1988/1989

OECD ECONOMIC SURVEYS

ITALY

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ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

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- to achieve the highest sustainable economic growth and employment and a rising standard of living in Member countries, while maintaining financial stability, and thus to contribute to the development of the world economy;
- to contribute to sound economic expansion in Member as well as non-member countries in the process of economic development; and
- to contribute to the expansion of world trade on a multilateral, non-discriminatory basis in accordance with international obligations.

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The Socialist Federal Republic of Yugoslavia takes part in some of the work of the OECD (agreement of 28th October 1961).

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Table of contents

Introduction		9
I.	**Macroeconomic consequences of the budget deficit**	10
	Deficits and debt	10
	Crowding out?	17
	Financial consequences	21
II.	**Industrial adjustment**	23
	Introduction	23
	Adjustment: productivity and export performance	25
	Factors behind adjustment	33
	The microeconomic role of the State	39
	Conclusion	53
III.	**Recent developments**	55
	Strong growth of domestic demand	55
	Continued high unemployment	60
	End of disinflation?	63
	Worsening current account	66
	Capital and exchange-market volatility	68
IV.	**Policies and prospects**	71
	Slow fiscal adjustment	71
	Monetary policy	80
	Prospects for 1989 and 1990	84
V.	**Conclusions**	88
Notes and references		95

Annexes

I. Industrial adjustment: background information 102
II. Main policy measures 112

Statistical annex 119

Tables

1. Trends in public deficits and debt 12
2. Changes in the general government financial balance 13
3. International comparison of government deficits and debt 15
4. Breakdown of government debt 19
5. Productivity increases in the business and manufacturing sectors 27
6. "Revealed" comparative advantage: main OECD countries 31
7. Financial position of enterprises 34
8. Public investment in Italy 40
9. Measuring the efficiency of some public services 42
10. Direct subsidies in some OECD countries 45
11. Transfers to industry, 1978-84 46
12. R&D expenditure and the diffusion of technology 50
13. Demand and supply 57
14. Households' appropriation account 58
15. Gross fixed capital formation by sector and product 59
16. Employment and the labour market 61
17. Regional indicators of unemployment in 1987 62
18. Wage indicators 65
19. Foreign trade volumes 66
20. Breakdown of changes in the current balance 66
21. Balance of payments 67
22. Central government budget 72
23. Consolidated general government account 74
24. Financing of public sector deficit and public debt 75
25. Public finance consolidation programme 77
26. Monetary aggregates 81
27. Short-term projections 86

Annex I

A1. Structural shifts 1968-1987 106
A2. Structure of output and of imports of main OECD countries 107
A3. Adjusted intra-industry trade index 108
A4. The public sector in Italy: definitions 109

Statistical Annex

Selected background statistics 120

A. Expenditure on gross domestic product, current prices 121
B. Expenditure on gross domestic product, constant 1980 prices 122
C. Gross domestic product, by kind of activity 123
D. Household appropriation account 124
E. General government account 125
F. Prices and wages 126
G. Employment indicators 127
H. Money and credit 128
I. Foreign trade by main commodity groups 130
J. Geographical breakdown of foreign trade 131
K. Balance of payments 132

Diagrams

1. Measures of fiscal stance 11
2. Saving-investment balances and macroeconomic performance 14
3. International comparison of real short-term interest rates 16
4. Composition of household wealth 20
5. Trends in value added in industry and the service sector 24
6. Trade balances by principal category 29
7. External performance and competitiveness in manufacturing 30
8. Capacity-expanding investment and capacity utilisation 35
9. Unemployment and capacity utilisation 36
10. Trends in industrial activity, by size of enterprises 38
11. Contributions to GDP growth 56
12. The disinflation process 63
13. Wholesale prices 64

14. The exchange rate and competitiveness 69
15. Government expenditure and deficits: targets and outturns 78
16. Interest rates 82
17. Business indicators 85

Annex I

A1. Trade balances and capacity utilisation by sector 110
A2. Value added as a percentage of output 111

BASIC STATISTICS OF ITALY

THE LAND

Area (1 000 sq. km)	301.3	Population of major cities, 1986:	Thousands
Agricultural area (1 000 sq. km) 1984	217.5	Rome	2 817
		Milan	1 479
		Naples	1 201
		Turin	1 025

THE PEOPLE

Resident population, 1/1/1987 (thousands)	57 291		Thousands
		Labour force, 1987	23 669
No. of inhabitants per sq. km	190	Employment, 1987	20 836
Net natural increase in population: annual average 1983-1986 (thous.)	34	in agriculture	2 169
Net rate per 1 000 inhabitants (average 1983-1986)	0.6	in industry	6 716
		in services	11 952

PRODUCTION

Gross Domestic Product in 1987 (trillions of lire)	982.6	Origin of gross domestic product in 1987 (at market prices) per cent of total:	
GDP per head in 1987 (US $)	13 224	Agriculture	4.1
Gross fixed capital formation:		Industry	28.6
Per cent of GDP in 1987	19.9	Construction	5.5
Per head in 1987 (US $)	2 626	Other	61.8

THE PUBLIC SECTOR

Public consumption in 1987 (percentage of GDP)	16.9	Public debt in 1987 (percentage of GDP)	92.4
Current revenue of general government in 1987 (percentage of GDP)	40.1	General government investment in 1987 (percentage of total investment)	17.8

FOREIGN TRADE

Exports of goods and services as a percentage of GDP, 1987, (OECD, SNA)	18.0	Imports of goods and services as a percentage of GDP, 1987, (OECD, SNA)	18.3
Main export categories, as a percentage of total exports, 1987 (SITC):		Main import categories, as a percentage of total imports, 1987 (SITC):	
Machinery (71 to 77)	26.0	Foodstuffs (0)	12.4
Fabrics and textile goods (65)	6.3	Machinery (71 to 77)	17.7
Chemical products (5)	7.5	Metals, ores and scrap (67 + 68)	5.7
Automobiles and parts (78 + 79)	8.8	Mineral fuels (3)	13.9
Mineral fuels (3)	2.4	Chemical products (5)	11.2

THE CURRENCY

Monetary unit: Lira	Currency units per US dollar, average of daily figures:	
	Year 1987	1 297.0
	November 1988	1 304.1

Note: An international comparison of certain basic statistics is given in an annex table.

This Survey is based on the Secretariat's study prepared for the annual review of Italy by the Economic and Development Review Committee on 21st November 1988.

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After revisions in the light of discussions during the review, final approval of the Survey for publication was given by the Committee on 13th December 1988.

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The previous survey of Italy was issued in August 1987.

Introduction

In 1988, for the fifth consecutive year, GDP growth in Italy was one of the highest in Europe at between 3½ and 4 per cent. This expansion has been based on the strength of domestic demand and rapid growth of exports. As a result, the rate of unemployment has stabilized, albeit at a level which is still high. The slowdown in inflation came to an end towards late 1987, with the rise in consumer prices – at nearly 5 per cent, the lowest rate for almost twenty years – still above the European average. Buoyant export volumes and favourable terms-of-trade developments have helped to limit the deterioration in the current balance: the external deficit for 1988 is estimated at around ½ per cent of GDP. It is the scale and speed of adjustment in industry since the early 1980s which are largely responsible for this sound performance. Private firms have been the main players involved, but central government has also devoted very substantial resources to the adjustment process.

But the overall picture is not entirely unclouded. The results achieved on the inflation front are largely attributable to external influences. The Lira has appreciated in real terms since 1985, worsening Italy's competitive position. The main source of macroeconomic disequilibrium remains the public sector deficit: government debt continues to expand and now amounts to almost 100 per cent of GDP. This inevitably tends to divert domestic savings from the private sector. It also means keeping real interest rates high, which exacerbates the accumulation of debt and also restricts the monetary authorities' room for manœuvre. Therefore one of the fundamental objectives of economic policy is to reduce the government deficit, and indeed achieve a primary surplus (i.e. exclusive of interest payments) in the near future.

The macroeconomic consequences of the fiscal imbalance are analysed in Part I. Part II assesses the scale of industrial restructuring to date and the effectiveness of adjustment. The role played by the authorities in this process and, in particular, government aid to industry are discussed in greater detail. Part III looks at recent developments in the economy. Economic policy and short-term projections are the subject of Part IV. Policy conclusions are presented in Part V.

I. Macroeconomic consequences of the budget deficit

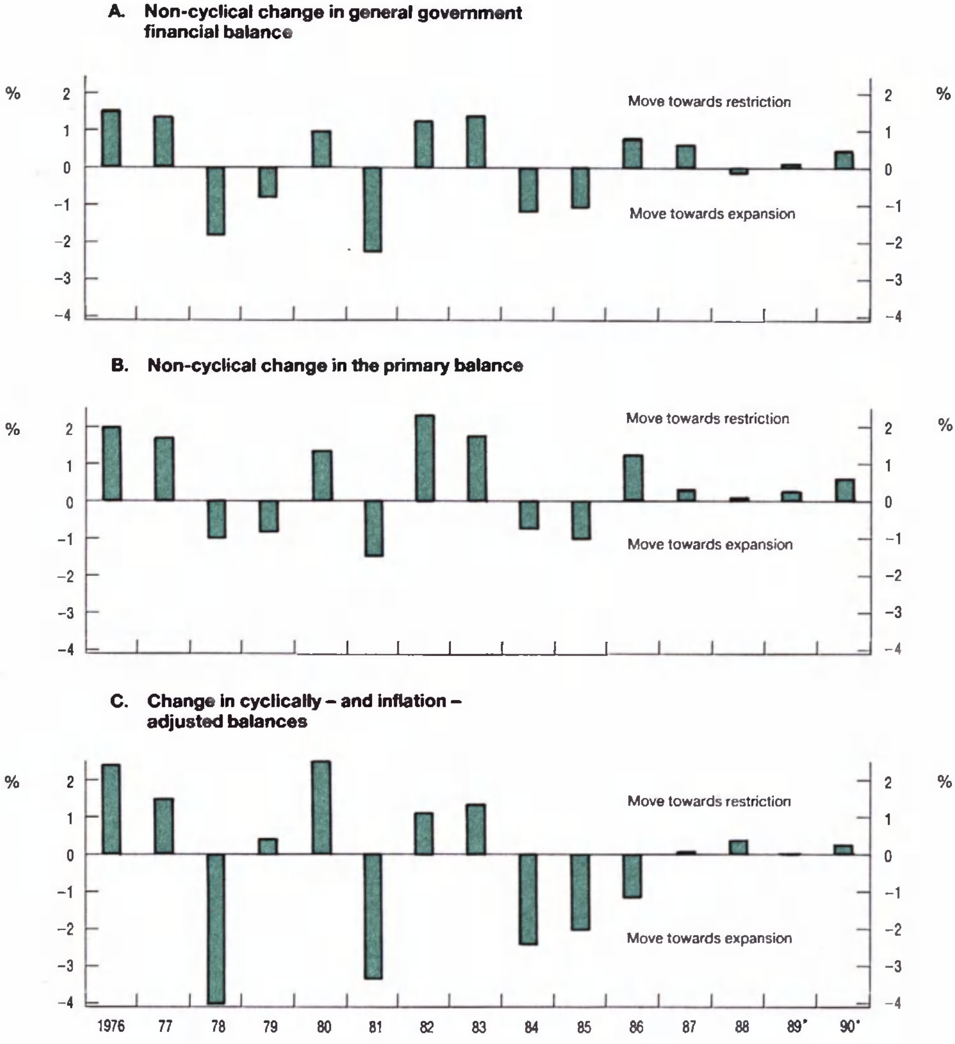
The rapid expansion of public spending since the early 1970s and the increasing burden of public sector borrowing are key features of the Italian economy. Government debt now stands at almost 100 per cent of GDP. Though the economic consequences of this have been many and diverse[1], growing public sector borrowing, in particular, may well have deprived the private productive sector of investible funds. The consequences of this have been partly masked by favourable external factors in recent years, with oil prices falling and international trade picking up.

Deficits and debt

At the end of the 1960s, Italy's general government borrowing requirement, at under 3 per cent of GDP, was fairly low, though still higher than that of most other OECD countries, with the exception of Ireland: the OECD average then stood at 0.5 per cent of GDP. From the beginning of the 1970s, the *government* deficit began to widen steadily and rapidly peaking at 12.5 per cent of GDP by 1985. In the same year, the *enlarged public sector* deficit – which includes a number of public and quasi-public bodies (post and telecommunications, railways, electricity, etc.) – peaked at 14.7 per cent of GDP[2]. This deficit has since declined both as a percentage of GDP and in absolute terms to L 114 000 billion in 1987, 11.6 per cent of GDP.

The persistent upward drift in the general government deficit (national accounts basis) was due both to lower growth and to structural factors (Diagram 1). Slower growth and rising unemployment in the early 1970s weakened tax receipts and increased social transfers. Fiscal policy was also deliberately expansionary, particularly from 1970 to 1975 when the structural budget deficit (i.e. the general

Diagram 1. **MEASURES OF FISCAL STANCE**
As a percentage of nominal GDP



* OECD Secretariat forecasts.
Note: *Panel A* shows the change in the cyclically-adjusted financial balance.
Panel B shows the change in the cyclically-adjusted financial balance excluding interest payments.
Panel C shows the change in the cyclically-adjusted financial balance adjusted to take account of the effect of inflation on the real value of the public debt.
Source: OECD Secretariat estimates.

Table 1. **Trends in public deficits and debt**

As a percentage of GDP

	Average 1970-74	Average 1975-79	Average 1980-85	1986	1987	1988[1]
1. General government borrowing requirement	–6.4	–10.2	–11.0	–11.4	–10.5	–10.0
2. Borrowing requirement excluding interest payments	–4.4	–5.8	–3.9	–3.0	–2.3	–1.6
3. Interest payments	–2.0	–4.3	–7.1	–8.5	–8.1	–8.4
4. Average nominal interest rate[2]	4.2	7.3	10.1	9.6	8.9	8.9
5. GDP deflator	10.8	16.7	13.9	7.5	5.6	4.9
6. Average real interest rate [4]-[5]	–5.2	–8.1	–4.2	2.0	3.1	3.8
7. GDP growth	4.0	3.8	1.7	2.9	3.1	3.7
8. Debt/GDP ratio[3]	50.0	61.2	83.6	87.9	92.4	94.1

1. Secretariat estimates.
2. Interest payments as a percentage of end-of-year debt.
3. End of period.

Sources: ISTAT, Banca d'Italia, OECD Secretariat.

government deficit corrected for cyclical influences) increased with virtually no interruption. Interpretation is complicated, however, by the problems of defining potential GDP growth in a period of supply shocks and industrial restructuring. From 1975 to 1980, the rising burden of interest payments – reflecting essentially the accumulation of past deficits – started to influence significantly the development of the borrowing requirement. Interest payments as a percentage of GDP doubled from 1970-1974 to 1975-1979 (Table 1). But it was movements in the primary budget deficit (i.e. exclusive of interest payments), reflecting fiscal policy choices, that really determined the development of the total deficit. The OECD's calculations of the primary structural budget balance shown in Diagram 1, panel B, suggest that up to 1980 the demand impact of fiscal policy remained broadly unchanged, with movement towards expansion one year being followed by movement towards consolidation the next.

From 1980 to 1985, fiscal policy first moved in a restrictive direction, becoming expansionary thereafter. But the main factor behind the growth of the global deficit was interest payments, averaging 7.1 per cent of GDP. The gradual improvement in the business climate from 1985, a slowdown in interest payments and the adoption of a number of discretionary measures to cut the primary structural deficit achieved deficit reduction of almost 1 percentage point of GDP a year. Given so many factors

Table 2. **Changes in the general government financial balance**[1]

As a percentage of GDP, annual averages

	1970-75	1975-80	1980-85	1985-88
1. Change in total balance	–1.7	–0.8	–0.8	+0.8
2. Change in cyclically adjusted balance	–1.2	+0.3	–0.4	+0.4
3. Change in cyclically- and inflation-adjusted balance	0	+0.8	–1.1	–0.3

1. A + sign denotes a decrease and a – sign an increase in the balance.
Source: OECD Secretariat.

conducive to lower budget deficits (the appropriation by the central government of much of the windfall gains from the fall in oil prices; a brisk pickup in domestic demand and exports, and revenue-enhancing tax reform), the extent of deficit reduction over the three years to 1988 was fairly modest.

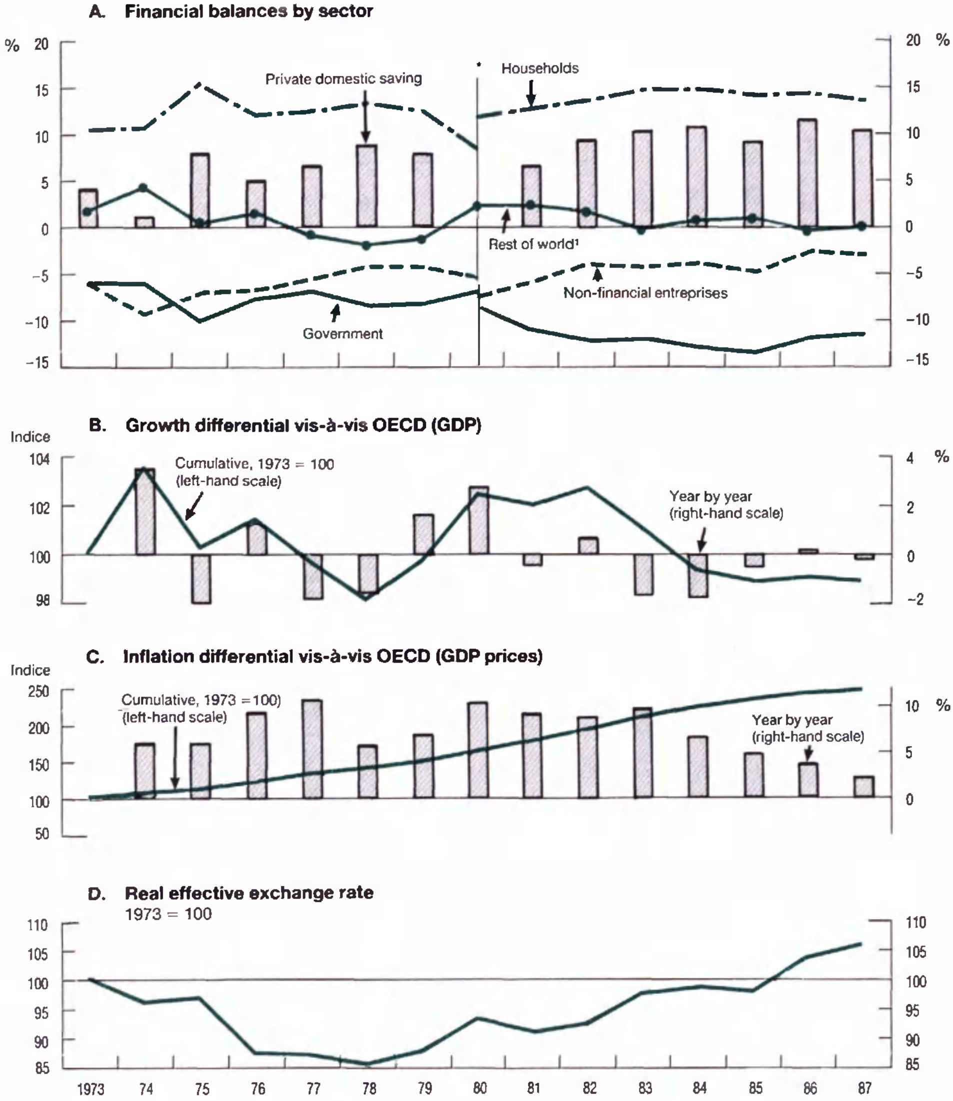
The inadequacy of fiscal consolidation in recent years appears all the greater when measured by the trend in the inflation-adjusted structural balance. Up to the beginning of the 1980s, accelerating inflation had the effect of reducing government debt in real terms. Since then, notably between 1981 and 1985, the pace of deceleration in inflation was such as to reverse the process. From 1980 to 1985, the structural deficit deteriorated faster after adjustment for inflation than before. Since 1985, taking the effects of the slowdown in inflation into account, fiscal policy has remained overall expansionary.

