

Effects of fiscal policy in the North and South of Italy

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JRC-IPTS workshop
Seville, 14th February 2013

What is the main contribution of the paper?

- This study seeks to contribute to a growing body of work within 'regional and public policy studies' exploring the **effects of fiscal policy in Italy**.
- The main contribution of this work is to estimate an **econometric model accounting for the dualistic nature of Italian economy**, and thus **to frame fiscal policy** (distinguishing between spending and revenue of the public sector) **at regional level**.

Plan of the presentation

- Conceptual framework
- Econometric model using a bottom-up approach
- Results

- Any questions and suggestions will be very welcome!

My conceptual framework

- Like Greece, **Italy** is a country with a **debt burden** that is **heavy for it to bear**. It is close at around 125% of GDP; it is among the largest in the world.
- In recent years, several **austerity measures** (such as LD 98/2011, LD 138/2011, and LD 201/2011) aimed **to eliminate Italy's budget deficit** have been undertaken by Monti government.

The north-south divide

- But the budget deficit is just one of Italy's biggest problems. **Another big, and long-term problem is the north-south divide.**

Tab. 1 GDP Euro per inhabitant

	1980	1991	2007	2009
North	4,122	15,370	30,944	29,725
South	2,387 (57%)	9,090 (59%)	17,561 (56%)	17,235 (58%)

Why does the *South* matter?

Tab. 2 Economic activity rate, from 15 to 64 years

	2008	2009	2010
North	69.68%	69.34%	69.20%
South	52.44%	51.08%	50.76%

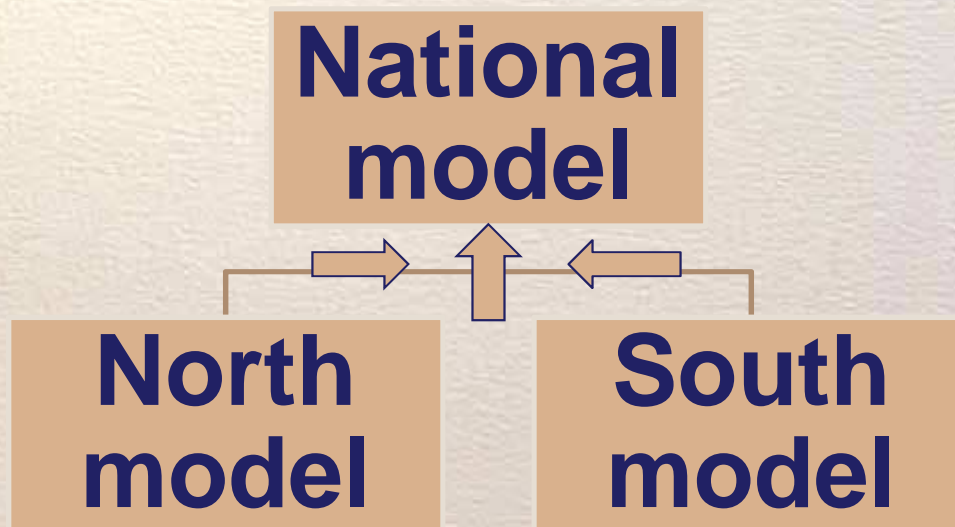
Tab. 3 Unemployment rate, from 15 to 64 years

	2008	2009	2010
North	3.9%	5.4%	6.0%
South	12.1%	12.6%	13.5%

Research method

- Given the **persistent gap** between the north and the south, we employ a **bottom-up approach**, which allows to compare the effects of fiscal policy in the south and the north of Italy.

This is perhaps a unique study in the regional and fiscal policy literature in Italy.



Macroeconomic model

- Our **macroeconomic model** is a system of **244 behavioural relationships**. Using time series data over the period 1980-2011, each equation is estimated at **regional level** using **OLS** method.
- For sake of clarity, our endogenous and exogenous variables can be grouped in six broad categories:
 - Price, earnings, and operating profit margins
 - Supply side (short run, and long run supply functions)
 - Demand side (consumption, and investment functions)
 - Trade (export function)
 - Labour market (supply, and demand)
 - Money market

Data

- Thus, the originality of our **approach** is that it allows to answer questions such as **did Italian government's chosen fiscal policy hit the south harder than the north?**
- To do so, we gather **data** in accordance with the definitions used in National Income and Product Accounts **at regional level.**
- Our main contribution to the existing knowledge is to provide **evidence**, through **primary data**, that informs policy.

