

# **Low Economic Freedom, Low Competitiveness and Low Growth**

The case of Italy

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**Italy, picture of an economic disease**

**Evidence concerning economic freedom**

**The reasons of the decline in economic freedom**

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# Introduction

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- During the last two decades, Italy showed low rates of growth, together with low competitiveness and a scarcely favorable business environment
- For what concerns economic freedom, the situation is similarly disappointing
- After an improvement of the performance during the period 1975-2000, the overall level of economic freedom remained substantially stable during the period 2000-2005 and decreased constantly since 2005
- This presentation briefly analyzes the current situation and discusses the possible developments

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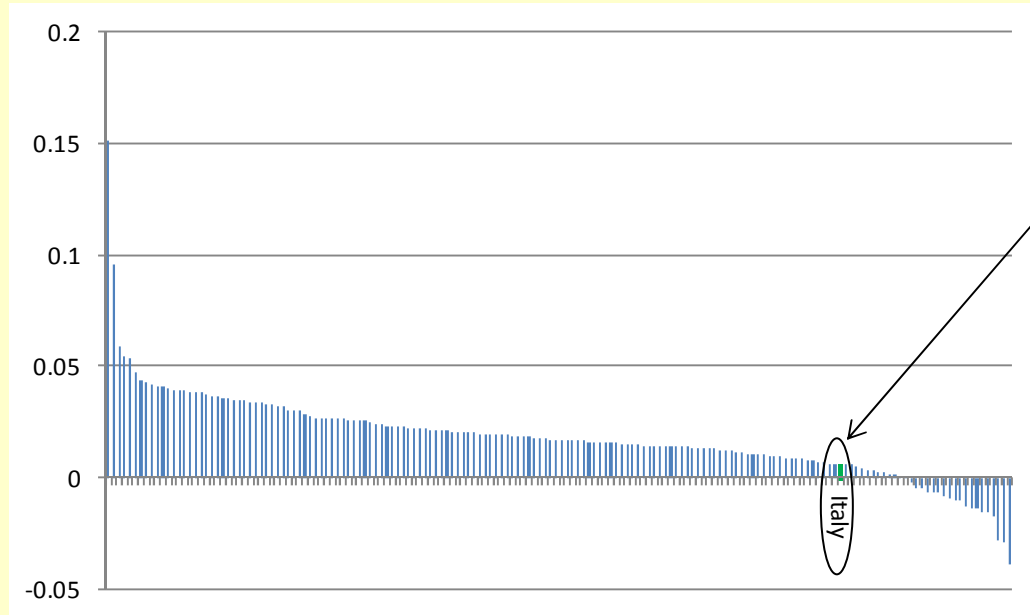
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# Italy, picture of an economic disease

*Two decades of missing growth*

GDP per capita, CAGR 1990-2009  
PPP, constant USD



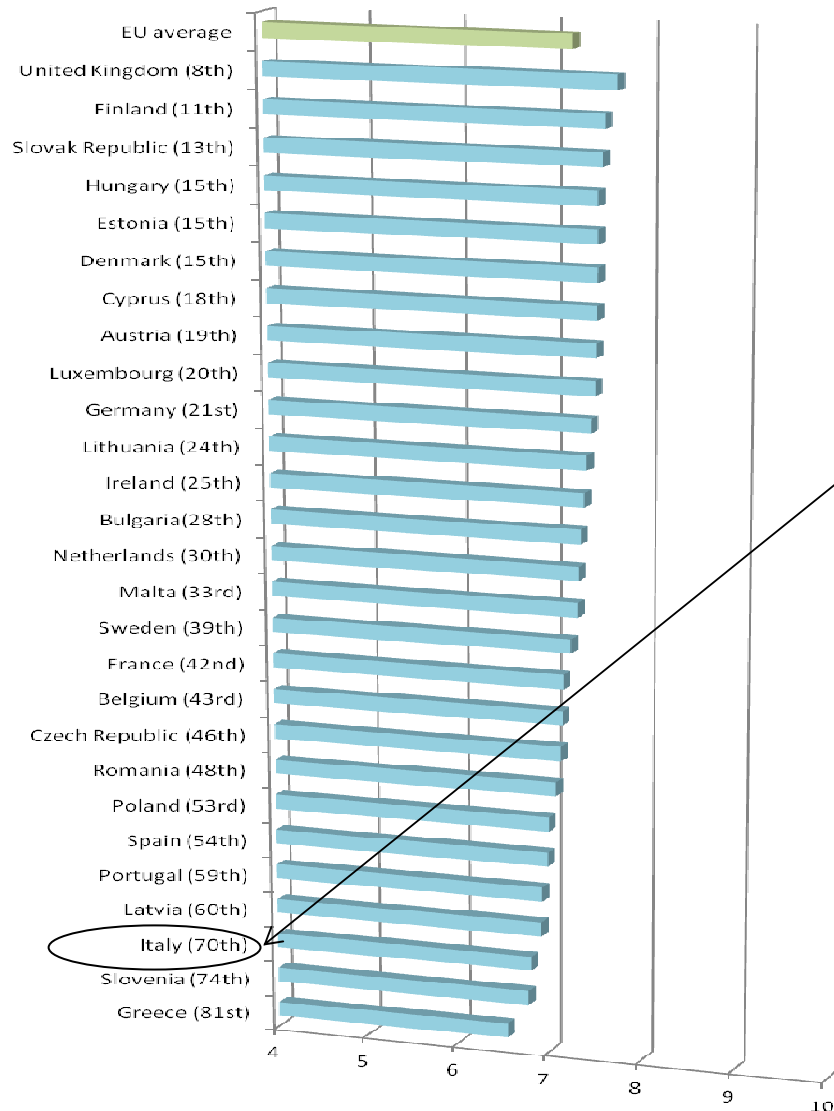
Source: World Development Indicators, *The World Bank*

