Strong expression of interest in Army, Carabinieri, etc acquiring Land Rovers
15 November	Racal Ltd	Presentation of mobile 2-way radio to Italian Armed Forces	Company asked to tender for supply of other equipment as an indirect result of presentation
15 November	Hotspur Engineering Ltd	Presentation of 6-wheeled Land Rover conversion to Italian Armed Forces	Negotiations opened for supply of 20 vehicles to Italian defence equipment company as indirect result of presentation
16 November	Land Rover Ltd	Presentation to FAO personnel	Direct contact established between company and FAO Purchasing Dept.

.../...



Date	Company	Event	Result
16/17 December	Royal Ordnance Factory	Presentation and live demonstration of Arwen riot control gun and related equipment to Italian Ministry of Interior, Police and Carabinieri	Continuing discussion with Ministry of Interior
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17 June	Marconi Ltd	Electronic measuring equipment	Orders placed immediately after presentation. Numerous letters shown in the test-equipment displayed.
24 June	Waggood Ltd	Electronic traffic equipment	The Italian Agent reported the negotiations in course with
14 July	Sella Hayes Ltd Aero Division	Presentation to Italian Ministry of Industry officials on past, present and potential aero engine supplies to Italy	Sella Hayes in discussions on possible further collaboration for supplying engines to the Italian helicopter

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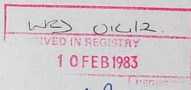
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Foreign and Commonwealth Office *See*

London SW1A 2AH *(5)*

7 February 1983

Sir R Arculus KCMG KCVO  
ROME




*Dear Ronald*

ANNUAL REVIEW FOR ITALY

1. Thank you for your Despatch of 20 January, which drew together in admirably comprehensive form the many varying threads that make Italy such a fascinating country. 1982 was a full year. Scarcely a day passed when some aspect of Italian policy or internal event did not feature prominently on the world scene and in the media, and the content of the Despatch will interest a wide readership. I am therefore arranging for it to be printed as a diplomatic report.
2. Much of the media attention devoted to Italy was a direct result of crime and terrorism. Last year will be remembered as the year of police success against terrorism. From the release of General Dozier onwards they went from strength to strength, and the Red Brigade threat has now been seriously weakened, for the time being at any rate. It may be partially luck that these successes took place during Senator Spadolini's period as Prime Minister, but at least he will be remembered for having achieved two of his four initial objectives ie control of terrorism and some success on the 'moral question', P2. These bright spots help balance the lack of progress in tackling Italy's economic ills.
3. Poor performance in the economic field has proved the undoing of successive Italian governments, and your gloomy analysis of the present position offers little encouragement for Fanfani's prospects. Despite the early boost for his administration provided by the successful conclusion of the scala mobile negotiations, this agreement alone is unlikely to ensure that inflation targets are met. What is more, public expenditure concessions appear to have made control of the PSBR even more difficult, while the external position has begun to deteriorate again. I fear that you are right in foreseeing little chance of an Italian government capable of taking sufficiently firm measures.

4. If 1982 was the year of success against terrorism, 1983 must surely be a year for concerted effort against the Mafia and organised crime. No real progress seems to have been made against this cancer. Effective action is long overdue. Otherwise organised crime may in the long run pose a bigger threat to civilised life in southern Italy than terrorism.
5. The year has begun well in terms of UK/Italian relations. We look well set for the next Anglo-Italian Summit taking place as planned on 25 February. The wider Ministerial participation is welcome, and complements the bilateral meeting between Mr Pym and Signor Colombo on 13 January. Other bilateral Ministerial exchanges early in the year look like giving UK/Italian relations a high profile. Senator Spadolini was, incidentally, wrong to think that we refused him a Summit last autumn. That was not the case. The Prime Minister's programme was simply too full to allow a full-scale Summit, so we could not offer dates immediately, and by the time we were in a position to do so his Government was on the way out. Meanwhile, you will recall that it was always our position that the frequency of Summit meetings should be allowed to slip to one a year in such a way as to avoid offending Italian susceptibilities.
6. Another matter, apart from the Falklands, on which there were differences is the Community budget. These will continue since most solutions to our problem are likely to cost Italy something. We hope the Italians have now taken the message that we share the Italian desire for the healthy development of the Community but we shall have to continue to ram home that the problem of budgetary imbalances must be solved. This cannot be done simply by expanding Community resources.
7. Predictions for 1983 are as usual tricky. We look forward with interest to the next elections, whenever they may be. The Socialists are risking much by adopting such a high profile. Craxi's tactics may backfire. He has not yet faced an election as the leader of a government party. The PCI has had the challenging task of providing the opposition at the same time as proving the Party's respectability. The March Congress will be important. Other parties of the left are demoralised, and it will be interesting to see how the protest vote is cast.

