Italy drags euro zone shares lower on risk of new government crisis

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* Euro STOXX 50 down 0.7 pct at 2,805.27 points.

* Italian stocks weigh on government crisis threat

* Index still heading to around 3,000 in next month-Day-By-Day

* Volume thin as London market shut for holiday

By Francesco Canepa

LONDON, Aug 26 (Reuters) - Italian stocks led euro zone shares lower on Monday as the risk of a new government crisis fuelled a selloff in companies exposed to Italian sovereign debt and posed risks to the country's still weak economy.

Italy's FTSE MIB share index was down 1.6 percent after members of Silvio Berlusconi's centre-right party warned they would bring down the government if the former premier is expelled from parliament over a recent conviction.

The threat of a government crisis raised the prospect of a new wave of political instability that could delay the country's economic reform and dash growing expectations for a pickup in the economy. Early signs of economic improvement have helped the FTSE MIB rise 6.8 percent in the last month, outperforming Germany's DAX and France's CAC.

"It doesn't look like the politicians will find a compromise to get out of this crisis, which in turn puts all measures that need to be taken to spur the economy on ice," a Milan-based trader said.

Italian banks UniCredit and Intesa Sanpaolo , fell around 4 percent, as investors worried about their holdings of Italian sovereign bonds, which fell in value on the secondary market.

The two stocks were the biggest drag on the euro zone Euro STOXX 50 index, which was down 0.7 percent at 2,805.27 points.

The reaction in Italian banking stocks, which have risen 14.7 percent since the start of the year, was magnified by underlying concerns about some of their other assets, which will come under scrutiny in an upcoming review of euro zone banks to be carried out by the European Central Bank.

"I wouldn't sell Italian sovereign bonds on the back of the latest government tensions," the head of strategy at an Italian investment bank said. "Banks, however, have got a few more problems of their own, such as the asset quality."

A recent improvement in data on the euro zone economic has helped the Euro STOXX 50 rise around 8 percent since the start of July, or more than twice as much as the U.S. S&P 500.

"It may take a few of days to build a base but it looks like we're going to have another top for 2013 in Europe," said Valerie Gastaldy, head of Paris-based technical analysis firm, Day-by-Day. She expected the Euro STOXX 50 to reach around 3,000 points in the next month.

Volume on the Euro STOXX 50 was thin at 27 percent of its 90-day average at 1054 GMT, partly because London financial markets were closed for a public holiday.

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