- During the last two decades, **Italy** exhibited one of the **lowest growth rates** at a worldwide level
- Also in comparison with the other developed nations Italy is performing badly: GDP per capita growth was about **40% of the average growth of OECD countries**

There are obvious, structural and long term problems that slowdown Italian economy. Let us analyze further the causes of this disappointing performance

# Italy, picture of an economic disease

## *Low levels of economic freedom*



- **Within the UE, Italy** classifies at the last positions of the ranking concerning Economic Freedom.
- Only **Greece** and **Slovenia** exhibit a worse performance
- At a **worldwide level**, with a score of **6.81**, Italy ranks **70th**

The result lead to some paradoxes and is worthy to be analyzed further. Italy obtains the same score as **Ghana** and the **Kyrgyz Republic**

# Italy, picture of an economic disease

## *Low competitiveness*

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- The **Global Competitiveness Index**, developed by the World Economic Forum, ranks **Italy 48<sup>th</sup>**
- It is the worst performance among the G7 countries. **Lack of growth, low labor market efficiency, insufficiently developed financial markets and poor institutions** are key structural weaknesses
- **Inefficient government bureaucracy, access to financing and high tax rates** are seen as the main concerns for potential investors
- Italy ranks only **118<sup>th</sup> worldwide in the field “Labor market efficiency”**, due to a scarce flexibility in the wage determination process, inflexible hiring and firing practices and low productivity

# Italy, picture of an economic disease

## *Unfavourable business environment*

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- The **Doing Business Index** of the World Bank ranks **Italy 80<sup>th</sup> worldwide**, with a loss of four positions with respect to the previous year
- It recently implemented several **regulatory reforms** in areas where results might be seen only in the longer term, such as judiciary or insolvency and it introduced online procedures concerning the process of starting a business
- However, it ranks **128<sup>th</sup>** in the area concerning **paying taxes procedures** and **157<sup>th</sup>** in the area concerning **enforcing contracts**