After hovering in the range of 25 to 30 per cent of GDP over the previous 25 years[3], government debt began to rise steeply from 1971 when it reached 40 per cent of GDP. By 1987 it was estimated at 92 per cent of GDP (revised national accounts basis)[4]. Mounting debt meant heavier-and-heavier interest payments, going from 1.8 per cent of GDP in 1970 to 6.2 per cent in 1980. This trend continued up until 1984, (with interest payments rising from 5.4 per cent to 8 per cent in GDP; revised national accounts basis). Since 1984, as the central government borrowing requirement declined, the interest burden stabilized at around 8 per cent of GDP. While such cross-country comparisons have well-known difficulties[5], it is worth noting that the debt/GDP ratio is very much higher in Italy than in other similar European countries.

Recent years have illustrated well the danger of falling into a vicious circle of deficit, debt and interest payments. The main elements on which the interaction

Diagram 2. **SAVING-INVESTMENT BALANCES AND MACROECONOMIC PERFORMANCE**

As a percentage of GDP



* Break in the series.

1. A positive rate denotes an inflow of capital (current external deficit).

Sources: Banca d'Italia; OECD, *National Accounts.*

Table 3. **International comparison of government deficits and debt**

As a percentage of GDP

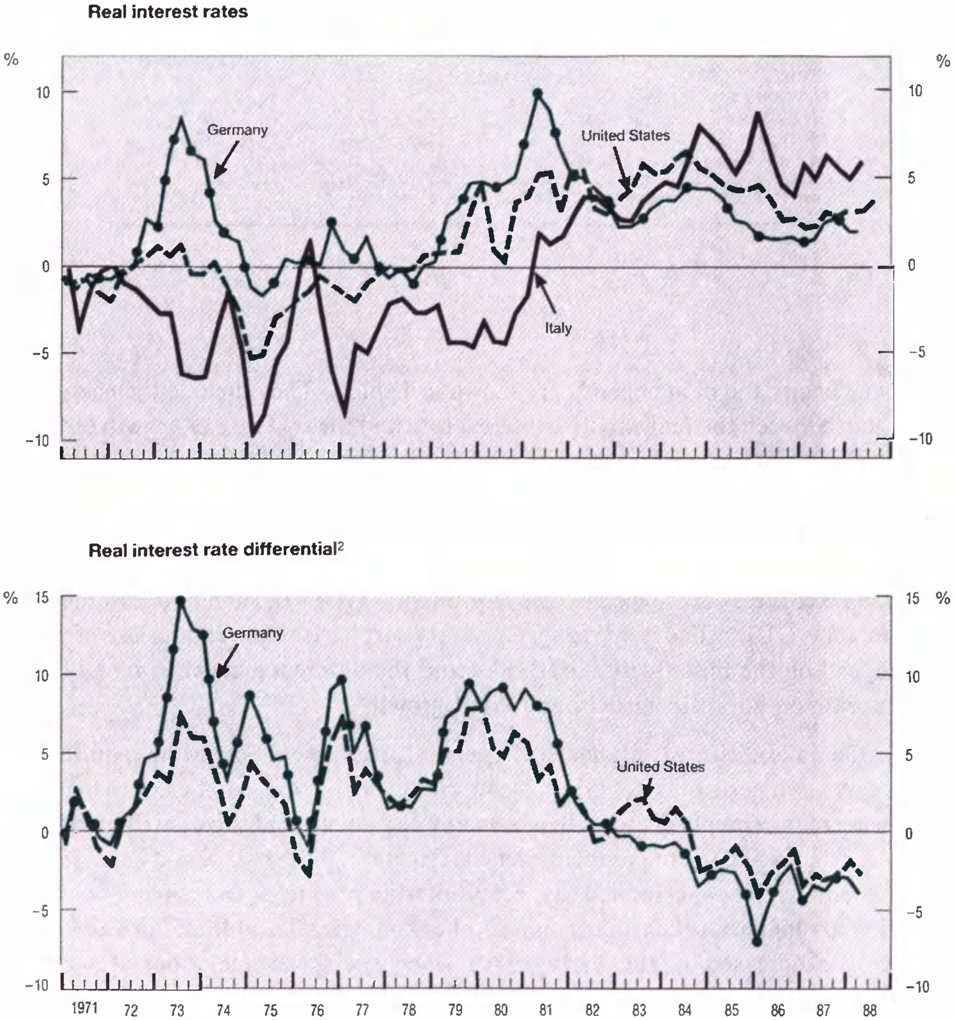
		Financial balance	Government debt (gross)
Italy	1970	–3.7	38.5
	1980	–8.5	58.5
	1987	–10.5	92.4
3 major European countries			
Germany	1987	–1.7	43.3
France	1987	–2.5	47.4
United Kingdom	1987	–1.5	50.6

Source: OECD *National Accounts*; OECD Secretariat.

between deficits and debt depends are shown in Table 1. They include the narrowing of the gap between the real effective interest rate and the real rate of growth of GDP. Previously the mounting debt burden had been partially masked by inflation and the monetisation of part of the debt. By 1988, the real effective interest rate (below the real market interest rates on government new issues inasmuch as a still large part of the government's financial resources – from, e.g., post office deposits – is raised at below market rates) overtook the rate of growth of GDP. In such circumstances, to prevent debt/GDP ratios from rising, a primary surplus is required, the size of which will depend on the initial debt/GDP ratio and the difference between real average interest rate on government debt and GDP growth[6].

In the wake of the two oil shocks, the general government borrowing requirement rose steeply as a percentage of GDP. Domestic saving proved insufficient to meet the borrowing requirements of the Italian economy as a whole, and this contributed to the build-up of a large current payments deficit. Except in these two periods, the general government deficit was funded by net domestic private sector saving which is traditionally higher in Italy than in most other countries. In addition, private sector saving has increased in the early 1980s when the government deficit widened substantially: despite a downward trend in the household savings ratio, a decline in the corporate sector's borrowing requirements ensured an increased financial surplus in the private sector. The early 1980s saw a fall in corporate and household investment ratios, partly cyclical in the aftermath of the oil shocks, but partly also perhaps due to "crowding-out" by the public sector. More corporate investment was internally financed from 1983 than earlier.

Diagram 3. **INTERNATIONAL COMPARISON OF REAL SHORT-TERM INTEREST RATES** [1]



1. Deflated by the change in the GDP price deflator on the corresponding quarter of the previous year.
2. Rate in the countries shown *less* rate in Italy.
Source: OECD.

Crowding out?

Since the beginning of the 1970s the public sector may, through various channels, have increasingly crowded out the private sector by absorbing a larger share of domestic saving. But the nature and extent of this effect is hard to quantify since the public sector has also played a role in redistributing income, to the productive sector in particular[7]. Such redistribution sometimes served to reduce corporate costs, thus maintaining healthy profits. State financing of early retirement schemes, paying part of employers' social insurance contributions from general taxation, and direct investment incentives, were thus simply income transfers. Similarly, much of the growth in public spending served to prevent the household saving ratio falling: redundant dependent workers affiliated to the Wage Supplementation Fund (the CIG) were a case in point, since the benefits they received meant they did not have to rely solely on their own savings (see note 19). In this sense, the public sector as a whole acted as an important financial intermediary. Crowding-out effects thus arose more from the reallocation of saving. The complicated interactions between the various public sector bodies and the private sector, and the resulting loss of efficiency, as well as the many forms that transfers and subsidies took, make accurate quantification difficult[8].

The impact of the government deficit on interest rates, and hence on the economy, has differed over the years according to the monetary policies followed[9]. Up to the beginning of this decade, monetary policy tended to be accommodating and financing conditions relatively easy. As Diagram 3 shows, real interest rates were usually negative and generally below those in other countries. Monetary expansion was extremely fast, at around 17 per cent a year over the period 1970-1981. The monetary authorities pursued a flexible exchange-rate policy, with the real effective exchange rate falling by almost 15 per cent between 1973 and 1978. Inflation accelerated and the differential between Italy and its main trading partners widened appreciably. This inflationary surge had the effect of easing the burden of government debt in real terms. The average real interest burden fell from a negative 5.2 per cent over the period 970-1974 to a negative 8.1 per cent over the period 1975-1978 (Table 1), so curbing growth of the debt/GDP ratio quite considerably. The counterpart of this was that the real value of households' financial assets was also reduced: despite a high saving ratio, the ratio of their net financial assets to disposable income remained virtually flat in the late 1970s. In this sense, the budget deficit, by contributing to inflation, to some extent indirectly "crowded out" private consumption.

Nominal values became harder and harder to control in the late 1970s, raising the spectre of runaway inflation. Given experience of accelerating inflation, economic agents refused to purchase long-term fixed-interest debt without a substantial inflation-risk premium in interest rates[10]. The authorities responded by allowing the maturity of debt to shorten dramatically and by linking interest coupons on medium-term paper to short-term interest rates. With inflationary expectations running high, international confidence was eroded, fuelling speculation against the lira and worsening Italy's external position. In 1982 monetary policy was given a more restrictive turn. After again becoming positive, real interest rates[11] rose above those in Germany and the United States. This encouraged domestic banks to borrow abroad: the short-term capital inflow thus generated supported an appreciation in the real effective exchange rate. This change in thrust of monetary policy was facilitated by earlier financial market reforms, and in particular by the opening up of the government securities market. This meant that the Bank of Italy was no longer automatically required to finance the deficit and the relationship between budget deficit overruns and money supply growth became less rigid[12].

The growth of the monetary aggregates began to slacken at the beginning of the 1980s, when an ever-increasing share of government debt was being directly financed from saving, and particularly household saving, at much higher interest rates than previously. Financing the budget deficit from saving rather than money creation, has helped to limit price increases since 1983 and thus narrow the inflation differential between Italy and other OECD countries. The interest burden has risen steeply in real terms for two reasons: one, the rise in nominal interest rates resulting from tighter monetary targets and the need to mobilise savings on a large scale; and, two, the heavier real debt burden resulting from disinflation. Thus, as pointed out above, the real interest rate on government debt stood at 3.8 per cent in 1988, a rate equivalent to that of real GDP growth.

Real interest rates, which rose particularly steeply between 1983 and 1985, have remained high since. And the differential with Germany has widened. There were several contributory factors: the persistence of heavy government borrowing, the replacement of administrative controls *via* credit ceilings, by control of the money supply *via* interest rates, and a commitment by the authorities to a more stable exchange rate within the EMS in the context of capital market liberalisation[13]. The rise in real interest rates undoubtedly helped to depress capital-widening investment and to alter the composition of real investment[14]. Private sector investors increased their financial assets at the expense of investment in real assets. Thus, households' financial assets, which accounted for less than 100 per cent of disposable income at end-1980, were over 140 per cent of disposable income in 1987, while their real assets

Table 4. **Breakdown of government debt**

As a percentage of total debt

	1978	1985	1987
Total debt	100.0	100.0	100.0
Bank of Italy	27.3	16.6	15.2
Excluding Bank of Italy			
Medium and long-term debt	25.0	43.2	47.2
Treasury bills	21.5	22.1	21.0
Post-office deposits	15.2	9.0	9.2
Loans by lending institutions	8.9	5.3	4.5
Other domestic debt	0.9	0.4	0.3
Foreign debt	1.2	2.7	2.6
Negotiable debt			
Medium and long-term[1]	100.0	100.0	100.0
Banks	64.5	43.3	31.7
Households	32.8	43.4	47.2
Other[2]	3.7	13.3	21.0
Treasury bills	100.0	100.0	100.0
Banks	44.8	17.6	13.9
Households	43.3	76.2	77.6
Other[2]	11.9	6.2	8.5
Total	100.0	100.0	100.0
Banks	55.9	34.6	26.2
Households	39.0	54.2	56.6
Other[2]	5.1	11.2	17.2

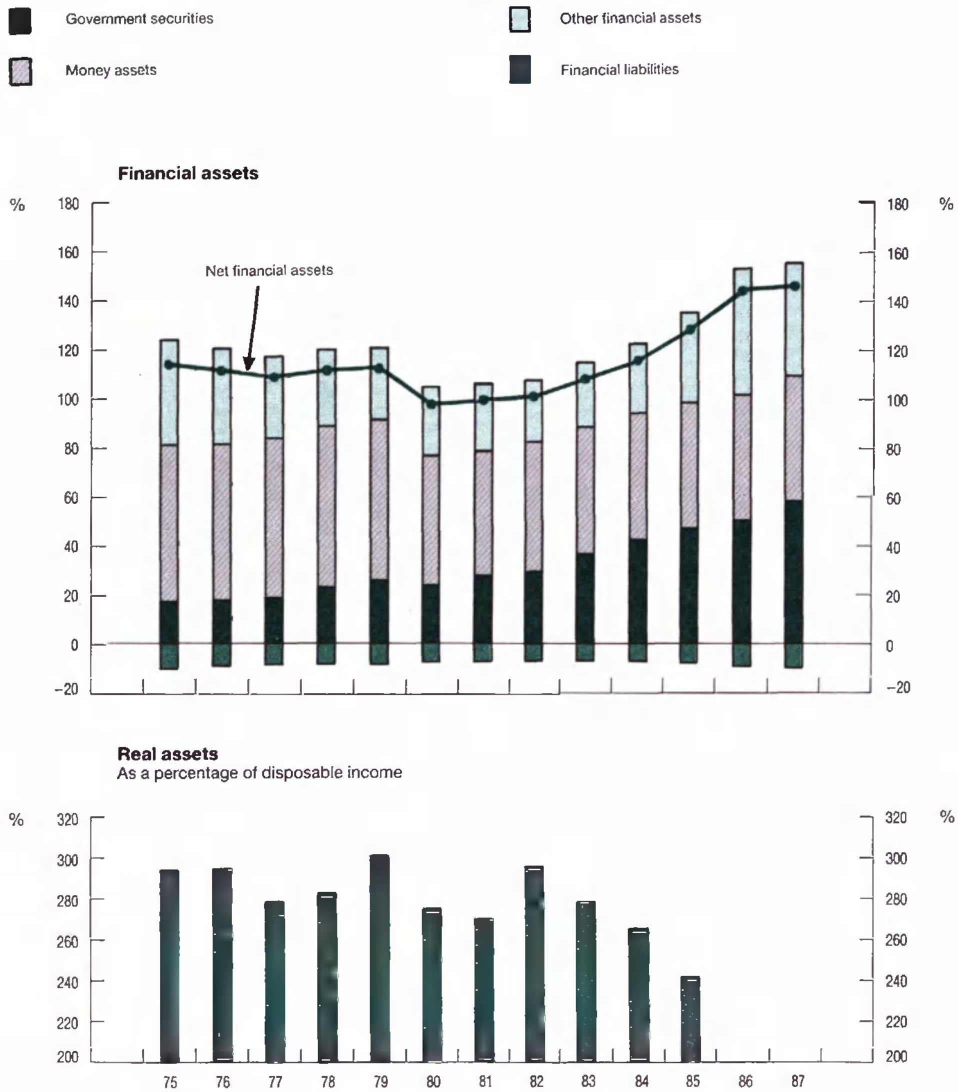
1. Mainly floating rate long-term debt, the interest rate on which varies with short-term interest rates.
2. Since 1985 this item has included mutual fund transactions.

Source: Banca d'Italia.

fell from three to two and a half times their income during the same period. Crowding out has probably also occurred *via* exchange rates, since the lira's appreciation has depressed demand for Italian goods. On the other hand, the impact of crowding out was cushioned by the fact that the appreciation of the lira forced the corporate sector to restructure in order to increase productivity (see Part II).

All in all, the public sector borrowing requirement may have had crowding-out effects varying in nature and intensity over time. In the early 1970s, financial crowding out was certainly limited by the public sector's role as financial intermediary and the accommodating thrust of monetary policy. However, this policy caused inflation to accelerate, and it was through the fall in the real value of assets that this effect was felt. During the 1980s, the rise in both real interest rates and the exchange rate crowded out the private sector by curbing their investment capacity, especially for capital widening investment and residential construction.

Diagram 4. **COMPOSITION OF HOUSEHOLDS WEALTH**
As a percentage of disposable income



Note: Break in the series of disposable income, 1980.
Source: Banca d'Italia.

Financial consequences

The absorption by the market of greater-and-greater amounts of government debt was facilitated by a significant shift in households' portfolios away from bank deposits to government paper. The share of government paper in the financial wealth of households has risen substantially over the past ten years, from around 4.5 per cent in 1976 to almost 30 per cent in 1987 (if government paper in households' mutual fund holdings are included). By contrast, the share of bank deposits has fallen by nearly 20 percentage points in the space of ten years to only 40 per cent of households' financial assets by 1987. The authorities encouraged households to shift their portfolios in this way by exempting income from government securities from personal tax. When interest payments are thus exempted, the risk of a surge in debt is increased[15]. Moreover, since the beginning of the 1970s – when controls were imposed on outward capital movements – the share of foreign assets has also fallen considerably[16]. As pointed out above, there has been a marked shift in household wealth from real assets to government securities since real interest rates started to rise. By the end of 1987, households held 56.6 per cent of total negotiable government debt (which itself accounts for 68 per cent of the total debt) against 46 per cent in 1976.