/8. 1982



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8. 1982 was on balance a reasonably good year for UK-Italian relations, despite hiccups. We have firm hopes on the industrial collaboration front (EH 101, Airbus etc) where we shall have to work hard to get what we want. We need to take care to avoid exaggerating the chances of success.

9. I hope that this letter will reach you before your departure from Rome. Your Annual Review was your last Despatch. It was appropriate as it recorded a catalogue of successes; ministerial visits, collaborative projects and commercial achievements. Your series of Despatches on areas of interest to us such as Italy and the Mediterranean, the Christian Democrats and the PCI have been greatly appreciated. May I thank you and send my best wishes for the future?

*Yours ever*

*A M Wood*

A M Wood  
Western European Department

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Mr Goodison

9/1  
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Mr Osborne

## ANNUAL REVIEW FOR ITALY

- A (1) 1. I submit Sir R Arculus's Annual Review for 1982. Advance copies have been sent to Private Secretaries, Under Secretaries and to interested Departments and their
- B (6) comments were incorporated in my reply, a copy of which is attached. The Despatch will be printed in the diplomatic series.
2. The Despatch is well drafted. It provides a full record of events in Italy in 1982, but contains few new insights. The reply is rather longer than is normally the case because the final paragraphs of the Annual Review comprise Sir R Arculus's valedictory Despatch. He retires on 10 February.

A M Wood

A M Wood  
 Western European Department

7 February 1983



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Mr Osborne, WED

## ANNUAL REVIEW FOR ITALY 1982

1. This annual review is a valuable appreciation of events and attitudes in Italy in 1982, and I agree with the points in your draft reply.
2. I would suggest expanding the reply slightly to include some thoughts on political developments, although, as Sir R Arculus says, to look forward in Italy is rash. It is as difficult as ever for an Italian seeking change to know how to place his vote and it will be particularly interesting to see how the left-wing parties perform in the next elections, and what happens to the protest vote. The only party of the left which is not demoralised, it seems, is the PSI which has been playing a high-profile and sometimes maverick, role in government. But Sig. Craxi has yet to face a general election as the leader of a government party (the PSI were out of government from October 1974 to April 1980) and it is difficult to know if his party's role in government will be a help or a liability. The Republicans will also be hoping that Sig. Spadolini's successes will attract more voters than are put off by his abortive second government and failure to deal with the economy.
3. As the despatch indicates, the main party of the left, the PCI, seems to have run out of steam and road, faced with the perennial problem of simultaneously having to prove its respectability and providing the opposition. The historic compromise has proved unacceptable to the DC and unpopular with the PCI rank and file and for the time being the Socialists are refusing to play ball with any sort of alternative involving the left. The PCI's March Congress will be important, as Sir Ronald says. The Radicals, who picked up so much of the protest vote in 1979 have lost some of their former impact after splits in the autumn and winter. Some of their vote could conceivably go to the Socialists, for their obstructive behaviour in government, or perhaps the protest vote will be used in more abstentions, spoilt papers etc. (the "invisible" party). As Sir Ronald says, it looks like more of the same thing with minor variations.
4. On a minor drafting point I think the effect of the second sentence of paragraph 2 of the draft reply is a little extreme and I would rephrase it to read "last year

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MR. GABORNE, WED

will be remembered as the year of police success against terrorism".

ANNUAL REVIEW FOR ITALY 1983

5. If this is Sir R Arculus' last despatch would it be appropriate to express our appreciation of the excellent despatches and letters on particular subjects of interest carried out during his time as Ambassador eg. the despatches on Italy and the Mediterranean, and the PCI? We have obviously also benefitted from Sir Ronald's special relationship with President Pertini.