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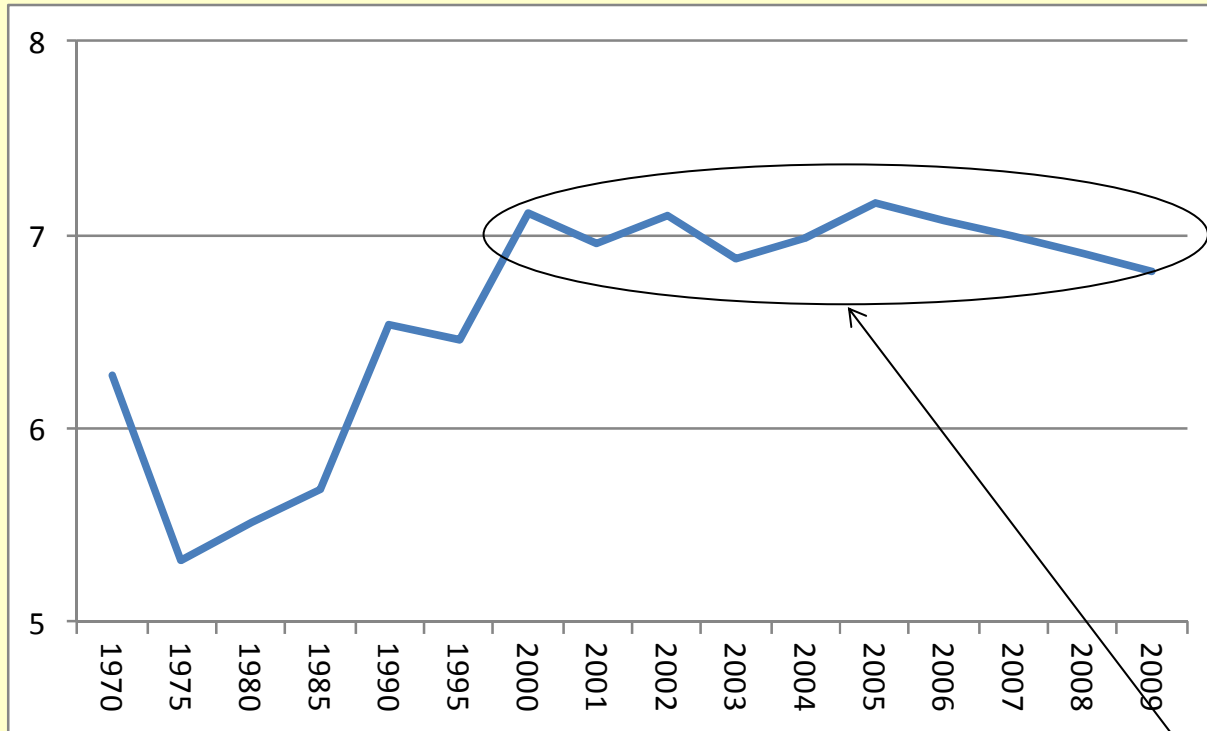
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# Evidence concerning economic freedom

*A decade of decline in economic freedom*

## Economic freedom in Italy

1970-2009

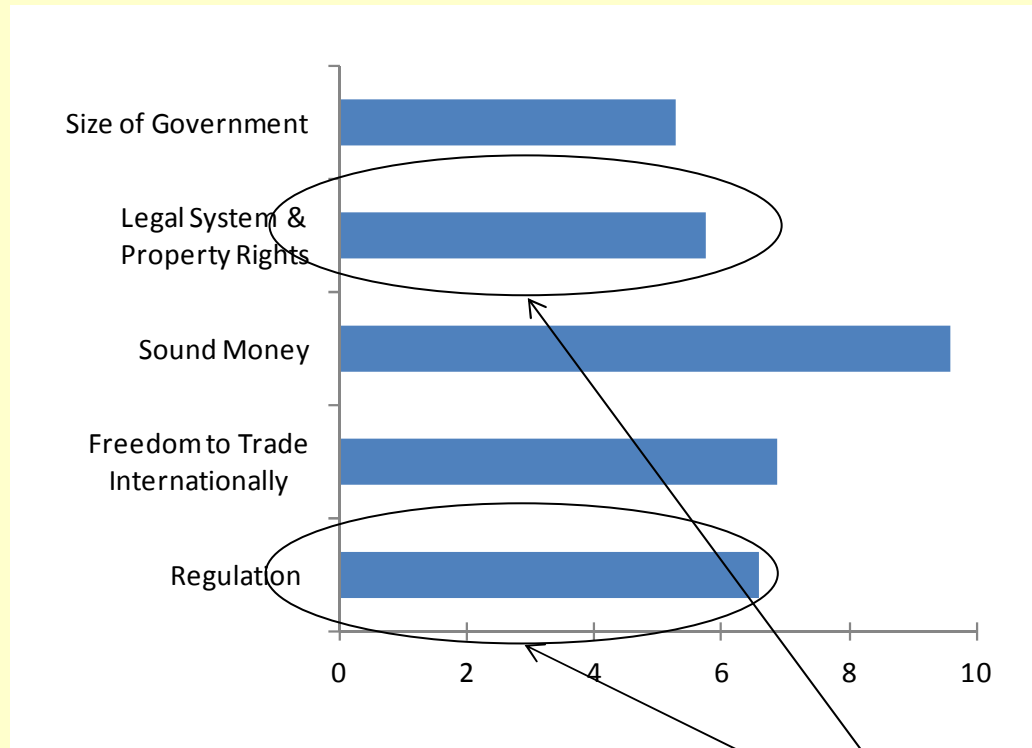


- **Economic freedom** increased almost continuously from 1975 to 2000

- During the **last decade**, however, **the level of economic freedom declined** and the current score is lower than the one obtained in 2000