In contrast to practices in the other major OECD countries, only a small proportion of the debt took the form of long-term fixed-interest securities. Inflationary expectations were such that such bonds would have had to carry a nominal rate of interest judged by the authorities to be unacceptably high[17]. Treasury bills and medium-term Treasury certificates (whose interest rates are pegged to those on six-month to one-year Treasury bills) accounted for 60 per cent of government debt in 1987. Government interest payments therefore follow closely short-term interest rates. This has several implications:

- In view of the burden of government debt, public expenditure and hence the budget deficit are extremely vulnerable to changes in short-term interest rates: a 1 percentage point rise in short-term rates results in additional budget expenditure over a full year of L 7 trillion (pushing up the budget deficit by around 7 per cent). Furthermore, an increase in rates can have a perverse effect on private consumption as interest on public debt received by households amount to a large part of their income.
- The independence of monetary policy from fiscal policy is thereby considerably diminished. Despite moves to greater reliance on interest rates to control credit, the Bank of Italy has had twice to impose ceilings on bank lending, so as to avoid rates rising too steeply at times of heavy growth in lending or pressure on the lira;

- The terms on which government debt can be funded depend in large measure on changes in agents' short-term expectations about inflation or monetary policy. In periods of strain (from mid-1987 to mid-1988, for example), the Treasury has had problems in raising medium and long-term funds, which could have quite considerable repercussions on the maturity of the debt (see the discussion of monetary policy in Part IV);
- Last, it is difficult to control the growth of bank lending because of the liquidity of government securities held by banks, who can meet a high demand for credit by selling off part of their government security portfolios. Similarly household savings are still highly liquid despite the fall in the share of the strictly monetary assets held.

Also the Italian Government has increased its Ecu borrowing (issues totalled Ecu 4.25 billion between January and September 1988). This had the immediate effect of reducing the direct cost of borrowing for the Treasury (7¾ per cent for five-year Ecu-denominated Treasury bonds, compared with 13 per cent for four-year bonds on the Italian market) and increase foreign exchange reserves. On the other hand, it does mean that greater domestic restraint and discipline will be needed in order to limit the exchange risk.

By virtue of its size and composition, government debt makes the Italian economy particularly vulnerable. The broadening and internationalisation of financial markets (exchange controls were relaxed in October 1988) has accentuated this vulnerability, since there is a risk that households may, one day, seek to diversify into new financial instruments. Both domestic and external considerations suggest that the positive differential between real interest rates in Italy and some other EMS countries, notably Germany, is likely to persist. Domestically, high interest rates will continue to be necessary in order to mobilise large amounts of cash savings, contain money growth and prevent a resurgence in inflation; externally, Italy's EMS commitments leave little room for manœuvre. The implications of high debt interest costs (especially if inflation continues to slow), as well as the allocation of investible funds, makes rapid fiscal consolidation necessary to produce a large primary surplus that would first at least stabilize (and then reduce) the debt/GDP ratio in the medium term. This concern is shared by the Italian Government which has proposed a medium-term fiscal consolidation plan (analysed more fully in the paragraphs on fiscal adjustment in Part IV), aimed at reducing the primary deficit by 1992, both by containing the public spending/GDP ratio and by increasing tax pressure. This plan also rests on a hypothesised fall in interest rates: this is assumed to result from a turnaround in financial-market expectations prompted by the changed outlook for the budget deficit.

II. Industrial adjustment

Introduction

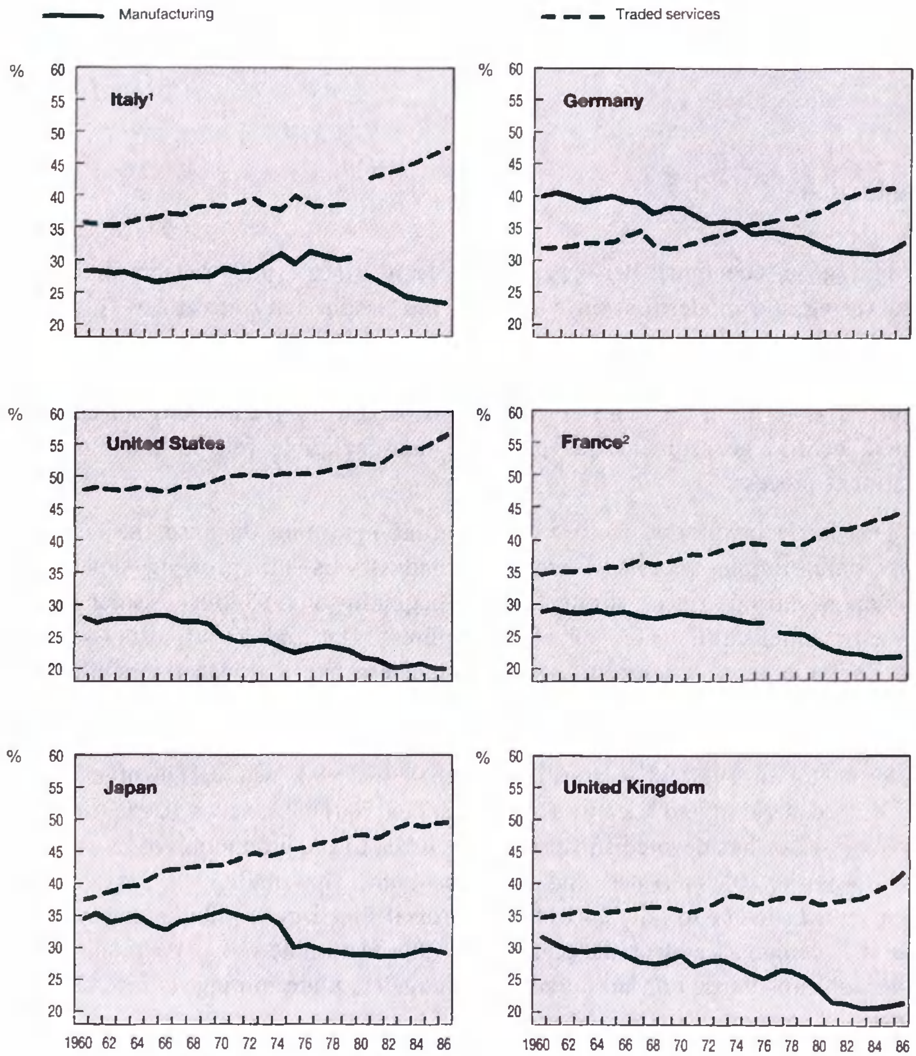
The good economic performance of Italy since 1983 reflects industrial restructuring and modernisation which spurred productivity growth, with private enterprises being particularly dynamic. The situation in the larger enterprises has improved and the key position of small and medium-sized enterprises has been reinforced. In terms of the scope of the measures taken and the amount of assistance granted, central government has played a non-negligible role in the industrial adjustment process.

This fairly favourable picture of the situation cannot disguise the fact that results differ among sectors. Capacity in industry is still growing slowly and employment started to increase only from the beginning of 1988. Businessmen appear to have remained cautious in view of high interest rates and labour costs (wages in particular) and, until very recently, to have concentrated their investment efforts on plant rationalisation and modernisation. Productivity is still mediocre in the sheltered sector of the economy. Despite improving recently, productivity in the marketable services sector in 1987-88 was still lower than in 1980, whereas in other major European countries it had risen by 10 to 15 per cent in the last seven years. Although the public sector has devoted substantial resources to the production of marketable and non-marketable services and to investment, the quality of services and infrastructures seems to fall short of standards attained in neighbouring countries. These shortcomings weigh on the economic system as a whole and, in particular, are a not insignificant burden on manufacturing industry, undermining its international competitive position.

This Part of the Survey deals with the main aspects of industrial adjustment. The first section analyses productivity trends and external performance as indicators of adaptability and efficiency. The next section looks at the factors behind adjustment, in particular the role of macroeconomic policies, and stresses the weaknesses which

Diagram 5. **TRENDS IN VALUE ADDED IN INDUSTRY AND THE SERVICE SECTOR**

As a percentage of GDP



1. New definitions, from 1980.
2. New definitions, from 1977.

Source: OECD, *National Accounts.*

stand in the way of improved performance. The third section is devoted to industrial policy; it considers policy targets and instruments and gives an estimate of the amount of assistance provided and an assessment of its impact.

Adjustment: productivity and export performance

Unlike most other OECD economies, the contribution of manufacturing industry to GDP continued to grow in Italy during the 1970s (Diagram 5). The counterpart of the share of marketable services and the public sector was the decline of agriculture, not manufacturing industry as elsewhere. Industry's share in GDP fell later in Italy than in the other main European countries, and the decline in the 1980s was less marked.

As in other OECD countries, the increased share of marketable services was correlated with higher standards of living[18]. But, contrary to what happened in some other countries (in particular in Japan and Germany, and to a lesser extent in the United States and France), the share of marketable services in household final consumption did not expand between 1975 and 1982. The consumption of services by industry, on the other hand, grew very rapidly (5 per cent a year in real terms between 1975 and 1981), with the share of purchases of services in industrial value added expanding. The process continued during the 1980s and partly reflects the fact that some industrial enterprises have contracted out service activities previously carried out in-house: this is discussed below. The two sections which follow look at industrial adjustment from two angles: the first considers recent productivity trends, while the second analyses export performance over the last ten or fifteen years.

The recent improvement in productivity

Labour productivity slowed very abruptly throughout the economy after the first oil shock, falling from an annual increase of 6.7 per cent over the years 1960-73 to 1.9 per cent during the period 1973-83 (Table 5). The fall in the rate of GDP growth was not matched by an adequate adjustment in employment. Up to 1980, total employment continued to increase by 1 per cent per year on average, compared with 0.3 per cent in the other European countries (Table A1 in Annex I). Unlike developments in other countries, the slowdown in productivity growth was particularly marked in the *non-manufacturing* sector. Employment in services in fact rose by 2.7 per cent per year in Italy, as against 1.8 per cent in Europe as a whole. In *manufacturing* industry, the sector hardest hit by the international recession, productivity gains were still averaging 3.7 per cent per year between 1973 and 1983 – a rate which was higher than in most other European countries because of relatively brisk growth of value added. The acceleration of productivity growth after 1983 was again concentrated in manufacturing. The labour shakeout which had begun in 1981 and 1982 gathered force subsequently as the Wage Supplementation Fund (CIG) made payments increasingly out of public funds to employees made totally or partially redundant by restructuring[19]. In the other European countries, productivity growth continued to slow (with the important exception of the United Kingdom).

Much of the improvement in labour productivity reflected an increase in the capital/labour ratio. This substitution was, however, less pronounced than during the period 1973-83. At that time it accounted for almost one-half of labour productivity growth. Labour productivity increased by 1.9 per cent per year, of which 0.9 percentage point could be attributed to factor substitution (substitution being calculated as the change in the capital/labour ratio weighted by the share of capital). Over the period 1983-1987, productivity growth rose to 2.1 per cent per year, with factor substitution accounting for one-quarter of this increase. The rest was attributable to the growth of total factor productivity (TFP).

Growth of total factor productivity is an indicator of increased efficiency, giving an approximate idea of the scale of the structural adjustment achieved by an economy[20]. Before the first oil shock, the rate of growth of TFP in Italy was one of the highest (along with Japan) amongst the OECD countries – 4.7 per cent per year on average, compared with 2.9 per cent for the area as a whole. Similarly, its rate of decline was one of the steepest. Between 1973 and 1983, TFP grew at about 1 per cent per year, which was less than in France, Germany and Japan. However, a turnaround from 1983 brought growth over the period 1983-87 nearly up to that recorded in the other main European countries, although it is too soon to say how much of this is purely cyclical and how much will last.

The upturn in TFP growth was possible only because of increased investment which embodied new technology. Investment had declined very sharply between the two oil shocks – in 1979, real non-housing fixed investment was 3 per cent below its 1973 level, whereas in Europe as a whole it was 6 per cent above that level – and the capital stock aged as a result. In 1983, when the effects of the second oil shock had worn off, it was estimated that only 23 per cent of machinery and equipment was five years old or less, compared with 45 per cent in the United States and a little over 33 per cent in France, Germany and the Netherlands. The very rapid growth of investment after 1983 – rising by a cumulative 24 per cent up to 1987 – mainly took

Table 5. **Productivity increases in the business and manufacturing sectors**

Average percentage changes at annual rates

	Total factor productivity			Labour productivity		
	Up to 1973[2]	1973-83	After 1983[3]	Up to 1973[2]	1973-83	After 1983[3]
Italy[1]						
Business	4.7	1.0	1.6	6.7	1.9	2.1
Manufacturing	4.2	1.9	3.3	6.2	3.7	4.8
United States						
Business	1.6	-0.4	1.5	2.2	0.2	1.4
Manufacturing	2.7	0.4	5.1	3.4	1.6	5.4
Japan						
Business	6.3	1.7	2.0	9.0	3.0	2.9
Manufacturing	4.8	2.7	2.9	9.8	5.4	5.3
Germany						
Business	3.1	1.3	2.0	5.0	2.7	2.5
Manufacturing	2.8	1.3	1.7	5.1	2.7	2.4
France						
Business	4.4	1.6	1.6	6.1	3.0	2.6
Manufacturing	4.9	1.5	0	6.4	3.1	1.7
United Kingdom						
Business	2.2	0.4	1.8	3.6	1.5	1.9
Manufacturing	3.2	0.7	3.5	4.1	1.8	3.9
Canada						
Business	2.3	0.2	1.3	2.9	1.4	1.8
Manufacturing	2.7	-0.8	5.2	3.8	0.8	5.2

1. Employment figures adjusted to take account of CIG-paid employees.
2. The starting years are: Italy, United States, United Kingdom 1960; Japan 1966; Germany 1961; France 1964; Canada 1962.
3. Closing year: 1987 for the business sector, 1986 for the manufacturing sector.

Source: OECD Secretariat.

the form of goods with a high innovation content: office machinery, precision instruments and electrical and electronic equipment. Purchases of machinery for production purposes, and machine tools in particular, returned to their 1980 level following a marked downturn at the start of the cycle. The increase in TFP after 1983 was then accentuated by the upturn in growth itself. However, capital productivity seems to have grown faster after 1983 than might have been expected on the basis of past relationships with growth of output[21]. The trend of TFP has varied very widely across sectors. In manufacturing industry, where rationalisation has mainly occurred, TFP growth increased from 1.9 per cent per year between 1973 and 1983 to 3.3 per cent per year between 1983 and 1986[22]. In private services, on the other hand, TFP declined slightly up to 1983 and has since remained sluggish.

The fairly rapid growth of productivity has helped to hold down production costs. According to a recent Confindustria study, unit output costs for the whole of the productive sector were 16 per cent lower in 1986 than the hypothetical costs that would have been registered with the same factor mix as in 1970 – the biggest improvement amongst the OECD countries after Japan[23]. However, because of higher wage increases in Italy, which were only partly offset by exchange-rate depreciation, unit output costs measured in a common currency increased more than in the other major countries. Also, stronger productivity growth does not mean that the Italian productive system is in a better position than those of the other European countries, since the calculations take account of neither the relative level of technologies nor the efficiency of productive systems in 1970.

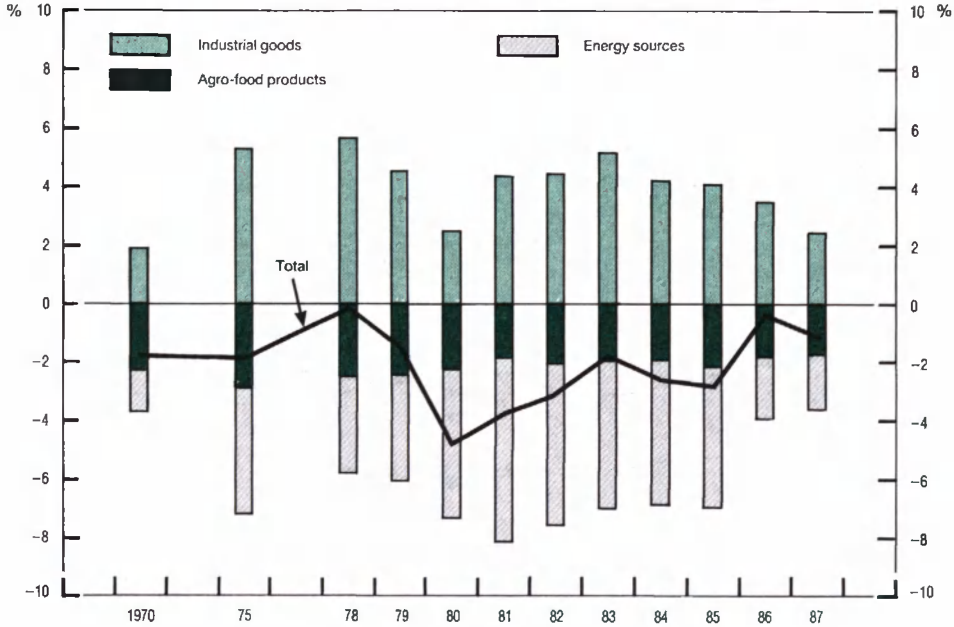
The Confindustria study also stressed the particularly good performance of *manufacturing industry* where costs were reduced by 23 per cent, evidence of the scale of adjustment required in the space of a few years to meet foreign competition. Some branches of manufacturing industry experienced more extensive restructuring, bearing in mind the resulting reduction in costs, examples being chemical and pharmaceutical products, the engineering industry, textiles and clothing, wood and furniture and the paper and publishing industry[24]. The reduction in costs achieved through restructuring in *service* activities was negligible; costs of public utilities and government-regulated services (for instance, transport, communications, banks) actually increased relative to hypothetical costs. This is particularly unfavourable in transport and communications in light of the absence of quality improvements.

A good external performance but increased import dependence

The export performance of manufacturing industry

The manufacturing sector's good export performance also gives some idea of the scale of the adjustment already achieved. Italy needs good manufacturing performance to compensate for the deficit on non-manufacturing goods trade occasioned by the country's strong dependence on energy and agro-food imports. The energy deficit widened as a result of the two oil shocks, stabilizing at around 5 per cent of GDP between 1980 and 1985 (Diagram 6). In 1986 lower oil prices halved the oil bill, but oil import volumes increased appreciably. The deficit in agro-food products has for some years been the second major cause of the trade imbalance. The deficit, close to 2 per cent of GDP on average between 1970 and 1985, declined slightly in 1986 and 1987 with the fall of the dollar, but here again volume trends remained unfavourable.

