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The main hurdles to overcome in order to save Italy

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The pandemic struck an Italy weakened by a quarter of a century of economic and social decline and trapped in a vicious cycle of "low growth-high debt" that is impossible to break when interest rates, albeit historically low thanks to the European Union, are higher than the GDP growth rates.

The breakthrough generated in the EU in recent months thanks to the initiatives of German Chancellor Angela Merkel and French President Emmanuel Macron offers Italy an opportunity that is as unexpected as it is unmissable not only to recover from the economic shock produced by Covid-19, but also to find a path of financially, socially and ecologically sustainable growth. Rather than dwelling on how to use the resources unexpectedly made available by the European Union, in these pages we draw attention to three hurdles that have hindered Italy's economic growth in recent decades. Without removing these obstacles, but instead trying to get around them with new subsidies, Italy risks wasting what seems to us its last chance to avoid a new public debt crisis.

Dissolve the subsidy system

The NextGeneration-EU (NG-EU) funds are an unmissable opportunity that can provide Italy with enormous resources with which to find its way back to growth, recover the productivity loss of the last 25 years and stabilize public finance. The availability of these funds constitutes one of the two pillars on which Italy's historical opportunity stands. The second pillar is represented by the institutional reforms and investment plans that Italy is required to implement in connection with the funds.

Using the European funds appropriately to increase the country's potential growth is a vital goal. In fact, despite the generous terms with which they are granted today, the loans and transfers must be largely repaid or covered with new own resources, just as the significant current increase in the debt/GDP ratio must be corrected.

Is Italy ready to take advantage of this opportunity? Up to now, we have seen the publication of general, broad-based reform plans for Italy which, however, have often lacked the concreteness necessary to identify and deal with the obstacles that are impeding a correct allocation of resources in the Italian market economy.

The difficulty is caused by the intertwining of political interests and rent-seeking positions that have become encrusted over the years. These rent-seeking positions - both economic and political - require a commitment that will not arise spontaneously just from having new resources.

For many decades, Italian politics have systematically avoided tackling obstacles to economic growth, trying to circumvent them through the disbursement of subsidies or compensation for inefficiencies. These mechanisms have created distorted and persistent incentives, rewarding, among other things, firms that preferred to remain small with little entrepreneurial dynamism.

An effect of this status quo subsidy strategy has been the increase in public debt, which expresses the inability of Italy's economic system to sustain itself.

A second effect was the construction of an intertwining of rules and benefits that took on a life of its own through legal and administrative practices, as well as through representatives of associations and social actors, which aimed at the pure survival of a system of interests united against the modernization of the self-sustaining country.

Thanks to the European NG-EU funds, in the coming months, for the first time in a long time, Italy will have the resources necessary to provide important incentives for the modernization of the Italian economy. In order for these funds not to get lost in the intertwining of interests, but rather to break the incrustations that prevent the country from growing, resources must be tied to fixed commitments. For this reason we believe that the NG-EU Fund must function through a conditionality mechanism, useful for identifying the hurdles to be overcome and for verifying the results of policy interventions.

The general framework

A reference for identifying the conditions necessary for the development of the country is certainly the [Country Specific Recommendations](#) document prepared in 2019 by the European Commission.

On June 5, 2019, the Council of the European Union approved the recommendations proposed by the European Commission regarding measures that the Italian government should have taken in 2019

and 2020. The document provides an analytical framework useful for orienting, even now, government action in view of the reform plan requested by the European Union as a premise for using the funds for post-pandemic reconstruction.

In particular, we highlight the main recommendations from the document, even though they date back to an economic phase different from that which was generated by the 2020 recession:

1. Shift taxation away from labour, including by reducing tax expenditure and reforming the outdated cadastral values. Fight tax evasion, especially in the form of omitted invoicing, including by strengthening the compulsory use of e-payments including through lower legal thresholds for cash payments. Implement fully past pension reforms to reduce the share of old-age pensions in public spending and create space for other social and growth-enhancing spending. Use windfall gains to accelerate the reduction of the general government debt ratio.
2. Step up efforts to tackle undeclared work. Ensure that active labour market and social policies are effectively integrated and reach out notably to young people and vulnerable groups. Support women's participation in the labour market through a comprehensive strategy, including through access to quality childcare and long-term care. Improve educational outcomes, also through adequate and targeted investment, and foster upskilling, including by strengthening digital skills.
3. Focus investment-related economic policy on research and innovation, and the quality of infrastructure, taking into account regional disparities. Improve the effectiveness of public administration, including by investing in the skills of public employees, by accelerating digitalisation, and by increasing the efficiency and quality of local public services. Address restrictions to competition, particularly in the retail sector and in business services, also through a new annual competition law.
4. Reduce the length of civil trials at all instances by enforcing and streamlining procedural rules, including those under consideration by the legislator. Improve the effectiveness of the fight against corruption by reforming procedural rules to reduce the length of criminal trials.
5. Foster bank balance sheet restructuring, in particular for small and medium-sized banks, by improving efficiency and asset quality, continuing the reduction of non-performing

loans, and diversifying funding. Improve non-bank financing for smaller and innovative firms.