# Evidence concerning economic freedom

## *Strengths and weaknesses*



- Like many other EU countries, Italy obtains a non sufficient score in the area “Size of Government” (due to an excess of government consumption, transfers and subsidies, and to high top marginal tax rates), excellent results in the “Sound Money” area and good performances in the “Freedom to Trade Internationally” one

The result in the area “Legal System & Property Rights” are not sufficient and quite lower than the average EU scores, while the ones in the area of “Regulation” are sufficient but declining in the last years

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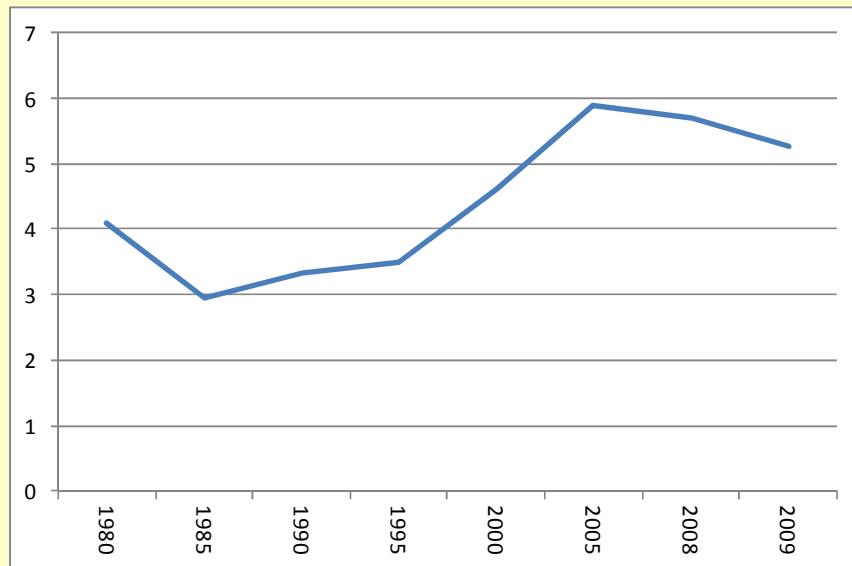
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# The reasons of the decline in economic freedom

## *Size of Government*

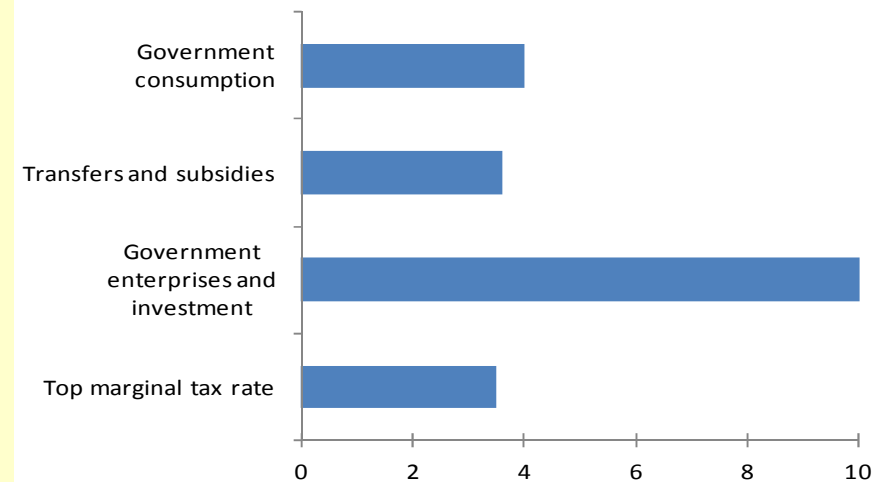
### Size of Government

1980-2009



**Government consumption, transfers and subsidies and high top marginal tax rates** are the three main problems emerging from the analysis of the sub-indicators

- Until 2005 the size of government was decreasing and the score in the related area increasing
- Afterwards, also for the lack of effective constraints, the direct intervention of the government in the economy has begun to increase again