2. I would suggest expanding the reply slightly to include some remarks on political developments, although, as Sir R Arculus says, to look forward in Italy is rash. It is as difficult as ever for an Italian seeking change to know how to place his vote and it will be particularly interesting to see how the left-wing performs in the next elections, and what happens to the vote. The only party of the left which is not demoralised, it seems, is the PSI which has been giving a high-profile and sometimes maverick role in government. But Sir R has yet to face a general election as the Research Department

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out of government from October 1974 to April 1980 and it difficult to know if his party's role in government will be a help or a liability. The Republicans will also be hoping that Sir R's successor will attract more voters than are put off by his previous second government and failure to deal with the economy.

3. As the despatch indicates, the main party of the left, the PCI, seems to have run out of steam and road, faced with the perennial problem of simultaneously having to prove its respectability and providing the opposition. The historic compromise has proved unacceptable to the DC and unpopular with the PCI rank and file and for the time being the socialists are reluctant to play ball with any sort of alternative involving the left. The PCI's March Congress will be important, as Sir Ronald says. The Radicals, who picked up so much of the protest vote in 1979 have lost some of their former impact after splits in the autumn and winter. Some of their vote could conceivably go to the socialists, for their obstructive behaviour in government, or perhaps the protest vote will be used in more substantial, specific papers etc. (the "invisible" party). As Sir Ronald says, it looks like more of the same thing with minor variations.

4. On a minor stylistic point I think the effect of the second sentence of paragraph 5 of the draft reply is a little extreme and I would rephrase it to read "last year

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- 7 FEB 1983

Mr Osborne (WED, W67)

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1. Economic difficulties have played a major role in the demise of successive Italian governments. HMA Rome discusses the economic situation only briefly in his despatch, although Mr Simpson-Orlebar examines the subject in greater depth in his letter of 17 January to Mr Thomas. A separate response will no doubt be sent to this earlier correspondence, but you may wish to make some further mention of economic prospects in your draft response to the Annual Review. I attach a paragraph to meet this requirement.

*incorporated in  
draft*

2. ESID will be commenting more fully on Mr Simpson-Orlebar's observations in due course. However, it is clear that despite the apparently successful outcome of the debate on the structure of the scala mobile very considerable economic problems remain. The context is for a third successive year of stagnation. Restrictions applied to the personal sector are likely to limit growth in consumption to only 0.5% in 1983, the same as for the previous two years. Business confidence continues to decline, and investment is forecast by the OECD to fall by 4% in the coming year, the largest decline arising in productive industry. As Italy's inflation rate remains well above the average for OECD countries, her competitive position (previously enhanced by periodic devaluations) has slipped once again. Exports are likely to be much less buoyant than during 1981 and the first half of 1982, whilst the lire is now (paradoxically) the strongest EMS currency. As reported in Rome telno 045 of 25 January, it is by no means certain that the new agreement on wages will ensure that the government's inflation targets will be met. Furthermore, the concessions offered by Scotti have compounded the administration's problems in limiting the size of the PSBR. A reduction in the budget deficit is a prerequisite for economic recovery; if this is not achieved rapidly, continuing high interest rates will add to the difficulties of the corporate sector while Italy's external finances will deteriorate further. One of the most worrying aspects of recent economic reports is the growing problems faced by the previously dynamic small and medium-sized firms; the cost of borrowing is one of their major concerns.

3. It would be difficult to disagree with the Ambassador's assessment that firm government measures are necessary during the recession. The early successes of the Fanfani administration may yet prove to be illusory; the determination of the political parties and the social partners to make the sacrifices necessary to ensure progress still seems to be absent. An improvement in international economic conditions would certainly ease Italy's external constraint, but by no means can this be relied on. Prospects are indeed far from encouraging.

4. British exports have been something of a bright spot; the gains in productivity over the last two years, and the more recent depreciation of sterling, should afford us the opportunity to consolidate our position. Perhaps these results point to the importance of the marketing and promotion efforts made both by firms and by the Post; as economic conditions in Italy worsen, these endeavours will become increasingly vital.

N R Chimes

ESID

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## ANNUAL REVIEW FOR ITALY

I attach an advance copy of Sir R Arculus's despatch of 20 January along with a preliminary draft reply. I should be grateful for any comments on the draft by 6pm on 3 February. I am copying this minute to POD as paragraphs 22-25 of the despatch form Sir R Arculus's valedictory. The despatch will be printed as a diplomatic report.



R P Osborne  
Western European Department  
W67 233 5903

31 January 1983

cc: Mr Young

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