Italy’s Decline: A Political Economy Perspective

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The Political Economy of Italy’s Decline

Declino. Una storia Italiana

Declino Italia

International observers have not been kind to Italy during the past two decades. The International Monetary Fund (IMF, 2016) wrote about the country’s two lost decades, the Economist (19 May 2005) described it as the real sick man of Europe and eminent economists, such as Bruno Pellegrino and Luigi Zingales (Pellegrino and Zingales, 2017), tried to diagnose the Italian disease. Italy’s GDP has barely grown since the mid-1990s and the past decade was the worst in the history of its economy, world wars included.

The three volumes by Andrea Capussela come at a time, when many have given up hope that the productive élan characterizing the ‘Italian miracle’ (1950–63), which propelled a backward and war-torn Mediterranean country to the forefront of the technology frontier, may ever be recouped.

Capussela, a competition lawyer by training, who worked as an economist in support of international organizations in Kosovo and Moldova, engages the reader in a refined political-economy exercise, thereby providing a unified account, grounded in new institutional economics and classical collective action theory, of the economic and political causes of Italy’s decline, i.e. the country’s hallmark since at least a quarter of a century. His argument can be thus summarized.

The main indicator of Italy’s incapacity to innovate and compete is the gradually deteriorating total factor productivity, a rare phenomenon among advanced industrialized economies (AIEs). Explaining the decline starts with the constatation that the institutions governing the country, i.e. the effectively applied as opposed to formally adopted rules, are inefficient. Examples abound. Despite having accounting standards comparable to France or Germany, the general unreliability of financial statements in Italian firms makes them less attractive to investors, thereby leading to chronic undercapitalization that stifles most innovation efforts. There is, hence, a systemic problem with the rule of law, whose marked erosion vis-à-vis other AIEs is punctually measured by the World Bank.

It is the responsibility of politicians and the judiciary to ensure that legality is respected, the duty of the public to act according to the letter of the law, and the task of parties and civil society to signal an eventual malfunctioning. Yet, it seems that these actors have failed in their obligations...
and have fallen prey to a series of collective-action problems that pushed Italy into an inefficient and inequitable ‘bad equilibrium’.

The post-war political-economy ossified around the ruling Democrazia Cristiana through a combination of clientelistic exchanges between political and economic elites and particularistic ‘selective inclusion’ through benefits aimed at the electorate. Routine depreciation of the Italian lira, tolerance of tax evasion, and shielding key firms from competition kept the economy running after it landed on the technology frontier, thus exhausting Alexander Gerschenkron’s (1962) comparative advantage of backwardness, and after the going got tough in the early 1970s. Micro-targeting of social policy benefits – often occupation-based, due to the propensity of blue collars voting for the Communist party – and public employment opportunities, especially in the disadvantaged South, created particularistic exchanges of welfare for votes that held the party system stable.

Yet, a game-theoretical equilibrium where the few extracting resources rely on a functioning economy, which by definition requires the many to abide by its rules, may rapidly deteriorate. Corruption and tax evasion become systemic, the disregard for the letter of the law becomes endemic. Italy’s implosion under socialist rule during the 1980s is the prime example of such degeneration. At the time, the watchdogs were still barking. Early on the Communist party condemned the amorality of clientelism, an independent judiciary uncovered the P2 and tangentopoli scandals and the voters, indignantly, swept away an entire political class.

The parties that emerged from the 1992–94 political earthquake, however, did not provide a clear explanation of the system’s woes or a programme to unshackle the country from its bad equilibrium. Instead a media mogul, Silvio Berlusconi, a key representative of the status quo and the most unlikely champion of the promised liberal revolution, prevailed. Decline followed as the country’s resources were squandered through a number of ill-conceived reforms, such as the flawed privatization process and the hurried liberalization of the labour market. The persistence of an uncompetitive economic structure and a managerial class selected for its loyalty over its merits made it impossible for the Italian economy to withstand the challenges of digitalization, globalization, and adoption of the Euro. Additionally, the watchdogs had been muzzled. The intellectual abilities of elected policymakers and of civil society are at a historic low and the conflict between the judiciary and the political class reached peaks never witnessed in a consolidated democracy. Electoral volatility and the emergence of populist parties blaming external enemies – immigration, the Euro, Chinese competition – for Italy’s decline, such as Matteo Salvini’s Lega and Beppe Grillo’s Five Star Movement, are manifestations of rampant anomie.

Instead of fighting Italy’s bad equilibrium, these parties offered renewed selective inclusion through, for example, the quota 100 early pensions or a flat tax for own-account workers. Utterly unprepared, the Italian political-economy was crushed by the pandemic.

Despite the enormity of the challenge, the author traces an escape route. A conditio sine qua non to reverse the decline is to, first, explain the inefficiency and inequity of the bad equilibrium to the Italian electorate. This may then engender a collective action effort centred around a renewed political programme, whose implementation may be secured by the institutional structures through which Italy is anchored to the European Union. Of the two components, the authoritativeness of Premier Mario Draghi is one. His National Resilience and Recovery Plan lashed Italian politicians to the mast of comprehensive reforms tied to the Next Generation EU recovery package. Yet, a key ingredient is missing: the former banker failed to explain to Italians the real causes of the country’s decline (Capussela, 2021). This disconnect verisimilarly lies at the heart of the dramatic rise in the polls of the far-right Fratelli d’Italia, the only major Italian party not backing Draghi’s executive.

The breadth and complexity of Capussela’s oeuvre gained praise from academics and practitioners alike, as the blurbs eloquently show. Nevertheless, some constructive criticism, both theoretical and substantial, is still possible. As the author himself acknowledges, the fiercest objection is that societies do not change through collective action efforts, but rather through incremental reforms that may eventually unblock their potential. On this account, Capussela neither turns
to the vast scholarship that emerged after the fall of the Berlin wall nor draws from his own experience in troubled post-socialist regions. The heated exchange between shock therapists and gradualists in the mid-1990s as well as Joel Hellman’s (1998) brilliant recount of the ‘partial reform equilibrium’ trap in economic transitions would have been welcome additions to the debate. More important still, Capussela does not indicate what kind of growth shall a new productivity-friendly equilibrium entail, as the fundamental issue of creeping inequality is virtually omitted from his analysis.

A final word on the different readers the three books are suitable for. While the two heftier OUP and Luiss University Press volumes are aimed at an international and Italian academic readership, possibly becoming key textbooks for any course on Italy’s political-economy, the shorter Einaudi compendium is an informative text meant for the general public. The existence of a popular version is laudable, yet, it probably presupposes too much background knowledge on behalf of the reader. The author cannot be blamed though: stepping outside of one’s own gnosis and abstracting from it is often a daunting exercise.

References