Diagram 6. **TRADE BALANCES BY PRINCIPAL CATEGORY**
As a percentage of GDP



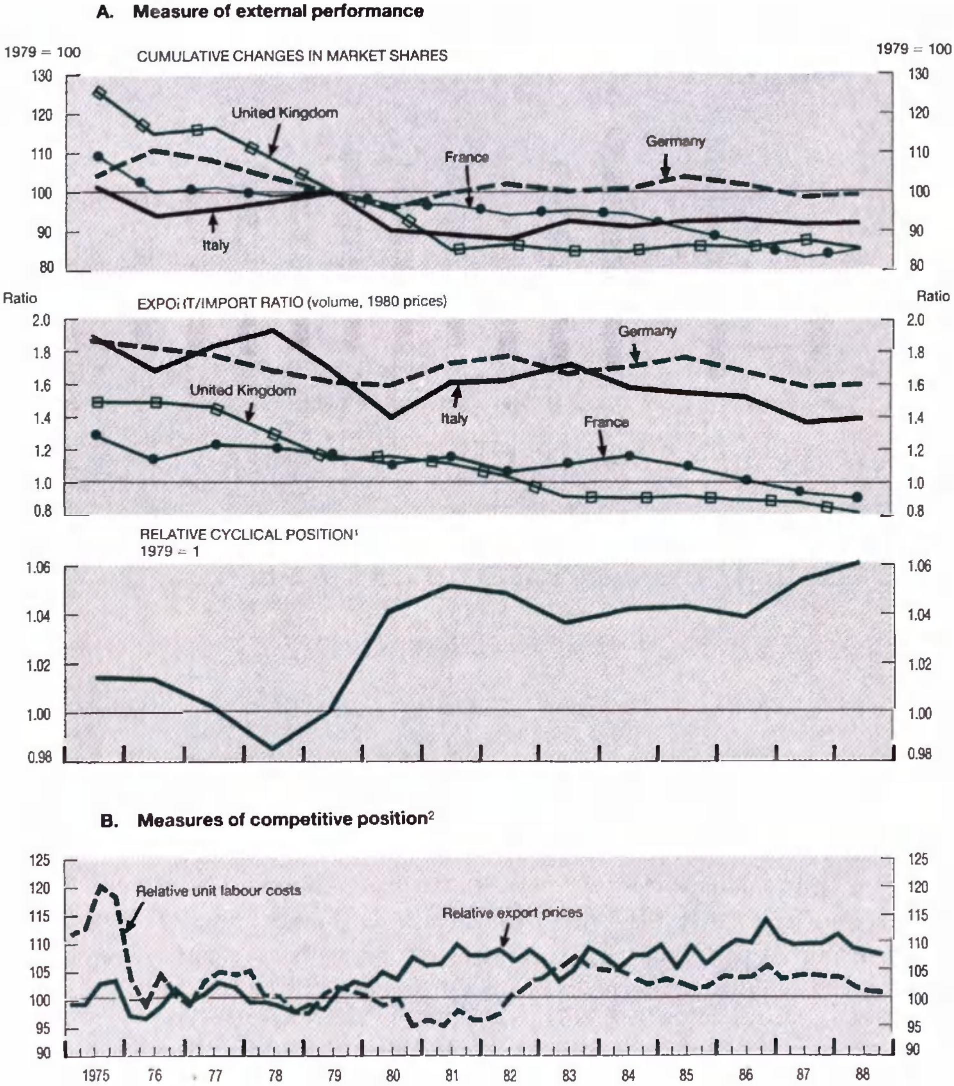
Source: Banca d'Italia, *Annual reports.*

Up to 1979, export volumes of manufactured goods increased faster than in neighbouring countries and Italy was able to maintain its market shares (see Diagram 7). In volume terms (1982 prices), the export/import ratio was over 1.5 on average, higher than in the United Kingdom or in France. From 1979 to 1983, however, overall performance deteriorated; but since then, export volumes have increased faster than those of its main European partners and Italy has again succeeded in maintaining its market shares.

Constant market share analysis

Constant market share analysis suggests that the relatively favourable trend of Italian exports over the period 1966-79 (apart from the year of the first oil shock) can

Diagram 7. **EXTERNAL PERFORMANCE AND COMPETITIVENESS IN MANUFACTURING**



1. Index of final domestic demand in Italy, divided by that of its main trading partners: Germany, France, United States, United Kingdom, Switzerland, Netherlands and Belgium, weighted by their share in Italian exports.
2. OECD Secretariat estimates for 1988.

Source: OECD.

be attributed to the fact that Italian producers succeeded in taking advantage of the most dynamic markets by adjusting the geographical distribution of their exports and the composition of their products[25]. The positive influence of geographical distribution was especially pronounced. The biggest contribution came from exports to the OPEC countries, which showed that there had been an adequate shift in resources to the most expansionary markets. The product composition of exports also contributed to market share gains, though to a lesser extent. Analysis shows that the major contribution came from the automobile, chemical and oil by-products sectors. Performance deteriorated as a result of the second oil shock. During the following period (1982-1986), Italy's performance improved progressively; geographical distribution, however, and, until very recently, specialisation by product appeared inadequate. This suggests something more fundamental behind good performance such as the overall efficiency of production, and in particular better competitiveness. Since trends in relative price or cost competitiveness were deteriorating during the 1980s, it appears that certain non-quantitative factors – technical performance and the quality of products, commercial drive and so on – sustained the growth of Italian exports. In 1985-86, moreover, the favourable results of the early 80's restructuring are becoming visible: the adjustment of product composition to foreign demand seems improved.

Efficiency of sectoral specialisation

Analysis of "revealed" comparative advantage shows the categories of products which have performed particularly well on export markets (Table 6). These

Table 6. **"Revealed" comparative advantage: main OECD countries[1]**

	Italy		Germany	France	United Kingdom	United States	Canada	Japan
	1970-72	1984-86	1984-86	1984-86	1984-86	1984-86	1984-86	1984-86
Industries[2]								
Resource-intensive	0.63	0.75	0.57	0.92	0.77	0.66	1.42	0.15
Labour-intensive	1.73	2.00	0.81	0.86	0.89	0.44	0.30	0.51
Scale-intensive	0.87	0.79	1.29	1.18	0.88	0.91	1.56	1.41
Differentiated products	1.20	1.04	1.16	0.82	1.02	1.20	0.50	1.73
Research-intensive	0.75	0.66	0.95	1.22	1.92	2.33	0.50	0.70

1. "Revealed" comparative advantage is calculated as the share of product i in the total exports of country j *divided* by the share of this product in world exports. The relative output and import structures are set out in Annex I, Table A2.
2. Examples of products in the various categories: *resource-intensive industries*: food products, aluminium processing; *labour-intensive industries*: textiles and clothing; *scale-intensive industries*: chemicals, iron and steel; *differentiated products*: machine tools; *research-intensive industries*: electronics, aeronautical industry.

Source: OECD Secretariat.

calculations suggest that the strong points of Italy's foreign trade are so-called "traditional" products with high labour intensity[26], a specialisation suggested by the pattern of both production and imports (Table A2 in Annex I). Italy also enjoys a certain comparative advantage in the production of differentiated goods (specialised machinery and equipment, engineering). The highly research-intensive sectors (pharmaceutical and electronic products), are the weakest: their share in Italian exports is small and diminishing – in sharp contrast with experience elsewhere. In Japan and Germany, for example, even though the initial situation was fairly mediocre, these products have increasingly been the focus of production and exports.

The income elasticity of Italian imports of manufactures is in the region of 2¼, close to the average for major OECD countries. Admittedly, this sort of figure implies that the foreign balance is to some extent vulnerable, but no more so than elsewhere, and the fact that exports of manufactures have responded well to changes in world demand reduces the potential vulnerability of the trade balance – as long as domestic demand growth does not differ too much from that of its main partners and relative labour costs in Italy remain fairly stable. The rate of import penetration in relation to total demand (total domestic demand plus exports) has in fact been drifting upwards for more than twenty years. This trend, altogether comparable to that observed in most of the main OECD countries, does not mean that Italy is "deindustrialising" because the process has been accompanied by a parallel increase in output sold abroad. And as production becomes more internationally integrated, intra-industry trade increases (Table A3 in Annex I). Nevertheless, the surplus on trade in manufactures has fallen from more than 5 per cent of GDP in 1983 to approximately 2 per cent of GDP in 1988 (Diagram 7).

The situation varies from one industry to another. By comparing trade balances and capacity utilisation rates by product, it is possible to single out three situations (Diagram A1 in Annex I). Industries in the first category have structural surpluses: potential supply corresponds to long-run domestic and foreign demand; the capacity utilisation rate varies according to short-term fluctuations in demand. The products concerned are the traditional ones, but they also include non-metallic minerals, metal products, agricultural and industrial machinery, wood and furniture, rubber and plastics, household appliances and televisions. The curve relating capacity utilisation and the trade balance has even risen in these industries (i.e. at given capacity utilisation, the trade surplus has increased: Diagram A1, panel A), reflecting producers' ability to exploit their comparative advantage. A second category of products is vulnerable because of inadequate productive capacity. For example, the computer, office equipment and vehicles and engines sectors face production bottlenecks; the shortfalls are persistent or even growing because supply is not expanding enough (in terms of either quantity or quality), whereas demand is increasing (See Diagram A1, panels D and E). The situation is least favourable, however, in the case of the third category, which includes sectors such as metals and basic chemicals. These sectors face serious structural difficulties, with persistent trade deficits and perennially under-utilised capacity (Diagram A1, panels B and C).

The growth of trade has resulted in Italy, as in most other OECD countries, in greater intra-industrial specialisation as well as by branch. The index of intra-industrial trade, showing the share of intra-industrial trade in total trade (Table A4 in Annex I), rose by about 10 points between 1967 and 1987, an increase comparable with the average for other European countries. The rise in the index partly reflects the more rapid expansion of categories of trade in which the proportion of intra-industrial trade is relatively high, but also an increase in intra-industrial trade in the major product categories: products whose manufacture is labour-intensive, products that show large economies of scale, and differentiated products. However, the level of the index in 1986 was still relatively low compared with the average for other European countries. Some characteristic features of Italy's system of production and distribution may partly account for this: for example, the highly-developed network of sub-contractors – which perhaps reduces external dependence – and particularly the fact that industry is specialised in the manufacture of finished products from imported intermediate products (which makes it possible to economise energy, an input that is relatively expensive in Italy).

Factors behind adjustment

Structural adjustment was facilitated in part by the introduction of specific microeconomic policies. These included, in order of importance: the increasing contribution of the State to the financing of redundant wage-earners out of public funds (the Wage Supplementation Fund, the CIG) and of early retirement – mainly from large enterprises; investment subsidies; lastly, the reduction in employers' social security contributions. It is also possible, however, that some of the positive results achieved by industry were attributable to, or indirectly encouraged by, the general thrust of macroeconomic policy. True, the latter was not specifically designed to achieve these aims, but it did at certain times have indirect effects which contributed to the productive system's good performance.

The macroeconomic environment

The role of exchange rates

During the second half of the 70's, the depreciation of the lira allowed exporters to maintain their international competitive position despite the very steep increase in labour costs (Diagram 7, panel B). There were able to adapt their selling prices to changes in their costs and so maintain or even improve profit margins. Stronger profits financed rationalisation and modernisation investment. After 1982, firmer exchange-rate policy, mainly aimed at reducing inflationary pressure, squeezed exporters' profit margins, relative export prices rising less quickly than relative unit labour costs. Above all, however, exchange-rate firmness obliged firms to hold their costs down and so encouraged restructuring – this was facilitated by the fact that the financial situation of firms was healthier at the beginning of the period and by the strengthening of foreign demand after 1982.

The role of interest rates

As examined more fully in Part I, the sheer size of the government deficit probably depressed private sector investment (see Diagram 2). However, a number of

Table 7. **Financial position of enterprises**

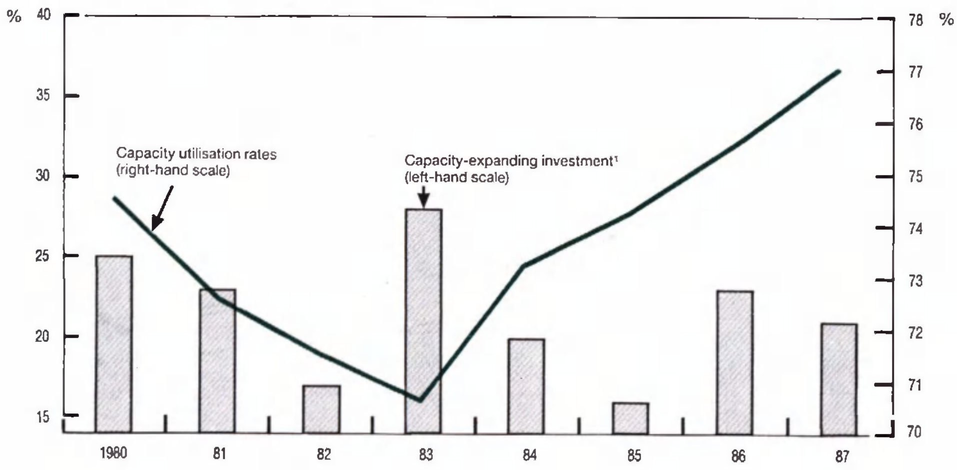
	1976-79	1980-81	1986-87
As a percentage of turnover			
Gross operating surplus			
Private enterprises	8.5	8.2	10.3
Public enterprises	9.3	6.0	12.1
Net financial costs			
Private enterprises	4.6	5.4	3.5
Public enterprises	9.6	8.7	6.2
Self-financing			
Private enterprises	5.0	3.8	7.4
Public enterprises	2.7	0.4	6.9
As a percentage of liabilities			
Short-term indebtedness			
Private enterprises	35.8	37.6	29.2
Public enterprises	36.1	38.4	30.2
Long-term indebtedness			
Private enterprises	13.8	15.1	12.0
Public enterprises	27.4	27.0	20.9

Source: Mediobanca, *Dati cumulativi di 1640 Società Italiane*, 1988.

factors mitigated the inevitable financial squeeze that enterprises suffered. First, monetary policy often remained accommodating as lending to the private sector was not reduced by the full amount of overruns in public sector targets. Second, credit controls were increasingly circumvented thanks to the development of new financial instruments and by foreign-currency borrowing. Lastly, and more recently, firms' access to the capital market was facilitated by the development of investment funds. The increase in the cost of credit in the 1980s had a stronger effect on capacity-enlarging investment than on rationalisation. It also had a decisive impact on corporate financial strategy, prompting firms to reduce their borrowing, manage their inventories more efficiently and substitute purchases of financial assets for real investment[27].

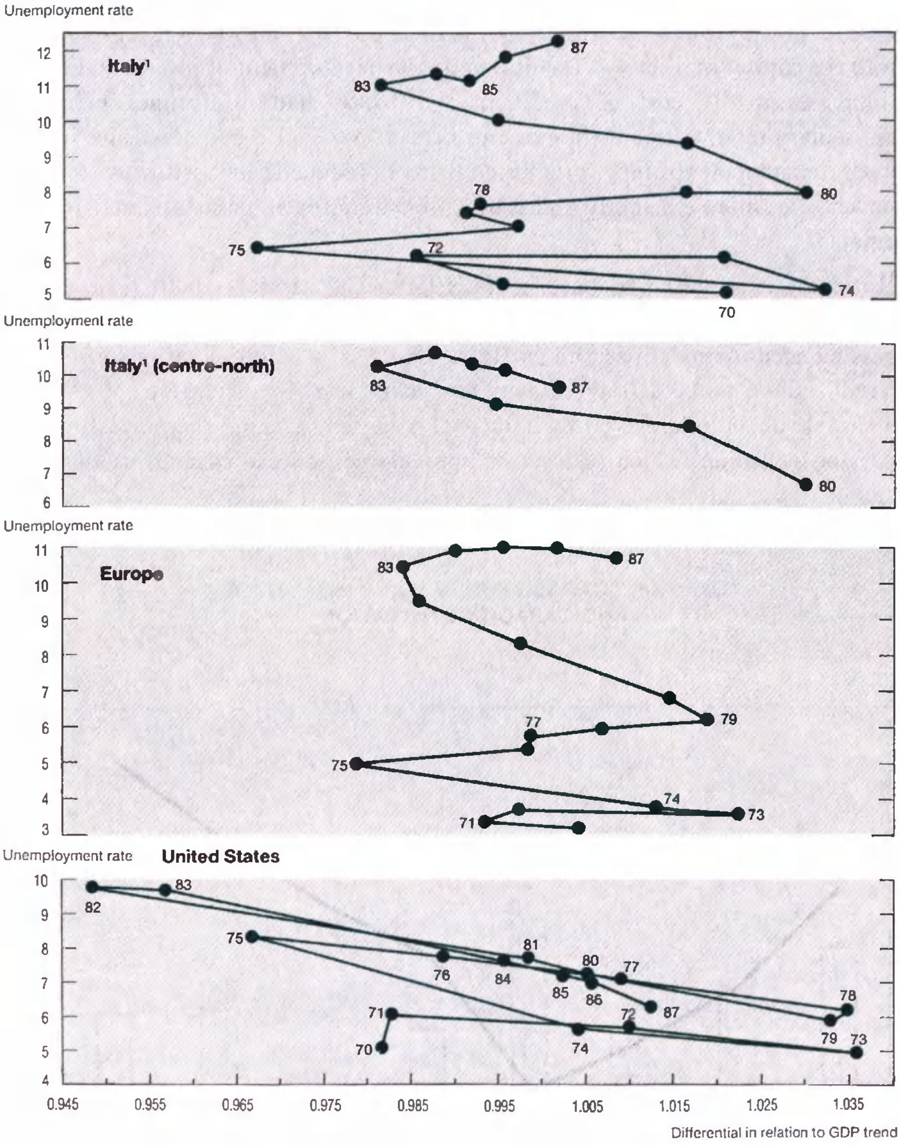
Rationalisation gathered pace in the 1980s. The capital/labour ratio (K/L) increased, despite the fall in the cost of labour relative to real interest rates, because of the pressing need to modernise and partly, no doubt, as a result of various incentives which reduced the final cost of investment for certain sectors and certain firms[28]. This is an example of the role played by industrial policy in masking the play of market forces. Modernisation, which resulted in appreciable gains in capital productivity,