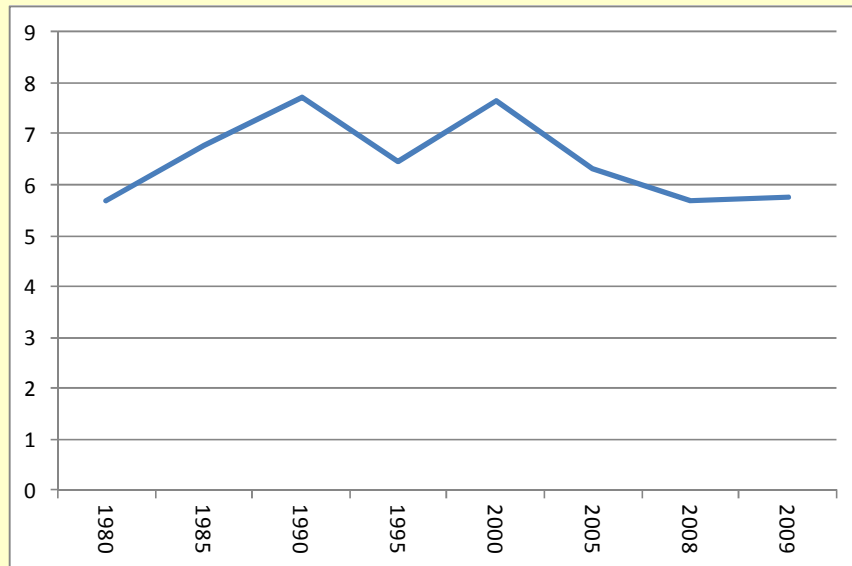


# The reasons of the decline in economic freedom

## *Legal Structure and Security of Property Rights*

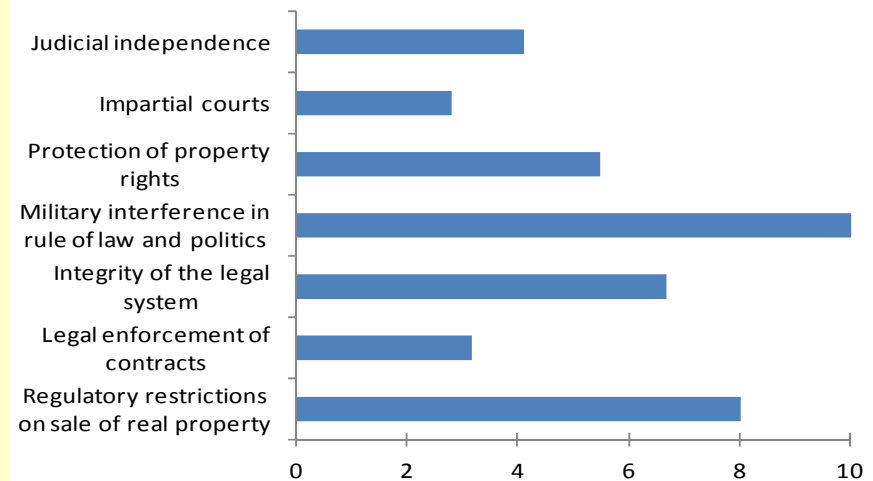
### Legal System & Property Rights

1980-2009



The **independence of the judicial system, scarce impartiality of courts** and difficulties in the process of **enforcing contracts** represent the main problems

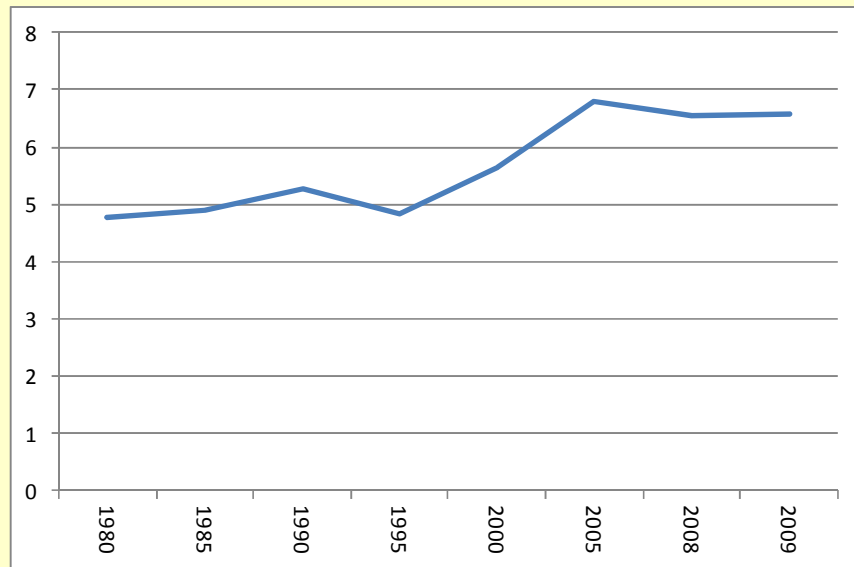
- A second trend inversion concerns the area Legal System & Property Rights. During the last decade a constant decrease in the score obtained is observed
- During the last year., the result is not sufficient