The Commission's recommendations offer an indispensable framework for government action, but something more is needed: a concrete sign that the Italian government is willing to tackle the historical obstacles that are impeding development in the country. In designing these interventions, it should be borne in mind that the Recovery Fund resources must be strictly used only for investment expenses over a few years, not in current expenses for wages and consumables. It is therefore necessary to ensure that investments are accompanied by the removal of institutional and behavioral obstacles that may prevent or slow down the continuation over time of the benefits obtained thanks to the expenditure of investments over the years of the plan. The temporary availability of substantial additional resources is an opportunity not to be wasted in order to carry out courageous reforms that have been necessary for some time. In this regard, we have identified three priority fields for economic policy measures which, by removing institutional and behavioral obstacles, can truly mark a new season of growth interventions: 1) the education and professional training sector; 2) the reform of the Public Administration; 3) the regulatory system for firms and the labor market.

The education and professional training sector

Italy's delay in educating its citizens compared to the rest of Europe is recognized (by the OECD, the EU, the Colao Report) as one of the factors that, in the long run, have weighed on productivity growth, as well as on essential components of social well-being and democracy itself. Together with that for public investments, education expenditure underwent not only a relative decrease but also an absolute decrease from 2008 to 2019. Progressively bridging this delay is possible today, also thanks to the financial resources obtainable with the Recovery and Resilience Fund.

European funds have a dual objective: to boost incomes and employment in the short and medium term and launch the country on a path of growth different from that of the past 25 years. If well planned and accompanied by institutional reforms, spending on education also contributes significantly to the achievement of both objectives.

Italian schools are often housed in dilapidated buildings, sometimes not even compliant with legal standards. Infrastructure is of poor quality and, unlike in other countries, does not improve the scholastic experience, does not make it more attractive to young people and thus does not contribute to the overall education process. These facilities are, for example, gyms, sports fields, libraries,

computer rooms, canteens. Similar deficiencies are seen in most universities, some of which do not even offer teachers an office. Better laboratories, libraries, equipped classrooms, structures for sports activities and canteens are needed. First and foremost, in order to bring the Italian university experience closer to international best practice, a substantial investment in residential construction for students is essential so as to decrease the cost of off-site attendance (fundamental formative experience) and, above all, to encourage the "College" experience - student communities that unite the university curriculum with additional courses, cultural and sporting activities and the participation in the life of the communities in which the university is located.

Significant investments in construction, information technology and laboratory equipment will make a decisive contribution to supporting employment in the short to medium term (the period foreseen for the Recovery Fund). These are expenses that typically have a multiplier greater than one. Being mostly of relatively modest amounts (less than 5 million euro), they have the advantage over large-scale works of enjoying the bureaucratic simplifications for the construction site foreseen by the recent measures. They are also investments for which many universities and some educational institutions already have projects ready to be launched sometimes with the relative areas and the bureaucratic authorizations, but everything has remained suspended due to the lack of funds.

However, the redevelopment of buildings and equipment will not be sufficient to significantly improve Italy's educational system in the absence of institutional reforms.

PISA (OECD) surveys show that the weaknesses of Italy's pre-university schools are mainly qualitative, if it is true that only 20 percent of Italian adults are able to read, understand and adequately summarize a short text. The quality of the schools is also very uneven among the different areas of the country, even within individual provinces. Italian schools do not need more teachers, but better territorial distribution and continuous requalification. A greater commitment must be accompanied by improvements in economic conditions and this will have to be achieved with a reallocation of resources within the current state budget (basically, we are speaking of transferring resources from the elderly to the young). The realization of these qualitative improvements is only possible within a framework of stability and certainty in the processes of training, hiring and promoting teachers. Public competitions must be carried out on a regular and predictable basis, on a regional basis and for a number of vacancies limited from time to time to the needs of the individual areas. The pandemic has highlighted widespread weaknesses in IT skills: the wider range of tools made possible by the investments mentioned above must be accompanied by adequate training courses. The exceptionally long time, in comparison with other countries, of summer holidays must be partly exploited for the diffusion and institutionalization of work experiences whose educational value is demonstrated by many international and Italian experiences. Financial and organizational

resources must be found to incentivize and disseminate these experiences and above all political capital must be spent to overcome the resistance of children, families and teachers.

As far as universities are concerned, the investments we have mentioned must be accompanied by the creation of institutional conditions for: (a) educating more and better students in a shorter time, finding the right combination from time to time between the transmission of general knowledge and professional training; (b) producing advanced professional training, necessarily intended for a relatively small number of students; (c) considerably improving the quality of research, which entails, at the same time, the creation of competitive doctorates of an international level.