Diagram 8. **CAPACITY-EXPANDING INVESTMENT AND CAPACITY UTILISATION**



1. As a percentage of total investment.
Source: ISCO.

Diagram 9. **UNEMPLOYMENT AND CAPACITY UTILISATION**
1970-1987



1. Unemployment includes CIG-enrolled employees.
Sources: OECD, ISTAT.

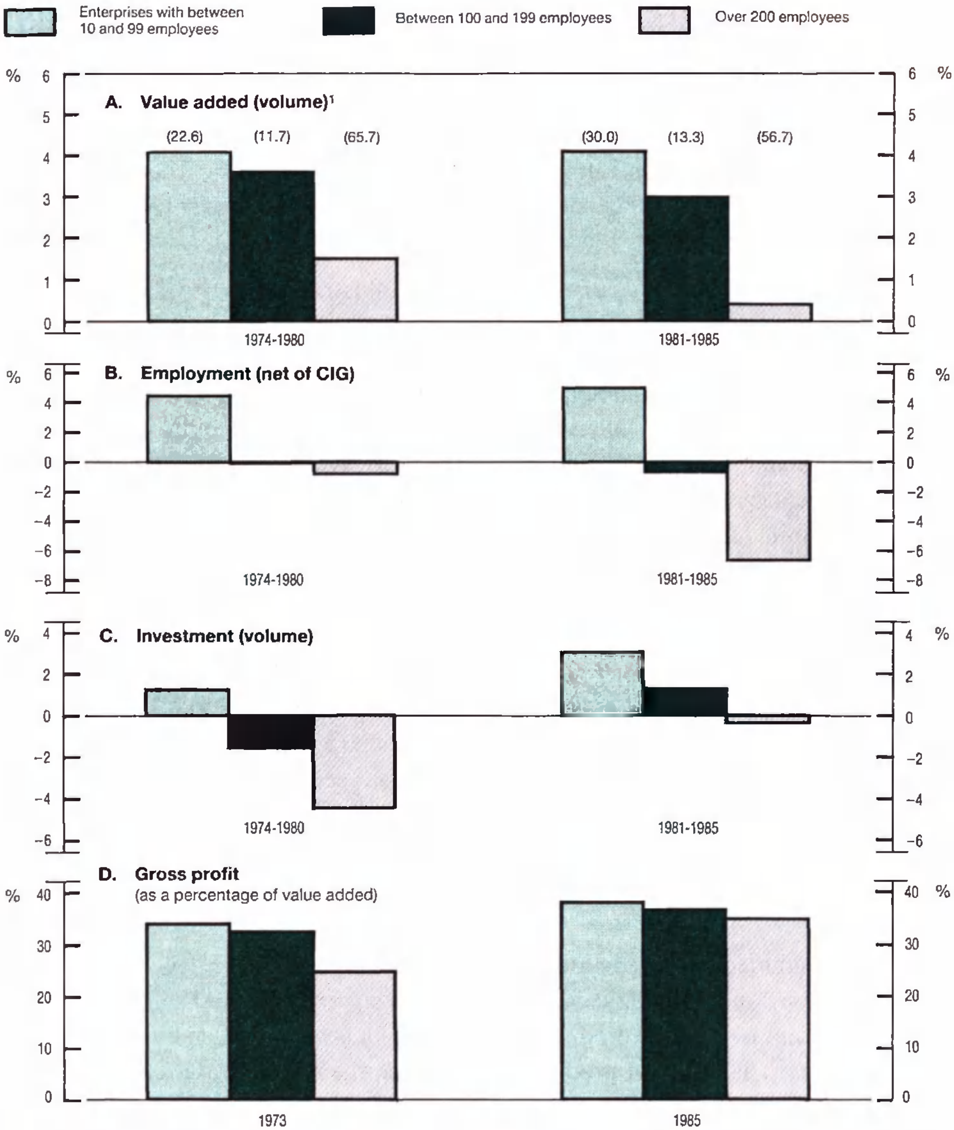
was carried out at the cost of capacity-enlarging investment, perhaps one area of inadequate industrial adjustment. According to the ISCO investment survey, the rate of growth of productive capacity in industry fell from an annual 4.6 per cent in 1970-74, to 2.2 per cent in 1974-80, and to 1.5 per cent in 1980-86. Capacity-enlarging investment, more than 60 per cent of total investment in industry in the early 1970s, had sunk to less than 30 per cent by the 1980s. Despite picking up slightly in 1986 and 1987, it still amounts to no more than 23 per cent (Diagram 8). At the same time, the capacity utilisation rate has been rising steadily since its 1983 low and, as in other major European countries, by mid-1988 exceeded the high reached during the previous expansion phase (1980). But in Italy's case it has also attained the all-time high reached in 1973.

The shift in the Okun curve (Diagram 9) illustrates the mismatch between production capacity and labour supply, a phenomenon clearly evident in Italy as well as in the other European countries. But since 1983, unemployment rates in the North and Centre of Italy and in the South have diverged. In the North and Centre region, the unemployment rate has fallen as capacity utilisation has increased. In the South, on the other hand, unemployment has continued to rise. The widening gap between the North-Centre region and the South also attests to poor regional labour mobility. Also, the strain on capacity varies according to the sector and bottlenecks are appearing despite increased flexibility – flexibility deriving from certain innovations, the development of sub-contracting and the increased number of hours worked. As the trade figures by sector show, developing products with a high technology content (computers, office automation, electronics, chemical and pharmaceutical products) are short of capacity. Shortages and inadequate capacity for the production of intermediate products have led to the relatively sharp increase in imports of such goods. By stark contrast, capacity in the traditional sectors (food industry, leather goods, artificial fibres) seems adequate[29].

The dynamism of small and medium-sized enterprises

Small and medium-sized enterprises (SMEs) bulk large in many sectors of the Italian economy and have played an active role in structural adjustment. The 1970s saw the segmentation of the production process, which was revealed by the 1971 and 1981 censuses[30]: as stages of production increased, the ratio of value added to gross output fell (Diagram A2 in Annex I). The average size of industrial enterprises thus diminished, sub-contracting developed in most sectors and particularly among enterprises with fewer than 100 employees: the medium-sized enterprises generally contracted out to small-sized enterprises. Also large and medium-sized enterprises

Diagram 10. **TRENDS IN INDUSTRIAL ACTIVITY BY SIZE OF ENTERPRISES**
Annual percentage change



1. The figures in brackets show the percentage share of enterprises in total value added.
Sources: ISTAT, *Censimento del industria*, 1981, *Indagine sul prodotto lordo*, 1985; Confindustria, *Risorsa piccola industria*, oct. 1987.

increasingly contracted-out services previously provided in-house. Major enterprises kept their co-ordinating role, while smaller units specialised in certain stages of production. However, this process seems to have come to a halt in the early 1980s, and the downward trend in the ratio of value added to gross output was reversed.

Gross profit margins are greater in firms with fewer than 200 employees than in larger ones, although the gap did narrow during the cyclical upswing (Diagram 10). Unit labour costs are 40 per cent higher in large enterprises than in SMEs[31], a differential partly due to the higher share of non-manual and managerial staff in large enterprises. However, hourly earnings of manual workers are also 50 per cent higher on average than in small firms. In large enterprises, the hours worked per employee are fewer and they are falling. Another aspect of the SMEs' dynamism is the particularly rapid growth of investment and, in particular, the relatively large share devoted to expanding productive capacity. By way of example, capacity-enlarging investment accounted in 1986-87 for some 40 per cent of total investment by firms with fewer than 100 employees, almost twice the average for all firms taken together. It is true that large enterprises enjoy greater production flexibility in their factories thanks to easier access to new technology, and this is reflected in high productivity growth. Also, they are much more active than SMEs in the takeovers of existing firms[32].

The microeconomic role of the State

Both directly and indirectly, the State plays a larger role in the economy in Italy than in the majority of other OECD countries. The following section analyses the microeconomic role that the State plays as an investor, a producer of public services and, lastly, an initiator of industrial policy.

The State's role as investor

In Italy the State plays a larger direct role in investment than in the other major European countries. Capital expenditure by general government accounted for 26 per cent of total investment in 1987, compared with less than 19 per cent in Germany, France and the United Kingdom. Its share in GDP continues to rise whereas it has been falling steadily in the other major European countries[33]. The share of investment by decentralised entities – local government and the social security system – in total *general government* capital expenditure has gradually increased, making public expenditure more difficult to control; in contrast, this share has been falling or has remained stable in the other three major European countries. When the *public sector in the broad sense* is taken into account – i.e. including posts and telecommunications, railways, market sector monopolies, municipal and provincial undertakings, the State electricity corporation (ENEL) – as well as *public and semi-public enterprises* in which the State has a stake ("partecipazioni statali"), total direct capital investment by the sector averaged 6½ per cent of GDP over the period 1980-87. The share of private investment in GDP fell during the recession of 1980-1983 while that of public investment rose, reflecting the countercyclical role assigned to it by the authorities. All told, in 1986-87 the public sector's share in gross fixed investment was 32 per cent, and even 45 per cent if housing is excluded, the highest ratio among the major OECD countries. The bulk of capital spending by the State goes to public services that are run on commercial lines, mainly to transport and communications, whereas in other European countries it is mostly channelled into housing (France and the United Kingdom) or social welfare (Germany). Infrastructure investment should help to improve the overall efficiency of Italy's economic system, but only if the quality of the services offered is maintained. In fact, the quality of many public services seems to be well below that in most other OECD countries (see below).

The public sector's role as investor is further amplified by large financial contributions by the State to nationalised enterprises, decentralised entities and the social security system, which go unrecorded in the national accounts[34]. These

Table 8. **Public investment in Italy**[1]

As a percentage of GDP

	1980-81	1982-83	1984-85	1986	1987
Direct investment expenditure					
Public sector broadly defined	4.3	5.0	5.0	5.1	5.0
of which: Government	3.4	3.7	3.7	3.6	3.5
Public sector enterprises	1.4	1.5	1.5	1.5	1.4
Total	5.7	6.5	6.5	6.6	6.4
Other indicators					
Government capital account transfers	1.1	1.4	1.7	1.6	1.6
Financial contributions of the "Settore Statale"	2.2	2.8	2.0	1.6	1.3
Memorandum item:					
Gross fixed capital formation	24.1	21.8	21.2	20.0	19.9
Excluding housing	17.3	15.2	14.9	14.3	14.7

1. See Table A4 in Annex I for a definition of the different component entities of the public sector.
Sources: ISTAT and *Relazione generale sulla situazione economica del paese*.

contributions consist of operating transfers and equity funding. They may be partly regarded as non-recoverable transfers to the public productive system to allow it to finance its investment. They also serve to cover the deficits resulting from current operating losses. Given their disparate nature and the differences in the way they are defined, they cannot be simply added to the capital expenditures by the public sector. Nonetheless, the recent fall in these flows is significant (Table 8): they declined from 2.8 per cent of GDP in 1983 to 1.6 per cent of GDP in 1986. This drop largely reflects higher operating profits (or smaller operating losses) of the major public enterprises. The State thus seems to be acting less as a "banker", operating instead *via* direct capital expenditure, which makes expenditure more transparent and highlights the permanent nature of certain transactions that was hidden in the past.

Inadequate public services

Bearing in mind the large amount of public investment in transport and communications, the productivity and quality of these services is inadequate, putting Italian enterprises at a disadvantage relative to their foreign competitors[35]. From the standpoint of reducing the public deficit, it is important that the public services should show a profit; usually, however, they have to meet social or political, as well as purely economic, objectives. The prices of the postal, rail and local transport services, for instance, are all set with an eye on social objectives.

Although it has improved slightly in recent years, the quality of the *postal service* in Italy is still below that in several other European countries: in 1985 it took three and a half days to send a letter from one town to another, compared with two days in the other major European countries (Table 9). The fact that the post goes via the often-unreliable public transport system certainly helps to slow down the delivery of mail. The postal service's operating deficit fell only very slightly between 1982 and 1987. Its workforce increased by nearly 30 per cent between 1980 and 1985 (to 240 000) while the volume of its business (measured in terms of the number of operations performed) increased by only 15 per cent. Investment in mechanisation and automation also increased by 4 per cent a year in volume. When output is measured on the basis of costs or prices, and labour input by hours actually worked, productivity is also seen to have declined in the 1980s. Compensation per employee increased by 16 per cent in real terms from 1983 to 1987. At the same time, the basic number of hours worked per employee fell, overtime pay rose and the number of auxiliary staff increased. The growth in private courier firms that offer businesses faster services is indicative of the poor quality of the public service.

Table 9. **Measuring the efficiency of some public services**

A. Postal service – Time taken (in days) to send a letter between:

	1983	1985		From Rome	To Rome
2 regional capitals	4.4	3.6	Rome and North (1985)	4.6	6.0
2 medium-sized towns	12.0	9.0	Rome and South (1985)	6.7	9.3

B. Railways - Productivity and profitability (1984)

	Italy	Germany	France	United Kingdom	Nether-lands	Spain	Sweden
Km travelled per employee	258	351	506	300	459	383	740
Employees per Km of network	13	10	7	10	9	5	3
Revenue as % of total cost	19	59	56	57	49	..	83

C. Local public transport – Profitability in selected European cities: revenue as % of total cost (1984):

Rome	15.8	Marseille	37.0
Milan	24.6	Vienna	45.0
Brussels	24.7	London	54.5
Paris	34.1	Hamburg	59.7

Sources: Panels A and C, Centro Studi Confindustria; *Stato ed Economia - Istituzioni, efficienza, sviluppo*, Edizioni del Sole 24 Ore, April 1988.
Panel B, Institut für Weltwirtschaft an der Universität Kiel, *Die Weltwirtschaft*, 1987, N° 1.

The telecommunications service also suffers from poor productivity, overmanning and inefficient equipment, so that the user pays more than in Italy's main competitor countries. In 1986 the UK Office of Telecommunications, which is responsible for supervising telecommunications activities in the United Kingdom, estimated that a basket of telecommunications services in Italy cost 28 per cent more than in the United Kingdom, 22 per cent more than in France and 14 per cent more than in Germany.

The Italian *railways* are another example of inefficiency. They have as many employees (214 000) as the French railways despite the fact the network is only half as long. The disparity with other European countries is equally marked. Likewise, productivity (passenger-kilometres and tonne-kilometres per employee) is lower in Italy than in most other European countries. Revenue covers only one-fifth of the railways' total costs, compared with over a half in the other major European countries. The main reason for the low profitability of the Italian railways is that their tariffs are held down for social and regional policy reasons. In return, the State subsidises the railways on a large scale (over 50 per cent more than in Germany, twice as much as in France and six times as much as in the United Kingdom). A medium-term restructuring plan currently under discussion aims to raise the efficiency of the Italian railways to a level comparable with that in the major European countries by 1993. The railways' operating conditions would be improved by cutting the number of employees and the length of the network (by 20 per cent and 15 per cent respectively). Also, tariffs would be liberalised so that they could reflect costs more accurately. At the same time, a major investment programme would be implemented to increase train speeds and so prevent a fall-off in demand.

Local public transport, which also has an important economic role to play in facilitating labour mobility, is equally inefficient. Inadequate investment for several years is partially responsible for this situation. The average age of vehicles has risen almost continuously since 1973; in 1985 nearly half of them were more than twelve years old and nearly 80 per cent more than ten years old. To achieve the age that the authorities consider acceptable in terms of safety and cost-effectiveness – a maximum of ten to twelve years – it would be necessary to replace as much as 75 per cent of all the vehicles. Furthermore, labour productivity has worsened and profitability is lower than in other world transport services in Europe, one of the main reasons being the fact that fares are kept artificially low (see Table 9 and the Technical Notes in Annex I).

Industrial policy

Growing government intervention

Since the beginning of the 1970s industrial policy has been guided by varying, and sometimes even ill-defined or contradictory, strategies. Nonetheless, some common features have characterised government action, especially since the first oil shock[36]:

i) The heavy weight of the public sector in traded activities, public enterprises serving as both an object of industrial policy and an instrument of macroeconomic policy;
ii) The large amount of direct state aid to industry, which has been rising steadily for the past fifteen years, accounting for 3 per cent of GDP in the mid-1980s;
iii) Extensive interventions of the State from the 1960s until the 1980s, to provide assistance to ailing enterprises by taking them over;

iv) Direct structural intervention, with the emphasis alternating between SMEs and major enterprises;

v) The growing role of social measures to accompany industrial adjustment;

vi) The exceptional scale of regional measures, especially to promote industrialisation in the South.

Industrial adjustment policy has often yielded disappointing results in the past. As elsewhere it may have created major distortions. While the effectiveness of some instruments of this policy is examined in detail below, a few broad generalisations do appear to stand out. Several measures have been used to maintain the level of employment rather than to improve the allocation of resources. Regional aid has not enabled the South to catch up with the North. The growth of subsidies and other forms of protection has distorted competition between enterprises and delayed certain necessary adjustments. In this connection, however, it should be pointed out that the widespread social unrest that preceded the first oil shock played a large part in the adoption of measures to minimise the social consequences of industrial adjustment. Lastly, the budget cost of industrial policy is still very high; certain types of expenditure will have to be reconsidered if the fiscal deficit is to be reduced. Since the beginning of the 1980s there has been a shift in favour of an industrial "development" or active policy which gives priority to sectors that are regarded as having a strategic role to play in the application of new technologies and in improving foreign trade performance. Other policies have sought to improve the working of markets. The modernisation of the financial system and the liberalisation of capital movements are both part of this approach. Privatisation should also make it possible to reduce the role of the State in the economy. However, compared with experience to date in other European countries, the process is still in its early stages.

It is difficult to make international comparisons of the amount of State aid to enterprises because the data are not strictly comparable. Direct subsidies represent only part, and sometimes only the smallest part, of State aid to enterprises. However, the rise in such subsidies as a percentage of GDP in most European countries may indicate growing State intervention in the process of structural adjustment. By contrast, the percentage is lower in Japan than in Europe and has been falling; in the United States it is negligible (Table 10). Secondly, there are extensive tax incentives to business investment: one of the most important tax expenditures in Italy arises from the fact that corporations can amortize for tax purposes all capital investment over four to five years. However the share of corporate taxes in total tax revenue is in line with the OECD average. To this form of aid one has to add equity funding, which depends on the importance of the role played by the public enterprises in industrial

Table 10. **Direct subsidies in some OECD countries**

As a percentage of GDP

	1965-73	1974-79	1980-84	1985	1986	1987
Italy	**1.9**	**2.7**	**2.9**	**2.8**	**3.0**	**2.6**
Germany	1.7	2.1	1.9	2.1	2.1	2.2
France	2.1	1.9	2.2	2.3	2.3	2.4
United Kingdom	1.8	2.9	2.3	2.0	1.6	1.4
OECD Europe[1]	1.8	2.4	2.5	2.4	2.4	2.3
United States	0.2	0.1	0.3	0.2	0.3	0.4
Canada	0.9	1.9	2.6	2.4	2.0	2.3
Japan	1.0	1.4	1.4	1.1	1.1	1.1

1. Average for 11 European countries, 1980 GDP weights.
Source: OECD, *National accounts.*

activity, specific aid for jobs as well as less visible forms of aid such as government procurement contracts and non-tariff barriers. According to an EEC study, from 1981 to 1984 Italy devoted a larger proportion of its GDP to aid to industry than any other major European country (5.4 per cent compared with 2.8 per cent in France and 2.3 per cent in Germany and the United Kingdom). On the other hand, government procurement contracts – often used to favour certain domestic industries – do not represent a larger share of GDP in Italy than in other EEC countries (estimated in 1984 at between 6 and 8.3 per cent, compared with 6.8 to 9.8 per cent on average in five European countries[37].