Spending, revenue data

- **Main items of spending**

- Consumption spending (current salaries for services)
- Transfer payments (pensions, etc.)
- Other current spending
- Capital spending, and other capital expenditure (construction of public roads and building public schools)

- **Main items of revenue**

- Income taxes
- Excise duty/consumption taxes (IRAP, IVA, IRES)
- Social security contribution
- Other elements of revenue

Italy's public finances

- **Sharply cutting budget deficit is the priority for Italy's government.**
 - Tax rises and spending cuts aimed to shrink Italy's deficit (from 3.5% to 1.2% in 2012 and $\approx 0\%$ in 2013)

Cumulated effects on public debt (billion euros)

	2011	2012	2013
Tax rises	5,7	49,5	59,0
Spending cuts	9,2	24,4	41,7
Overall effect	14,9	73,9	100,7

Breaking Italy's public finances

At 7.6% of GDP the south has a higher burden than the north.

	Values in billion euros			As % of GDP		
	2011	2012	2013	2011	2012	2013
	Overall manouevre					
Total	14,9	73,8	100,7	0.9	4.5	5.9
North	10,8	53,4	71,2	0.8	4.2	5.3
South	4,2	20,3	29,5	1.1	5.4	7.6

Breaking Italy's public finances

	Values in billion euros			As % of GDP		
	2011	2012	2013	2011	2012	2013
	Revenue					
Total	5.8	49.5	59.1	0.3	3.0	3.4
North	5.0	37.9	44.9	0.4	3.0	3.4
South	0.7	11.6	14.2	0.2	3.1	3.7
	Spending					
Total	9.2	24.3	41.6	0.6	1.5	2.4
North	5.8	15.6	26.3	0.5	1.2	2.0
South	3.4	8.7	15.3	0.9	2.3	4.0

At 3.7 % of GDP the south will have a slightly higher tax burden than the north; at 4% of GDP, the south will suffer from the spending cuts more than the north.

Breaking Italy's public finances

- **Tax rises, rather than spending cuts, are the bulk of Italian government's work.**
- At 0.7% of GDP, the north carries the load of income taxes, while at 3.0% of GDP the south carries the load of excise duty.
- The south suffers from consumption, and capital spending by more than the north (1.2% of GDP against 0.4-0.6% of GDP).

Major estimation results

Fiscal multiplier (2011-2013)

- Income tax rises and spending cuts hit the south harder than the north.

	North	South	Italy
Tax rises	-0.23	-0.23	
Income tax (+)	-0.16	-0.43	-0.23
Consumption tax (+)	-0.41	-0.42	-0.41
Spending cuts	-0.22	-0.58	
Consumption spend. (-)	-0.27	-0.70	-0.42
Capital expenditure (-)	-1.48	-1.85	-1.67

Major estimation results

The overall impact of Italy's emergency budget (2012)

- Tax rises and spending cuts hit the south harder than the north.

	North	South	Italy
Effect due to tax rises	-0.23%	-0.31%	-0.25%
Effect due to spending cuts	-0.56%	-1.77%	-0.85%
Overall effect	-0.80%	-2.08%	-1.10%
Expected change of GDP (2012)	-1.40%	-2.90%	-1.80%

Conclusions

- Empirical evidence shows how **fiscal policy** in the south **differs** from that in the north.
- The **south** suffers from **income tax and spending cuts** by more than the north.
- The **north** and the **south** should be treated as **different types of economy**. Italy is indeed a **dual economy**.

Policy implication

- Our data shows that the south suffers from spending cuts, especially from capital spending cuts, by more than the north. **Is such fiscal policy for the south of Italy, i.e. an under-developed area, desirable?**

Thank you very much!