# The reasons of the decline in economic freedom

## *Regulation*

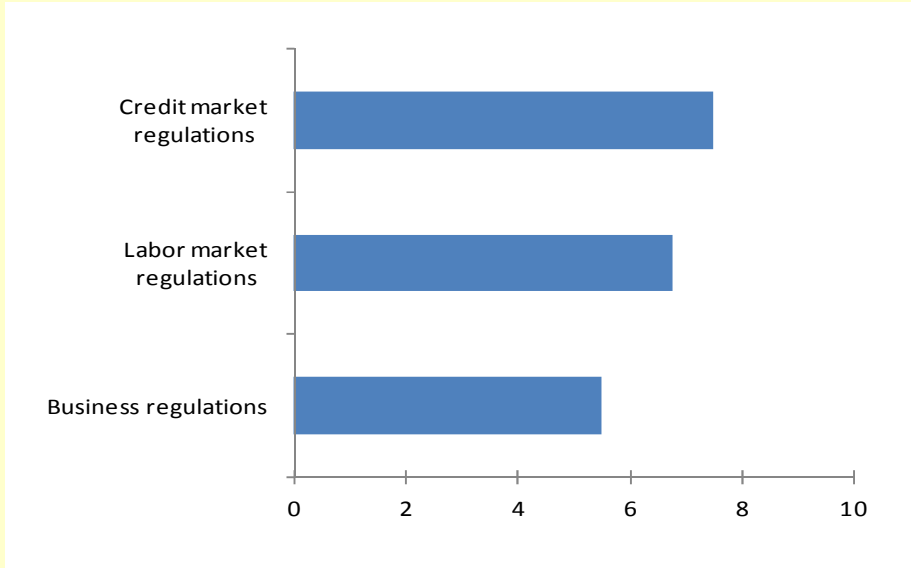
**Regulation**  
1980-2009



**Business regulation is the most critical sub-indicator.**

Concerning labor markets regulation, hiring and firing regulations and centralized collective bargaining are the most critical issues

- Also the trend concerning the quality of regulation inverted its direction after 2005
- Following a period of improvement in the decade 1995-2005, a worsening of the score is observed in the last years



# The reasons of the decline in economic freedom

## *Weak institutions*

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- In general, it can be noted that the main Italian weaknesses are related to an excess of government intervention in the economy and to institutional factors
- Concerning the first point, Italy obtains 3.99, 3.59 and 3.5 for what concerns, respectively, government consumption, transfers&subsidies and top marginal tax rates sub-indicators
- Analyzing the institutional factors a high degree of inefficiency of the public sector and of the bureaucracy emerges clearly:
  - The judicial system is not working properly: a 4.13 is obtained in the sub-indicator concerning judicial independence, 2.82 in the one concerning impartiality of courts and 3.18 in the one concerning legal enforcement of contracts
  - In the area of business regulations, a 2.03 is obtained in the sub-indicator on administrative requirements and a 3.76 in the one related to bureaucracy costs (and a 4.74 if extra payments/bribes /favoritism are considered)



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## Final remarks

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- The overall decline in the levels of economic freedom has at least three causes
- As it was shown, three positive trends were reversed during last years, and Italy lost competitiveness in the fields Size of Government, Legal System & Property Rights and Regulation
- In the fields Sound Money and Freedom to Trade Internationally Italy obtains, respectively, excellent and good scores. The performances in these areas were certainly influenced by the membership to the EU and by the adoption of the Euro

### **Which trends might we expect?**

- After a period characterized by an improvement in economic freedom, the impetus towards new reforms stopped. The achievement of the goal of joining the Euro and the availability of low interest rates considerably weakened the need for reforms and the constraints on government expenditure
- The current crisis pointed out the importance of improving institutional conditions. However, mainly due to a weak political system and to the existence of strong interest groups this need has remained up to now largely unsatisfied