On the most detailed estimates available for Italy (CER-IRS), direct State aid to industry more than tripled between the beginning of the 1970s and the beginning of the 1980s (to 3¼ per cent of GDP in 1983-84) (Table 11). Despite a change in trend in 1982-83, the share of investment incentives (including those to promote technological innovation) in total aid was small compared with aid to ailing sectors and the social measures "accompanying" restructuring. In 1984, the main categories of expenditure were as follows:

i) Equity funding for undertakings in which the State has a stake ("partecipazione statale"), accounting for 28 per cent of transfers to industry;
ii) Expenditure on social measures – early retirement, the Wage Supplementation Fund (CIG), incentives to increase labour mobility – which, after rising steadily for a few years, constituted 24 per cent of total aid in 1984;

Table 11. **Transfers to industry, 1978-84**

	Composition as % of total	Trend as % of GDP		
	1984	1978-79	1980-82	1983-84
Funding for "partecipazioni statali"	28.3	0.43	0.80	1.08
Early retirement, CIG, mobility	24.5	0.13	0.34	0.76
Funds to rescue or assist crisis sectors	5.2	0.28	0.15	0.26
Mezzogiorno	21.8	0.67	0.73	0.72
of which: budgetisation	18.7	0.54	0.63	0.62
Promotion of GFCF and R & D	7.3	0.16	0.20	0.25
Exports	12.9	0.07	0.16	0.36
Total	**100.0**	**1.73**	**2.38**	**3.42**

Source: Centro Europa Ricerche (CER), Istituto per la Ricerca Sociale (IRS), *Quale Strategia per l'Industria* ? Il Mulino, 1986.

iii) Funds to put back on their feet, or to provide temporary assistance to, enterprises in difficulty (7 per cent of total aid);

iv) Aid to the Mezzogiorno, essentially in the form of reductions in social-insurance contributions for enterprises located there, still accounting for 24 per cent of total aid[38];

v) Export aid (interest-rate relief on export loans, and subsidies to the SACE (Export Credit Guarantee Scheme) for commercial and political risks), representing 12.7 per cent of total aid in 1984, a marked increase since 1978-79;

vi) On a more limited scale, but growing in importance, expenditure on measures to promote (or special tax allowances for) investment, research and innovation (over 7 per cent of total aid in 1984).

The policy of reducing labour costs

The policy of reducing labour costs, although not an integral part of industrial policy in the strict sense, has played a crucial role in industrial adjustment. The decline in corporate profitability at the beginning of the 1970s stemmed to a large degree from the wage increases won by the strikes of 1968-69. Major enterprises, which provided a quarter of all manufacturing jobs and which were already heavily in debt, were the most severely affected by the social unrest. In contrast, small enterprises were relatively unscathed. Several measures taken after the first oil shock were explicitly designed to cut labour costs. The Wage Supplementation Fund (the CIG) compensated, partly out of public funds, workers who had become redundant because their firms were in temporary difficulty or were undergoing restructuring, enabling enterprises to cut their labour force despite the extremely restrictive legislation on redundancies. Large enterprises, the most affected by stringent labour legislation, have been the major beneficiaries of this measure. It is estimated that 30 per cent of the job cuts in large enterprises from 1980 to 1985 were financed by such funds (CIG and early retirement scheme).

Non-wage costs in Italy are among the highest in the OECD countries. Reductions in social insurance contributions have been made on several occasions, the loss being covered out of general tax revenue. The aim of the reductions in 1977 and 1979 was to encourage employers to hire workers, particularly in the South (see the section on regional intervention below), or to improve the profitability and competitiveness of enterprises. In fact, the use of general tax revenue to reduce employers' social insurance contributions has continued virtually without break, and its scope has been extended. However, to increase government revenue the authorities have re-increased the rate of contributions in recent years, so that in 1986 social insurance contributions still accounted for 38 per cent of total gross wages in Italy compared with 40.7 per cent in France but 26 per cent on average in European countries.

Regional intervention

Regional aid to the South (Mezzogiorno) has perhaps been the most disappointing. The massive efforts made from 1965 to the first oil shock to promote investment in the region – with the obligation on all public sector entities to channel nearly half of their investment into the Mezzogiorno, financial assistance provided by the national banks on preferential terms to the major enterprises setting up there and so on – introduced major distortions in relative factor prices, giving investment a strong capital bias, a questionable choice for a region with a plentiful labour supply. Although a few investment projects were profitable, on average the investment in the Mezzogiorno showed a low return. Although the share of the Mezzogiorno in total manufacturing investment was 30 per cent between 1963 and 1973, compared with 17 per cent during the previous ten years, value added in the region still accounted for only 13 per cent of national value added and employment in the region for 18 per cent of industrial jobs. Furthermore, the large heavy-industry firms that had set up there proved to be particularly vulnerable when industrial relations worsened in 1969 and when the first oil shock struck.

After the first oil shock a change in attitude on the part of the authorities became gradually apparent. Measures to lower employers' social insurance contributions were extended from 1976 to offset previous distortions by cutting the labour costs of enterprises in the Mezzogiorno. The cost of these measures, which accounted for less than one-third of all the aid for promoting industrialisation in the South in 1970, increased to 70 per cent of total assistance by 1980 and over 78 per cent by 1984[39]. At the same time, small and medium-sized enterprises were given special financial assistance. According to census data, the number of industrial jobs in the South increased by 25 per cent between 1971 and 1981, mostly in small firms. However, although the gap between the Mezzogiorno and the North narrowed slightly, it remained very marked in terms of growth of value added and unemployment. Between 1970 and 1985 productivity per employee in industry rose less rapidly in the Mezzogiorno than in the North, and capital productivity also fell more rapidly. On account of the low productivity gains, and despite State aid, the Mezzogiorno remains at a relative disadvantage in terms of unit labour costs: in 1985, unit labour costs in industry (excluding construction) actually exceeded those in the North and the Centre.

As mentioned above, a large number of laws contain specific provisions designed to promote development in the Mezzogiorno. Recent measures have been added to the initial measures that are still in force, and sometimes conflict with them; for example, measures to reduce labour costs are implemented alongside investment incentives. The overall effect is not clear: employment incentives are automatic, and should operate more effectively than aid to investment, which first needs to be approved by special committees. However, their advantage over investment incentives is less clear cut when the current system is compared with the previous system and with that in force in the North-Centre[40]. In some cases, the measures are used for purposes other than those for which they were initially intended. The proliferation of measures makes it harder to monitor implementation. Furthermore, because there are so many different types of measures, neither taxpayers nor consumers nor entrepreneurs know what they really cost. Lastly, certain measures have been challenged by the Commission of the European Communities on the grounds that they do not comply with EEC rules.

Sectoral assistance

Distributed through many channels, sectoral assistance aims in principle to facilitate industrial adjustment and restructuring. The initial aim was to help firms cope with short-term difficulties by providing temporary assistance: preserving jobs was secondary. In practice, the preservation of jobs gradually became the main objective. The example of the GEPI, one of the main instruments of sectoral assistance, shows clearly the distortion that has taken place[41]. Set up at the start of the 1970s, it was responsible for putting ailing enterprises back onto a sound financial footing to allow them to regain their market position. In practice, when this proved impossible, the GEPI kept them going artificially, before being authorised to start up companies to employ the workers that had been laid off. The frequency and the scale of its intervention overstretched its resources, and intervention had to be limited to priority regions, in particular the Mezzogiorno. Recently, better economic conditions has reduced the GEPI's losses and made it possible to return some enterprises to private control (twelve companies employing 33 000 people in 1986, nineteen companies employing 2 400 people in 1987). The Prodi Act, passed in 1979, provided "extraordinary assistance to major enterprises in serious difficulty", and complemented the GEPI. Its initial purpose was to prevent firms from going out of business. When this proved impossible, some of the firms' viable plants were sold off and their other activities were wound up. Here again, as in the case of several GEPI's operations, the Wage Supplementation Fund was the main instrument used to facilitate the closures.

Sectoral assistance also helped small and large enterprises in various branches: textiles, shipbuilding, iron and steel, electronics. In most cases it involved the State taking a stake in an ailing enterprise, but it also took the form of ordinary or subsidised loans for the purchase of capital goods, allocated on an automatic basis. The shortcomings of this type of assistance became clear at the beginning of the 1980s: a lack of rigorous selection criteria, the extension of assistance to firms that were no longer viable, deviations from initial objectives. Several amendments have been made to the system, but despite better economic conditions sectoral assistance continues to absorb a large share of State funds.

The promotion of innovation

Various indicators suggest that, technologically, Italy lags behind other major OECD countries, and that it spends relatively little on R&D. Since the beginning of the 1980s the Government has become more active in this area, allowing some of the ground to be made up (Table 12). The proportion of GDP devoted to R&D has risen by 30 per cent, but it is still below that of the major industrialised countries. The share of public funds in the financing of R&D carried out in industry virtually tripled from 1981 to 1986, and is now close to the average (excluding Japan). The main instruments for promoting technological innovation are: *The IMI Fund for Applied Research*, which comes under the Ministry for Scientific Research, whose responsibilities were broadened by Law 46 of 1982; *The Fund for Technological Innovation*, set up at the same time, which comes under the Ministry of Industry; low-interest loans for the purchase of machinery with a high technological content by small and

Table 12. **R & D expenditure and the diffusion of technology**

A. Resources devoted to R & D

	Total expenditure as a percentage of GDP		Expenditure in industry as a percentage of total		Percentage of expenditure in industry financed by the State	
	1981	1987[1]	1981	1987[1]	1981	1987[1]
Italy	**1.0**	**1.3**	**56**	**61**	**9**	**25**
Germany	2.5	2.7	70	73	17	14
France	2.0	2.3	59	58	25	23
United Kingdom	2.4	2.4	62	67	30	25
United States	2.5	2.8	70	71	32	35
Canada	1.2	1.3	49	51	11	12
Japan	2.3	2.8	61	67	2	2
OECD Average	2.0	1.9	61	64	20	19

1. 1986 for France, the United Kingdom and Japan.

B. Selected indicators of technology diffusion

	Italy	Germany	France	United Kingdom	United States	Japan
Numerically controlled machine tools as percentage of total machine tool stock						
1981	**2.2**	2.2(1980)	1.9	3.2(1982)	4.7(1983)	2.9
Machine tools per 10 000 employees in fabricated metals industry						
1981	**90**	93	79	87	119	58
Installed industrial robots per 10 000 employees						
1982	**14**	19	8	9	19	120
1984	**33**	35	27	26	28(1983)	239
Percentage of office workers with a computer workstation						
1986	**4**	8	7	11	30	..
Business demand for IT as a percentage of GFCF						
1984	**8.8**	11.6	9.0	15.0	14.6	6.9
1987	**10.6**	13.6	9.7	16.7	18.1	8.3

Source: Panel A: OECD, *Main Science and Technology Indicators*, 1988.
Panel B: OECD, *Science and Technology Policy Outlook*, 1988.

medium-sized enterprises, introduced by an Act of 1983 supplementing an earlier Act (Sabatini Act of 1977).

The growth in the activities of the IMI Fund has made it possible to increase the number and scale of the measures to support applied research[42]. Most of the beneficiaries are major enterprises in good economic and financial health, and which have been recently modernised. It is estimated that patents were filed on over half of the projects financed up to 1984. The Fund for Technological Innovation finances up to 70 per cent of programmes for the introduction of new technologies in four priority sectors – motor vehicles (and sub-contractors), aviation, electronics and fine chemicals – and helps to finance capacity reductions in the iron and steel industry. Enterprises have found the Fund for Technological Innovation easier to use than the IMI Fund; also, it distributes aid faster than other similar bodies[43]. 20 per cent of the Fund's annual appropriations was set aside for small and medium-sized enterprises; the number of SMEs applying to the Fund rose gradually, and the full appropriation was taken up in 1986. By then, nearly 40 per cent of the aid went to the electronics sector, while the share of aid to the motor vehicles sector had been gradually falling. However, this trend cannot be interpreted as constituting a shift to a sector with a greater high-technology content since the term "electronics" embraces industrial automation systems in sectors as diverse as chemical engineering, textiles, clothing and footwear.

In addition to the assistance provided to firms that manufacture products with a high-tech content, another measure was introduced to strengthen the effective demand for these products – the Act of 1983 for small and medium-sized enterprises, which makes available non-recoverable grants for the subsidised purchase of machinery with a high-technology content[44]. However, experience has shown that the previous measure (Sabatini Act of 1977), whose initial aim was to provide short-term support for demand and not to promote technological diffusion, was still a highly effective investment incentive, since it allowed the seller to lower the price of his machinery and the purchaser to delay payment for it; furthermore, it was less costly than the Act of 1983. It would seem that, in making a decision to purchase equipment, small enterprises are more readily influenced by the "liquidity" factor than by the subsidies available. However, in some cases, subsidies have proved useful in helping small enterprises to overcome the difficulties involved in introducing automation. The existence of two, sometimes duplicable, instruments – one of which performs a role for which it was not intended – no doubt entails a loss of efficiency. If the scope of each Act were clarified, it would probably be possible to attain policy aims more effectively and at a lower net cost.

Among the most frequent criticisms of the policy for promoting innovation during the 1980s are the lack of co-ordination between the bodies that allocate the aid, and the fact that instruments are not sufficiently differentiated. The scope and the priorities of each of the two above-mentioned Funds – which come under two separate Ministries – would need to be defined more clearly so that they complement instead of duplicating each other. Second, while it seems desirable to increase the resources available for this type of more directly "positive" action, any increase should be offset by a reduction in some types of "defensive" expenditure. Similarly, it would be possible to reduce the State's participation (from 70 to 50 per cent for example) in the programmes approved by the Fund for Technological Innovation – which functions fairly satisfactorily – thereby allowing it to intervene more frequently without increasing its resources excessively. This would have the added advantage of increasing the share of private venture capital in the programmes.

Privatisation

The privatisation of industrial enterprises has two aims: to reduce the public debt, and to strengthen market mechanisms and so make enterprises more efficient. It is to the extent that it aims to make enterprises more efficient that privatisation can be regarded as being an integral part of industrial adjustment. The process of denationalisation has not gone as far in Italy as in France or the United Kingdom. One of the reasons for this is perhaps the ambiguous nature of the objectives that have been set for public enterprises. In principle, public enterprises served to channel capital to the productive system whenever private capital was lacking. In practice, they have often been used to curb the impact of market forces in accordance with the various and often conflicting objectives of macroeconomic and industrial policy: the preservation of jobs, promoting development in the Mezzogiorno and, more recently, reducing Italy's external dependence, the provision of incentives to key sectors in order to promote innovation.

Despite the difficulties encountered in achieving a consensus on the enterprises that should be denationalised, and on how it should be done, there have been some examples of privatisation in recent years. For instance, from 1983 to 1985, the IRI sold off 20 enterprises and acquired only one; in contrast, over the period of 1971-80, it had sold off 18 but acquired 55. In 1986 the Alfa-Romeo Group was sold to the Fiat Group. Together with the sales by other public agencies, over the period 1983-86 nearly 40 public enterprises were sold off[45]. As a result of these privatisations the State has completely withdrawn from certain sectors. In addition, between 1983 and 1986 the IRI sold off a dozen minority shareholdings in enterprises – more than half of which were in the industrial sector. But enterprises can be sold off only when they are sufficiently profitable to attract private investors. The withdrawal of the State can take a third form: public and private enterprises set up joint ventures to operate in an international context or in advanced sectors. There have been a few examples of this type of collaboration. Insofar as it modifies the way in which an enterprise is managed, partial or total privatisation may have been a means of making the enterprise more efficient.

A competition bill is currently before Parliament. No such legislation previously existed in Italy; when passed, it should make it possible to help limit the dangers of an excessive degree of concentration in some industries. At the same time, various types of barriers to international trade continue to exist: customs procedures, technical standards and bilateral arrangements, which reduce foreign competition and may impede the modernisation of industry. It is always difficult to quantify the share of imports that are subject to non-tariff barriers. However, an EEC survey of business leaders conducted in 1987 showed that, compared with their counterparts in the other major European countries, in Italy they considered non-tariff barriers – especially administrative barriers, delays and charges at border crossings, and technical standards – to be relatively high[46]. Also, Italy has some of the tightest voluntary restraints on the imports of Japanese cars.

Conclusion

The industrial restructuring that has taken place in the past few years has made the production system more efficient: productivity gains have risen, external performance in manufactures trade has been maintained, unemployment has fallen in the North and Centre, the most industrialised regions, and small and medium-sized enterprises, which are the most exposed to competition, have been particularly dynamic. In contrast, the service sector, which is perhaps less sensitive to external market requirements seems to have lagged behind. Admittedly, real value added in trade and services has risen more rapidly than in industry (by 1½ percentage points per year on average), but productivity has fallen (an annual differential of 4 points with industry) and the annual rise in the output price deflator has been higher (by nearly 3 points). To an even greater extent, the productivity and quality of public services are clearly insufficient – especially given the large amount of State funds received, and compared with the situation in the other major OECD countries. The inadequacies of the public services penalise the entire system of production and distribution. Rationalisation and tighter control over expenditure, better selected investment projects and a greater emphasis in general on economic criteria in the management of public services, would improve the situation. In view of the forthcoming creation of a Single European Market in goods and services in 1992, the need for progress in this area is particularly urgent. By 1992, aid to industry will have to be reconsidered and the most protected industries will have to have made the necessary adjustments. By pushing ahead rapidly with the process of privatisation and by slanting policies more towards competition – among domestic producers as well as from abroad – there could be substantial gains (lower costs and prices) for the whole economy.

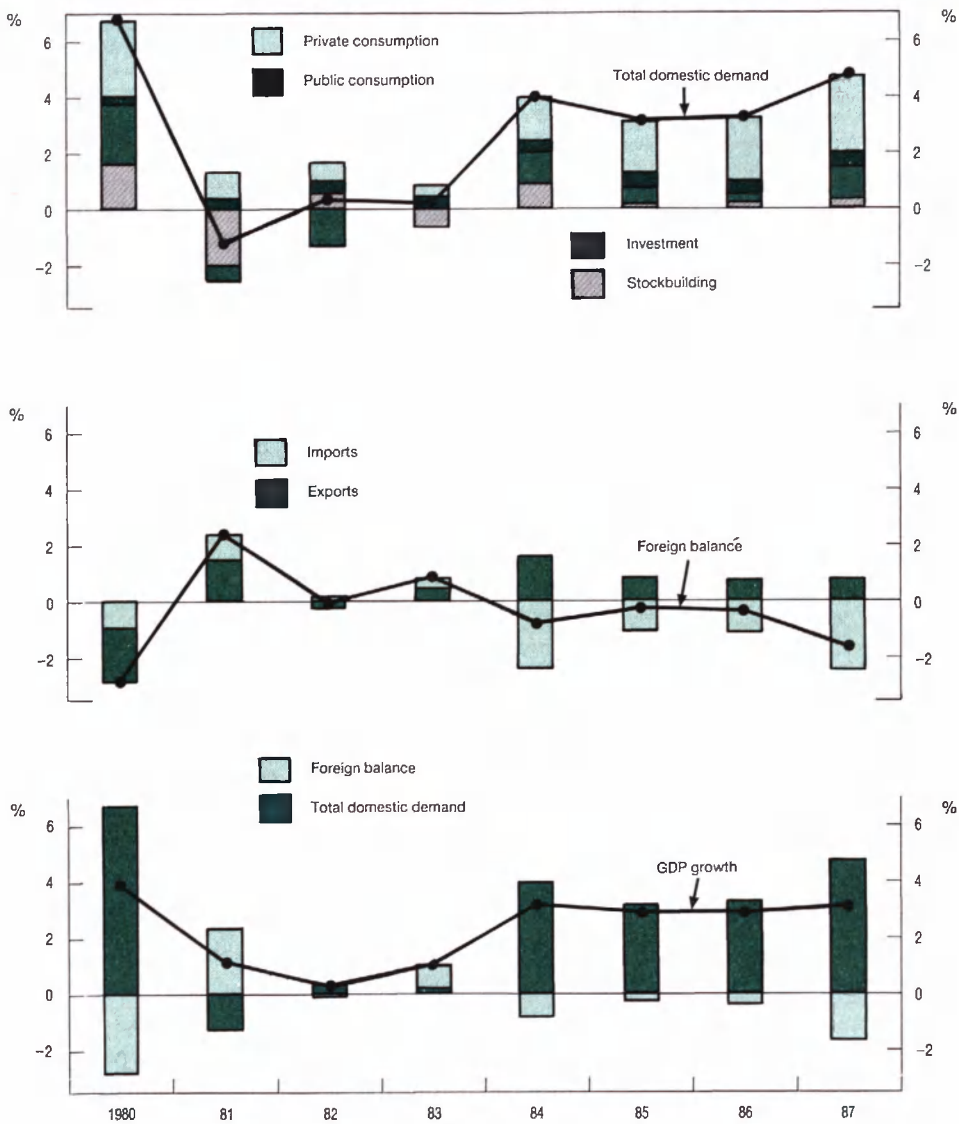
III. Recent developments

GDP, which grew by around 3 per cent in 1987 for the fourth year running, accelerated somewhat in 1988 to about 3.7 per cent, stabilizing the unemployment rate. Italy's growth over the period 1984-1988 has thus been somewhat above the average for OECD Europe. The rise in the consumer price index stabilized in the first half of 1988 at around its previous-year rate, interrupting a period of price deceleration which began in 1980. While the gap has narrowed considerably, the inflation rate in Italy still exceeded that in its trading partners by some 2.2 percentage points in 1988; wage costs also continued to rise faster. Growth was again driven by domestic demand, with real net exports falling. The current account balance, in surplus of 0.4 per cent of GDP in 1986, reflecting the fall in oil prices, has since moved slightly into deficit, despite buoyant export growth.