In almost all advanced countries where academic education functions well, these tasks are carried out within a framework in which universities enjoy broad autonomy, a framework in which each single institution is free to select and recruit teaching and non-teaching staff (non-teaching staff - of which it is rarely spoken - is absolutely decisive), to decide the remuneration standards, the creation of teaching programs, the students' admission criteria and, in general, the management of their resources. The reform that must accompany investments in universities must be based on two pillars: (i) making the universities' current false autonomy real, removing some of the limits of administrative law (for example, transforming the universities into foundations), (ii) distributing the resources that the state budget allocates to the university on the basis of precise didactic and scientific performance assessments and the correction of any external elements, to be identified and quantified rigorously, which negatively affect the acquisition of own resources by the various universities.

For students admitted to university the government should offer scholarships that can be spent in the university of their choice. The all-Italian taboo on the legal value of degrees must be overcome with serious state exams for admission to certain professions and with competitions for the public administration capable of assessing the aptitude of candidates to perform the specific tasks required. In all other cases, the legal value has long been, in fact, useless and obsolete even in Italy.

This will mean accepting that some universities will misuse their autonomy in the short term, but it will free others from improper constraints that prevent the full realization of their latent potential. There will be few "generalist" universities, equipped with almost all faculties and research doctorates. Many will specialize in areas where they have already had relevant experiences. Still others will focus mainly on the quality of training, without aiming for international research. Doctoral programs will only be carried out in the best universities for the quality of research in the individual fields.

The driving force behind new investments in construction and research equipment accompanied by the adaptation of Italy's universities to the best international institutional practice will allow its

universities to form a complex group which will respond, overall, to both local needs and those of international excellence. The attractiveness of Italy's universities for foreign students and professors will be of enormous importance in establishing a new international reputation for the country. At the same time, more dynamic, culturally vibrant universities with residing students will be an important factor in revitalizing Italian cities.

The Public Administration

If Italy really wants to create a favorable environment for investments, public and private, the good functioning of the Public Administration is one of the great objectives to be achieved. The Simplifications Decree published last July 16 takes a few steps in the right direction but does not overcome the basic hurdles (and the instrument of the decree, moreover, did not allow it to).

It is easy to say what was done. For public contracts, a temporary regime has been introduced, until 31 July 2021, in which the procurement procedures are simplified, especially for contracts below the EU threshold, and strict terms are introduced to avoid delays in carrying out the works. For authorizations involving multiple administrations, the decree extends to 2021 the possibility of applying the simplified "conference of services", with the obligation for all administrations to express themselves within 60 days. Numerous sector simplifications have also been introduced, especially for construction, infrastructures for electronic communications, energy and the environment. For initiatives not expressly prohibited by law relating to technological innovation and digitization, the possibility is given to contact the Ministry of Innovation to quickly obtain authorization for the testing.

Concerning controls, the decree limits the liability for tax damage before the Court of Auditors to the hypothesis of willful misconduct, excluding that for gross negligence (except in the case of "omissions" in acting). In addition, the crime of abuse of office (which could have been abolished) is better delimited.

More courageous steps are still desirable, in particular, in the conference of services to overcome disagreements between administrations, in terms of environmental impact assessment, in the functioning of the Inter-ministerial Committee for Economic Planning, in the reduction and qualification of contracting authorities.

Whatever happens in the parliamentary process, the task of simplifying Italy for the revival of the economy does not stop here.

The biggest challenge for modernizing the country and encouraging public and private investment is to restore to Italy's Public Administration the ability to decide by exercising its administrative discretion. The modernization of Italy's administrative system requires systematic and long-standing government action. The idea, expressed in the Law Decree, of a 2020-2023 plan for administrative simplification must be filled with content in order to lighten the individual procedures in the various sectors, concentrating responsibilities and reducing the number of subjects with veto powers.

This requires rebuilding the administrative capacity in the State and throughout the territory, filling the conspicuous shortage of managers and officials with managerial, technical and IT skills, due to decades of blocking the turn-over, and restricting the intervention of politics in the choices of top management administrations and managers. The extensive hiring program currently envisaged for the Public Administration must be aimed at recruiting specialized personnel with adequate technical and managerial skills.

To discourage the inertia of the administrations and encourage the "to do" ethic, a specific commitment from the office managers and the administration heads is needed to implement the provisions already present in the system, in particular, taking into account the results of the administrative action for the purposes of attributing managerial positions and of setting the remuneration or result bonuses.

Finally, a chapter of the utmost importance concerns the system of controls on administrative action, which must be concentrated on ex-post results, minimizing preventive controls focused on compliance with procedures. In this perspective, the role of the Court of Auditors and of ANAC should be radically reviewed.