Strong growth of domestic demand

Total domestic demand grew by 4.7 per cent in real terms in 1987, against 3.2 per cent in the previous year. The acceleration in demand began mid-1986 and was led at first by investment and then by private consumption. In the first half of 1987, the growth in private consumption accelerated, leading to final domestic demand growth of 5.3 per cent year-on-year. Private consumption was fuelled by a steep rise in real wages and by the continuing decline in the saving ratio[47]. Compensation of employees rose by 3.9 per cent (in real terms) in 1987, largely as a result of public sector wage increases of 7.8 per cent in real terms (see below). The saving ratio fell by around 2 points in 1987 but still amounted to nearly 22 per cent of disposable income. Private consumption has from 1983 to 1988 been one of the most dynamic components of domestic demand, contributing two-thirds of GDP growth. During this period, private consumption grew faster than disposable income and the saving ratio fell by 3½ percentage points.

Diagram 11. **CONTRIBUTIONS TO GDP GROWTH**
As a percentage of GDP in the previous year



Source: OECD, *National Accounts.*

Table 13. **Demand and supply**

Percentage changes from previous period, seasonally adjusted at annual rates
Volume (1980 prices)

	Current prices 1985[1]	1988/1983	1986	1987	1988[3]	1987 II	1988 I	1988 II[3]
Demand and output								
Private consumption	510.0	3.4	3.5	4.3	4.1	2.5	5.1	3.7
Public consumption	135.8	2.9	3.1	3.4	2.2	3.0	1.5	2.8
Gross fixed investment	171.7	3.9	1.4	5.2	5.8	2.4	8.5	4.0
Machinery and equipment	81.7	7.5	2.0	11.5	7.5	4.1	10.4	5.3
Construction	90.0	0.3	0.7	−1.3	3.8	0.3	6.2	2.5
Final domestic demand	**817.4**	**3.4**	**3.0**	**4.4**	**4.2**	**2.5**	**5.3**	**3.6**
Stockbuilding[2]	13.5	0.3	0.5	0.7	−0.1	−0.5	−2.1	4.4
Total domestic demand	**830.9**	**3.8**	**3.2**	**4.6**	**4.0**	**2.0**	**3.1**	**7.9**
Exports of goods and services	169.0	4.8	3.4	3.6	6.6	10.6	7.9	0.4
Imports of goods and services	184.3	7.4	4.7	10.0	7.5	5.1	5.5	14.0
Foreign balance[2]	−15.3	−1.0	−0.7	−3.3	−1.0	1.0	0.3	−3.5
GDP at market prices	**815.6**	**3.2**	**2.9**	**3.1**	**3.7**	**3.1**	**3.6**	**4.6**
Industrial production	–	3.1	2.7	4.0	4.5	-0.5	8.2	2.2
Prices	–							
GDP price deflator	–	7.6	7.5	5.6	4.8	5.9	4.6	4.0
Consumer prices	–	7.3	5.9	4.8	4.9	6.3	4.6	4.4
Breakdown of GDP								
Agriculture	36.6	0.1[4]	2.3	1.3		0.5	1.0	
Industry total	281.2	2.4[4]	2.7	3.0		3.2	4.9	
Manufacturing	195.3	3.5[4]	3.3	4.3		3.6	5.6	
Energy	37.2	1.8[4]	4.3	1.5		4.2	−1.4	
Construction	48.7	−2.2[4]	−1.0	−2.2		0.7	5.5	
Services	384.0	4.2[4]	3.4	3.7		2.9	2.9	

1. Thousand billion lire.
2. Changes expressed as a percentage of GDP in the previous period.
3. OECD Secretariat estimates.
4. 1987/1983.

Sources: ISTAT, *Quarterly National Accounts*; *Relazione generale sulla situazione economica del paese*, 1988; OECD Secretariat.

The Bank of Italy has recalculated movements in households' average propensity to consume out of total disposable income adjusted by two factors: first, the effect of inflation on the real value of financial assets, and second, the effect of the fines under the amnesty on unauthorised building (assumed to have been paid from savings). Thus adjusted, the propensity to consume was estimated to be virtually flat between 1984 and 1986 whereas on a non-adjusted income basis, it would have risen

Table 14. **Households' appropriation account**

Percentage changes from previous year

	1985 Lire thousand billion	1988/1983	1984	1985	1986	1987	1988[2]
Compensation of employees	379.4	9.6	11.9	12.2	8.1	8.9	7.2
Income from property and other income	350.4	10.8	14.9	9.7	11.5	8.4	9.5
Current transfers received	148.1	10.4	10.2	15.2	9.8	6.8	10.0
Total income	877.9	10.2	12.8	11.7	9.8	8.3	8.6
Less: Direct taxes	87.2	11.7	11.2	12.1	10.8	10.4	14.2
Current transfers paid	124.9	10.3	9.7	11.7	12.6	9.5	8.0
Disposable income	**665.9**	**10.0**	**13.7**	**11.6**	**9.1**	**7.9**	**8.0**
Private consumption	504.9	11.0	13.8	12.3	9.5	10.6	8.9
Saving ratio[1]	–		**24.6**	**24.2**	**23.9**	**21.9**	**21.3**
Real disposable income	–	2.5	1.8	2.2	3.0	2.9	2.9

1. As a percentage of disposable income.
2. OECD Secretariat estimates.
Sources: ISCO and OECD Secretariat estimates.

by around 3 percentage points[48]. By contrast, the propensity to consume on both bases increased significantly in 1987, despite an acceleration in real disposable income. The Bank of Italy also estimated that in 1987, despite the end-of-year capital losses, the value of households' financial assets, excluding stocks, rose twice as fast as disposable income. The differential narrows if shares are taken into account, but is nonetheless still positive.

Household consumption continued to grow strongly in 1988. On the quarterly national accounts basis, private consumption rose by an annual rate of 5 per cent in the first half. Other indicators and surveys suggest that this growth was sustained in the second half, so that over the year, its growth could be close to 4 per cent. Since 1984, consumer durables (particularly cars) have been the most buoyant component of demand (real growth of household purchases of vehicles of all kinds averaged 7.8 per cent over the period 1984-87). Despite a stabilisation in the second quarter of 1988, domestic car sales rose by 8.9 per cent in the first 10 months of 1988 over the same period of the previous year.

Investment rose 5.2 per cent in real terms in 1987, accounting for one-quarter of GDP growth[49]. Growth in fixed investment came entirely from investment in machinery and equipment, which rose by 12.1 per cent in real terms. Total construction fell 1.3 per cent as residential investment declined for the third year

Table 15. **Gross fixed capital formation by sector and product**
Percentage changes, at constant 1980 prices

	1982	1983	1984	1985	1986	1987
Total	**–5.7**	**–1.6**	**4.4**	**3.3**	**1.4**	**5.2**
By sector						
Agriculture	–2.4	3.9	–1.2	–6.7	–2.0	
Industry	–7.0	1.1	8.3	3.9	3.5	
Traded services	–4.8	–2.9	2.5	3.1	0.4	
Transport and communication	–7.7	–2.8	10.7	4.0	–0.8	
Trade, credit, insurance, rental and other services	–4.1	–3.0	0.6	2.9	0.7	
Non-traded services	–11.3	–9.6	9.2	15.2	0.8	
By product						
Construction	–6.6	1.1	0.0	–0.6	–0.7	–1.3
Housing	–5.0	4.1	0.8	–1.9	–1.7	–3.6
Other	–8.5	–2.4	–1.0	1.2	3.8	1.4
Machinery and equipment	–5.5	1.4	12.6	5.3	2.9	12.1
Means of transport	–1.9	–11.8	6.0	7.2	–1.6	8.4

Source: *Relazione generale sulla situazione economica del paese*, 1988.

running, probably because of high real interest rates. By 1987, investment in residential building had fallen 7 per cent below its 1984 level. Overall, economic conditions were particularly conducive to investment in 1987 with capacity utilisation continuing to rise (Diagram 16). Profits continued to grow in 1987 and the trend remained favourable in 1988. Much investment in machinery and equipment aims at modernisation: in 1987 investment in computer hardware and precision tools rose by 21.7 per cent in real terms and in electrical and electronic equipment by 14.3 per cent. The pick-up of non-residential construction, averaging 2.5 per cent over the two years 1986 and 1987, reflects a greater emphasis on the expansion of productive capacity.

Investment in machinery and equipment rose by 8.5 per cent in the first half of 1988, with equipment investment accounting for 12.5 per cent of GDP (at 1980 prices), roughly 1 percentage point more than at the end of the previous cycle in 1980. But, as elsewhere, the nominal ratio declined from 11.5 per cent of GDP in 1981 to 10 per cent at the beginning of 1988, as the deflator for capital goods rose much less than the GDP deflator. Despite the steep rise in investment in the productive sector, the rate of capacity utilisation steadily increased from 1983 onwards, averaging 77.5 per cent for industry as a whole in the first half of 1988, slightly above the rate at the peak of the previous cycle and equivalent to that registered in 1973[50].

Inventory accumulation added 0.5 of a percentage point to GDP growth in 1987[51]. Stocks of raw materials rose, while inventories of finished products were drawn down as a result of brisk final demand. In the first half of 1988, inventory investment appears to have had a strong negative influence on growth; but it is quite possible that this change in stockbuilding, as estimated in the provisional quarterly national accounts, embodies a large part of statistical adjustment.

Although total domestic demand growth in 1987 was 1½ percentage points higher than in the previous year, the acceleration of GDP growth was more moderate. The fall in real net exports – mainly the result of the strength of imports – was largely due to faster total domestic demand growth in Italy than elsewhere in Europe. Growth of manufacturing value added was 4.3 per cent, making it the most dynamic component of GDP. The industrial share in GDP expanded in 1987 for the first time since 1981, primarily as a result of buoyant household demand: by contrast, much of the heavy demand for capital goods was met by imports. In the first half of 1988, value added in manufacturing rose at an annual rate of 5.6 per cent from the previous half year. The index of manufacturing output rose by 4.4 per cent in the first 8 months of 1988 compared with the same period in 1987[52].

Continued high unemployment

Although GDP grew slightly faster in 1987 than in 1986 and 1985, the rate of increase of total employment slowed to 0.4 per cent and the number of salary earners increased by 0.2 per cent[53]. As a result, the unemployment rate rose by almost 1 per cent of the labour force. This reflected a sharp slowing of the rate of dependent employment creation in the traded services sector which fell to 1.3 per cent, compared with an average of 3.7 per cent during the three previous years. The slower pace of decentralisation of productive services may have played a part in this development. In manufacturing, employment continued to decline (by 0.8 per cent) and productivity picked up (increasing by 5.1 per cent in 1987 against 4.5 per cent a year earlier) reflecting not only continued restructuring since the early 1980s, but also a partly cyclical expansion in working hours.

The rate of unemployment rose again in 1987 but it fell in the first half of 1988 to 12.1 per cent of the labour force[54]. However, this trend masks sizeable differences according to regions and age groups. The unemployment rate has actually declined since 1985 in the North and Centre regions, whereas in the South (Mezzogiorno) it continues to climb. In the North and Centre, there is virtually no unemployment among prime-age males (25 to 59-year olds), though in the South, unemployment in

Table 16. **Employment and the labour market**

A. Trend of employment measured in labour units

Labour units and percentage changes

	1984 thousands	1985/1984	1986/1985	1987/1986
Total employment	22 412.9	0.8	0.9	0.4
Dependent employment	15 188.0	1.3	0.5	0.2
Agriculture	792.4	–1.0	–2.5	–1.5
Industry	5 698.8	–1.5	–1.3	–1.0
Manufacturing	4 343.2	–1.4	–1.2	–0.8
Private services	4 737.4	4.6	2.1	1.3
General government	3 959.4	2.0	1.2	0.9
Self-employed	7 224.9	–0.3	1.9	0.7
of which: Industry	1 305.8	–0.5	2.1	–1.9

Source: *Relazione generale sulla situazione economica del paese*, 1988.

B. Labour market indicators

Thousand persons and percentage changes from same period of previous year

	1984 thousands	1985/1984	1986/1985	1987/1986	1987 I	1987 II	1988 I
Labour force	22 905.3	0.9	1.5	0.9	0.9	0.8	0.8
Total employment	20 647.5	0.4	0.6	–0.1	0.1	–0.3	0.3
Dependent employment	14 477.8	1.2	0.4	0	–0.3	0.3	0.4
Agriculture	872.8	–1.9	–3.4	–4.0	–4.8	–3.2	–4.6
Industry	5 885.5	–2.3	–1.6	–1.6	–2.7	–0.5	–0.8
Other	7 719.5	4.2	2.2	1.6	1.8	1.3	1.7
Self-employed	6 169.8	–1.4	1.1	–0.4	0.9	–1.7	0
Enrolled at the CIG							
Total	475.1	–11.7	–12.0	–14.6			
Manufacturing	436.0	–14.9	–9.3	–19.6			

	1984	1985	1986	1987	1987 I	1987 II	1988 I
Unemployment rate[1]	**9.9**	**10.3**	**11.1**	**12.0**	**11.6**	**12.3**	**12.1**
Including the CIG	11.9	12.1	12.7	13.3			
Youth unemployment[2]	32.9	33.9	34.5	35.5			
Long duration unemployment[3]	50.0	56.4	48.2	49.0			

1. As a percentage of labour force, seasonally adjusted.
2. Aged 14 to 24, as a percentage of youth labour force.
3. Unemployed seeking a job for 1 year and over as a percentage of total unemployment.

Sources: ISCO, *Rapporto semestrale*; ISTAT, *Rilevazione delle forze del lavoro*.

Table 17. **Regional indicators of unemployment in 1987**

As a percentage of the labour force

	Total Italy	North-Centre	South
Unemployment rate			
Total	12.0	8.4	19.2
Men	8.1	5.2	13.6
Women	18.7	13.5	30.7
14 to 25s, total	35.6	26.3	53.1
Men	29.8	20.1	45.1
Women	42.2	32.2	63.6
26 to 59s, total	7.0	4.7	11.4
Men	4.4	3.0	7.8
Women	11.9	8.3	20.6

Source: ISTAT, *Rilevazione delle forze di lavoro*, 1987.

this same group was running at 7.8 per cent of the labour force in 1987 (Table 17). In the case of the most unemployment-prone groups (women and young people), the divide between North-Centre and South is even greater. This regional imbalance has important economic implications. Since sectoral wage agreements are centrally negotiated and labour mobility is low, wage pressure in the North spreads throughout the economy which makes employment prospects in the South still worse[55].

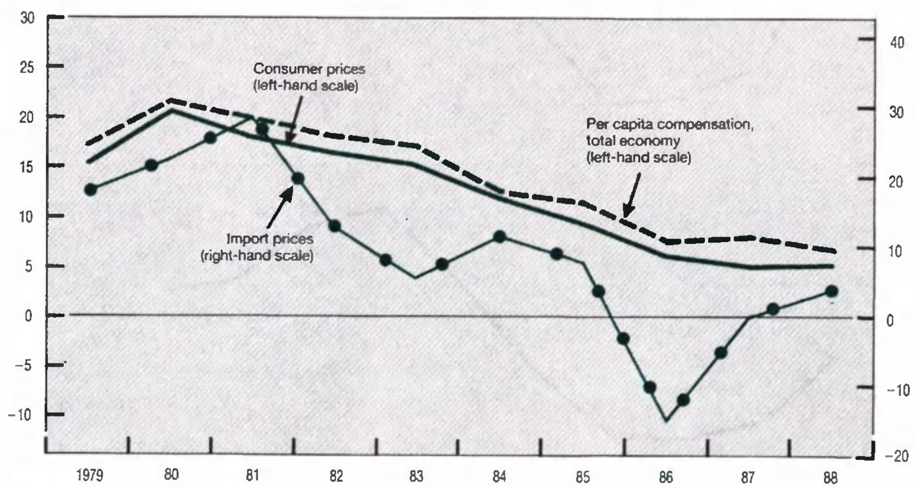
Long-duration unemployment (one year and over), though decreasing since 1986, still amounted to close to 50 per cent of total unemployment in 1987, one of the highest rates in the OECD area. Youth unemployment (those aged between 14 and 24) continued to increase in recent years while it has fallen in most OECD countries (Table 16). The unemployment rate for youth reached 35.5 per cent of the total youth labour force in 1987, compared to 15 per cent on average for twelve main OECD countries. In the last few years, an increasing share of public expenditure on labour market programmes has been directed at youth. Such measures amounted to 29 per cent of labour-market expenditure in 1987 (equivalent to 0.37 per cent of GDP), against 21 per cent in 1985. The number of employment training contracts rose from 103 000 in 1985 to 400 000 in 1987. These were granted in small industrial enterprises mainly in the North and Centre. They have been attractive to employers because they both reduce social security contributions and ease hiring procedures. For instance, it allowed fixed-term contracts and personalised hiring rather than the traditional system of hiring jobseekers in the order in which they appear on a list (collocamento) drawn according to various criteria: duration of unemployment, other incomes in the family, etc. Various other training schemes, financed by regions and the European Social Fund, have been designed. In addition, more specific youth measures were introduced, such as support of young people starting enterprises in the Mezzogiorno, projects to restore cultural assets, employment incentives for long-term unemployed youth. The extension in recent years of part-time contracts (140 000 such contracts were granted in 1987, mainly in services) has also increased labour market flexibility.