In general, we have to ask ourselves if it is possible to move from an approach based on distrust - in the citizen, in the firm, in the public official - to one based on full transparency and empowerment of all those involved. Without this cultural passage, the Gordian knot of excessive bureaucracy will never be cut.

The system of regulating firms and the labor market

The consequences of the recession following the pandemic crisis are already so profound that they can be considered unprecedented. Similarly, the medium to long term consequences are difficult to predict. The most conspicuous manifestations of the current recession, however, already point to the need for a profound reorganization of production activities.

The first phenomenon of productive transformation to be evaluated concerns the asymmetrical impact of the crisis on individual production sectors, some of which could emerge from the crisis completely transformed. The second phenomenon is the shift in the capital-labor use relationship due to the social distance measures whose duration is still difficult to evaluate, but which have already radically changed the organization of work in almost all production areas and accentuated the phenomenon of the digitization of the economy. The third factor is the recomposition of international trade: since 2009 the increase in global trade has stopped growing faster than global GDP, but in the current year it is estimated that world trade will drop well over 20%, with the prospect of recovering the loss of volume and value only partially in the following years.

Until 2020, the European growth model was based on the export of goods and services outside the EU. Just halving the EU's current account surplus by volume would almost mean halving the European average annual growth rate of the last decade. To compensate for this demand and supply gap in the EU, it would be sufficient for the Italian economy to operate at the rate of the factors' full employment. From this simple consideration, it is possible to understand why the EU has taken Italy's role as a recipient of reconstruction and resilience funds to heart. In some cases, the global value chains will need to be shortened and this will create opportunities for the inclusion of Italian firms in new European value chains. For Italian firms whose dynamism has been running out in recent years this will require an extremely dynamic, albeit demanding, process of reorganization and modernization.

To go through this process, firms will have to deal with the difficulties that have hampered their dimensional and technological development in the past thirty years. The same challenge concerns labor organizations. Italy is in fact the only advanced economy in which there is a marked and stubborn discrepancy between productivity and labor costs with different characteristics depending on the sectors and geographical distribution of activities and with a persistent divergence between North and South that risks being further aggravated. Overall, Italian labor productivity is stagnant and has lost out to competitors. In recent years, the contribution of capital to labor productivity has been zero and, in traditional activities, it has even been negative.

Productivity dynamics depend on appropriate public and private investments. The lack of such investments in Italy from the beginning of the nineties is due to complex and multiple reasons: from the lack of diffusion, among the very small and the small firms, of the innovative processes carried out by the nucleus of Italian firms that have managed to place themselves on the technological frontier, to the consequences of political and institutional uncertainty, to the lack of evolution of the industrial relations system. The fact is that the accumulated delay has been particularly significant in advanced

technologies and intellectual property whose non-collateralizable nature has made banks' lending inadequate and has thus revealed the weakness of the non-bank sources for financing firms (bonds and shares). To compensate for these shortcomings, investors should be able to rely on stable time horizons, on less uncertainty in the economic policy framework, on the wide availability of alternative sources of financing and, possibly, on a public guarantee mechanism. For all these reasons, the offer of financing and investment subsidies in the NG-EU multi-year program represents an opportunity of existential value for the Italian economy.

This program envisages that the investments that must support the dynamics of labor productivity and the total factors productivity are carried out in conjunction with adequate reforms to guarantee their microeconomic effects. Obviously, the reforms that must accompany the disbursement of the European funds must take into account the special - albeit still unpredictable - transformation of production systems following the post-Coronavirus recession. In sum, we can refer to three interventions:

1) An initiative to reform the organization of production that guarantees the dynamism necessary to accompany the transformation of Italy's individual sectors and individual firms and to increase the quality of the demand for work. The second area of intervention is the system of professional requalification of the workforce in consideration of the need for rapid technological advancement of the Italian production system. This assistance and training system must be widely subsidized with public resources (also in the process of inserting the worker in the firm, both in the apprenticeship phase and in the specialized employment phase) and based on local efficacy and capillarity, in a way as to prevent the temptation for firms to specialize in low value-added processes by exploiting the low labor costs that could result from a lasting recession.

2) A new welfare system that prevents the persistence of unemployment, which could worsen in the coming months, and that is able to support the redevelopment system and to channel through a system of active labor policies a qualitatively higher supply of workforce towards the new occupations. This would require simplification and concentration of labor market support measures in a single instrument, both in terms of crisis management and reallocation of workers.

3) Further incentives should concern business investments in terms of: greater capitalization and investments in tangible and intangible human capital (giving more structure, coherence and continuity to 4.0 measures). In parallel, spending on public investment in strategic sectors should be accelerated. The "Next Generation - EU" funds can accompany this transition with public investment programs, but also with adequate incentives to strengthen the capital and technology of small firms that are able to survive and increase in size.