End of disinflation?

The 15.2 per cent fall in import prices of goods and services in 1986 did much to further disinflation. But import prices remained virtually unchanged in 1987 and the rise in the private consumption deflator – at 4.8 per cent – was only 1 point down on the previous year, whereas the rise in the domestic demand deflator remained flat at 4.7 per cent.

The pace of consumer price increases continued to slow up to mid-1987, falling to 4.2 per cent by the second quarter (year-on-year), down from 6.2 per cent the previous year[56]. Since then, however, price rises have moved higher. The carryover of

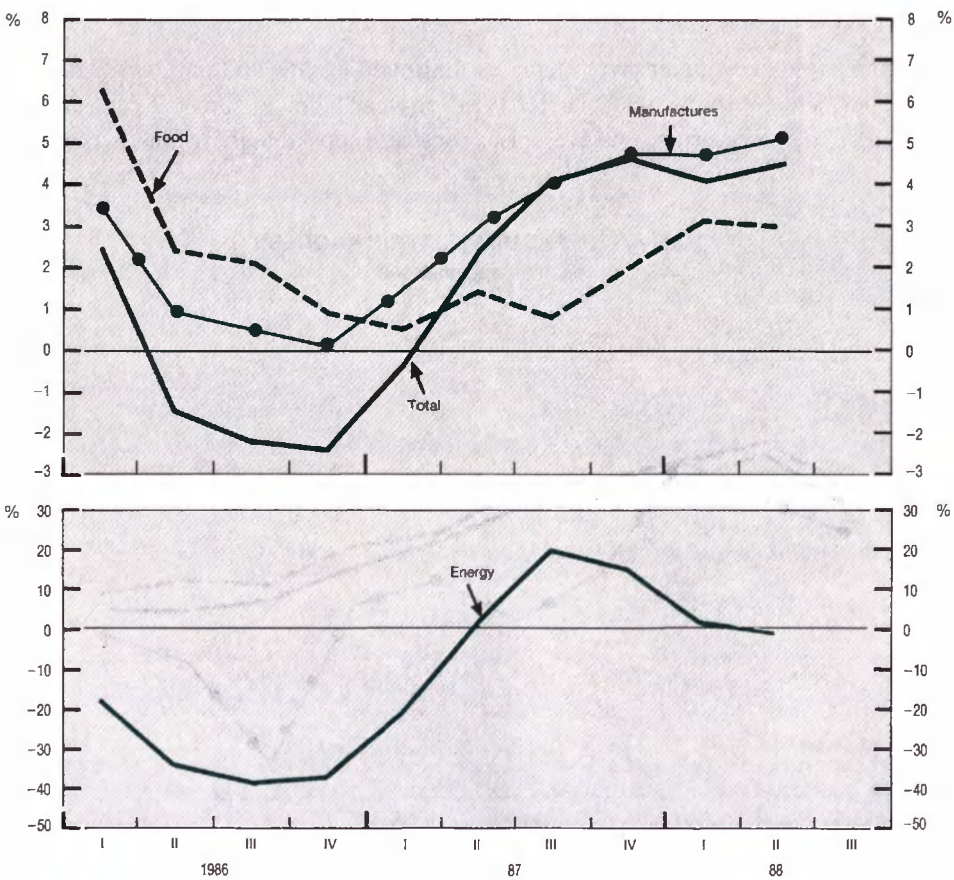
Diagram 12. **THE DISINFLATION PROCESS**[1]
Percentage changes



1. 1988, OECD Secretariat estimates.
Source: OECD, *National Accounts.*

earlier disinflation was such that the annual average price increase was 1.2 percentage points below that of 1986. The increase of VAT rates in August 1987, which added 0.4 per cent to the price index in the fourth quarter, accounts for much of the jump in the price index. During the first half of 1988, consumer prices rose at an annual rate of 4.5 per cent, accelerating to 6.7 per cent in June to November. In that month, consumer prices were 5.3 per cent up on November 1987. Consumer prices continue to rise faster in Italy than in its trading partners, but the gap has narrowed steadily from 10 per cent in 1980 to around 2.5 per cent by end-1986. Since early

Diagram 13. **WHOLESALE PRICES**
Changes from corresponding period



Source: ISTAT.

1987, when inflation accelerated not only in Italy but in the other countries too, the differential has stabilized.

From the second quarter of 1986 to the first quarter of 1987, the general wholesale price index actually declined. This was essentially due to energy prices and was only partly translated into retail prices. However, wholesale prices began to increase at a quick pace from mid-1987. In the third quarter of 1988, wholesale prices were 4.9 per cent up on the same period of 1987.

Compensation per employee rose by 8.6 per cent in 1987, almost 1½ percentage points more than in 1986; in real terms, the rise was 3.7 per cent as against 1.5 per cent in 1986. Because of the timing of the triennial wage negotiations in the public sector, there were large pay increases in the public services and the civil service, where real compensation per head increased by 4.4 per cent in 1987[57]. In industry, by contrast, the increase was only 1.8 per cent, significantly below productivity growth. At the time of writing, the only indicators for the first half of 1988 were contractual wage rates per head. These show a significant acceleration for the economy as a whole, once again stemming largely from the public sector (Table 18). Smaller rises in industry were offset by higher rises in the civil service and public services (education and health), where contractual wages rose by 12.5 and 17.3 per cent respectively in the space of a year.

Table 18. **Wage indicators**

Percentage changes

	1985/1984	1986/1985	1987/1986	1988 I/1987 I
Total economy				
Per capita compensation	10.5	7.5	8.9	
Contractual hourly wage rate	9.4	4.5	6.9	8.5
Industry				
Per capita compensation	11.4	7.1	8.0	
Unit labour costs	7.5	2.5	3.2	
Contractual hourly wage rate	9.7	4.5	6.5	6.4
General government				
Per capita compensation	9.6	7.8	11.5	
	9.8	4.4	7.7	12.5
Memorandum item:				
Contractual hourly wage rates				
Trade	9.7	5.4	6.3	6.9
Transport and communication	9.8	5.3	3.9	6.5
Credit, insurance	11.2	3.7	10.4	5.9
Public services (health, education)	7.7	3.6	9.0	17.3

Source: ISTAT.

Worsening current account

The current balance moved into deficit in the second half of 1987, reaching a deficit of $1 billion or 0.1 per cent of GDP for the year as a whole. Foreign trade performance in volume terms sharply worsened overall in 1987 (Table 19). Merchandise exports grew by 3.3 per cent implying a loss of market share. The volume of imports rose by 10.9 per cent – by 15.2 per cent for manufactures, but with slower growth of energy import volumes than in 1986. There was a further improvement in the terms of trade in 1987, but much more modest than in 1986. However, the deterioration in trade volumes was more marked, amounting to some L 9 500 billion, only partly offset by terms-of-trade gains (Table 20).

Table 19. **Foreign trade volumes**

Annual growth rate from previous period, seasonally adjusted

		1985	1986	1987	1986 I	1986 II	1987 I	1987 II	1988 I
Imports		8.2	2.7	10.9	1.0	0.8	15.4	11.6	4.0
of which :	Manufactured goods	7.0	4.2	15.2	9.0	–8.9	28.8	10.0	4.0
	Energy	4.0	4.6	4.7	8.5	5.3	–5.1	20.0	..
Exports		6.1	1.8	3.3	0.9	–5.8	0.7	13.1	4.1
of which :	Manufactured goods	5.3	1.7	4.1	0.4	–3.8	1.2	11.1	4.2
Memorandum item									
Market growth		3.8	4.4	5.7	..	..	..	..	..

Source: OECD Secretariat.

Table 20. **Breakdown of changes in the current balance**

Billion lire

	1980	1981	1982	1983	1984	1985	1986	1987
Current balance	–8 532	–10 301	–8 432	2 323	–4 314	–7 111	3 791	–1 286
Trade balance (goods)	–14 492	–13 257	–11 960	–3 713	–10 254	–11 928	6 283	141
Change in the current balance	–13 085	–1 769	1 869	10 755	–6 637	–2 797	10 902	–5 077
of which:								
Change in the trade balance	–13 701	1 235	1 297	8 247	–6 541	–1 674	18 211	–6 142
of which:								
Due to terms of trade	–6 440	–8 427	666	5 097	–3 677	1 895	19 908	3 401
Due to volume changes	–7 261	9 662	631	3 150	–2 864	–3 569	–1 697	–9 543

Source: Banca d'Italia, *Annual Report*; OECD Secretariat.

New reporting and computation procedures for customs statistics mean that only partial and hard-to-interpret estimates of foreign trade volumes are available since the beginning of 1988. Customs statistics on a volume basis suggest that merchandise imports rose by 6.4 per cent in the first half of 1988 (year-on-year), while exports rose by 5.8 per cent over the same period. The deficit (cif-fob) widened by L 1 200 billion in the first 9 months of 1988 compared with the corresponding year-earlier period, despite a L 2 500 billion narrowing of the energy deficit over the same period.

The invisibles deficit fell by around $580 million (L 1 000 billion) in 1987. The net balance on travel, in terms of lira, declined, continuing an earlier trend. While receipts rose by 7.4 per cent (around 2.5 per cent in real terms, as the lower dollar discouraged United States tourists), spending by Italian tourists abroad increased by 35.5 per cent (around 30 per cent in real terms)[58]. The deficit on investment earnings

Table 21. **Balance of payments**

$ million

	1985	1986	1987	1986 I	1986 II	1987 I	1987 II	1988 I
				Seasonally adjusted				
Exports FOB	75 686	96 395	116 000	46 046	50 349	55 450	60 550	63 447
Imports FOB	81 933	92 181	115 891	45 492	46 689	55 144	60 747	63 817
Trade balance	-6 247	4 214	109	554	3 660	306	-197	-370
Services net	1 467	-64	-103	12	-78	821	-924	-1 085
of which:								
Travel	6 474	6 944	7 634	3 433	3 510	4 101	3 534	3 441
Investment income	-3 979	-6 210	-6 610	-2 938	-3 271	-3 296	-3 315	-3 658
Private transfers	1 324	1 458	1 286	700	757	695	591	969
Government transfers	-267	-3 066	-2 283	-1 530	-1 536	-563	-1 719	-1 037
Current account balance	-3 724	2 543	-991	-263	2 804	1 259	-2 249	-1 523
				Not seasonally adjusted				
Current account balance	-3 724	2 543	-991	-2 166	4 709	-1 110	119	-4 004
Non-monetary capital	-650	-4 532	1 919	827	-5 359	-319	2 238	1 783
Long-term	2 445	-2 693	2 080	1 503	-4 197	-96	2 177	3 733
Short-term[1]	-3 095	-1 838	-162	-676	-1 162	-223	61	-1 950
Balance on non-monetary transactions	-4 375	-1 989	928	1 340	-649	-1 429	2 357	-2 221
Private short-term monetary capital	2 775	-4 329	4 297	-4 808	478	-3 141	-1 156	-3 746
Net transactions by monetary authorities	-7 150	2 341	5 225	3 468	-1 127	1 712	3 513	1 525

1. Including errors and omissions.
Source: Banca d'Italia, *Annual Report*; OECD Secretariat.

widened by around $400 million, though probably narrowing by around L 700 million in terms of lira reflecting the lira's appreciation against the dollar and a reduction in the foreign debt. The decline in net government transfers was due both to cuts in development assistance and to higher receipts from the European Community.

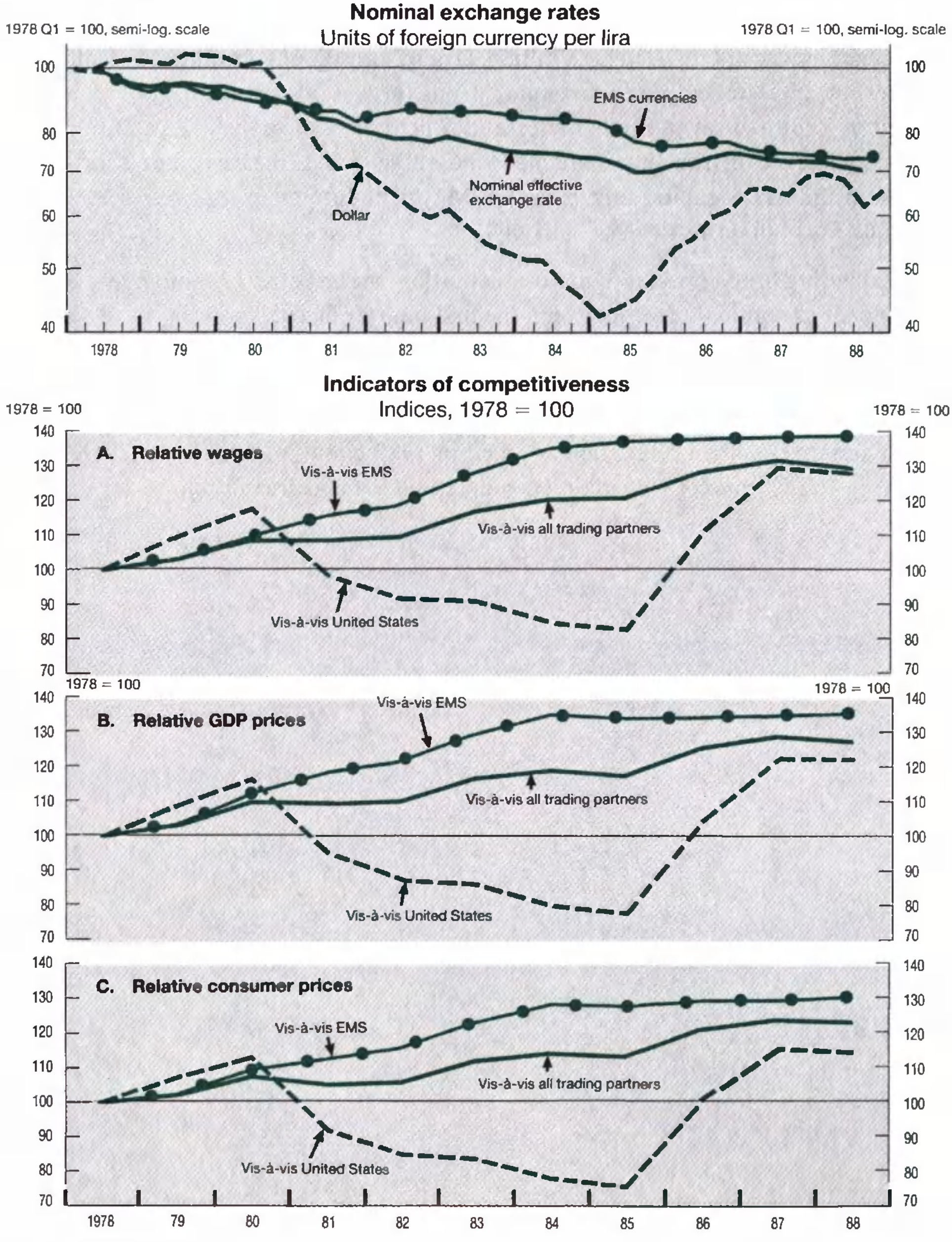
On a seasonally adjusted basis, the current payments deficit, narrowed by $700 million in the first half of 1988 compared with the previous half-year, an improvement due to public transfers. On a non-seasonnally adjusted basis though, the result for the first half of 1988 implies a marked deterioration (of $3 billion) on the corresponding year-earlier period.

Capital and exchange-market volatility

Net inflows of non-monetary capital totalled nearly $2 billion in 1987, in sharp contrast to 1986 which saw a net outflow of capital of $4.5 billion. Net direct investment in Italy was $1.7 billion, against net disinvestment a year earlier of $2.7 billion (1986 was marked by the sale of Libya's Fiat holdings amounting to $2.5 billion). Purchases of foreign assets by Italian residents almost doubled in 1987, as a result of purchases by investment funds (L 11 500 billion), stimulated by the abolition in May 1987 of the compulsory non-interest bearing deposits required for purchases of foreign assets. The required deposit was 10 per cent of the invested sum at the beginning of 1987. Net sales of Italian financial assets by non-residents totalled $3.7 billion, mainly reflecting net sales of Italian shares. Altogether, capital outflows for portfolio investment totalled $7.3 billion in 1987 against $1 billion in the previous year. Last, net direct foreign borrowing by Italian residents rose steeply (by some L 7 300 billion), largely a reaction to the greater stringency of monetary policy in the second half year, when bank-lending ceilings were reinstated. Ecu-denominated Treasury borrowing expanded strongly, totalling L 2 137 billion in 1987.

Foreign exchange market volatility, along with frequent and major changes in exchange-rate expectations about the lira sparked off large-scale short-term capital movements. Net monetary capital inflows again amounted to about $4 billion in 1987, with some volatility during the year. After the January 1987 EMS realignment, prospects of a more stable lira and high interest rates led to massive banking inflows. Expectations swung the other way in the second quarter with the lifting of exchange controls and the Summer saw a large outflow of capital. This movement was only stemmed when bank-lending ceilings were reinstated and exchange controls reintroduced in mid-September. These controls encouraged inflows of monetary

Diagram 14. **THE EXCHANGE RATE AND COMPETITIVENESS**



Source: OECD Secretariat.

capital once again, leading to a renewed net inflow of banking funds for the second half of around L 1 400 billion. For 1987 as a whole, Italy's official foreign exchange reserves rose by L 6 775 billion ($5.2 billion). In the first half of 1988, net inflow of non-monetary capital totalled $1.8 billion, largely a result of substantial net inflow of long-term capital, reflecting in particular strong foreign investment in Italy. The first quarter of 1988 too saw a further substantial net inflow of monetary capital; but in April, confidence in the lira weakened and there was a massive, but short-lived outflow of monetary capital that halted in May. The foreign exchange reserves rose by about $1.5 billion in the first half of 1988.

Excluding brief episodes of major fluctuation, the effective exchange rate fell by 5.5 per cent in nominal terms between the first quarter of 1987 and the third quarter of 1988. The lira depreciated by 7.3 per cent against the dollar and 4.4 per cent against the Deutschemark. However, real effective lira exchange rate (deflated by consumer prices) was broadly stable up to January 1988, falling by 3.2 per cent since then. Exchange-control relaxation adopted in 1987 came into force on 1st October 1988 (see the Chronology of main economic policy measures in Annex II).

IV. Policies and prospects

Economic policy sought to achieve sufficient economic growth to bring down unemployment, reduce the budget deficit and combat inflation. But the implementation of fiscal policy was impeded by the unstable political situation. Last Spring, the new government nonetheless adopted a medium-term programme of fiscal consolidation according to which the draft 1989 Budget was prepared. Also, reforms in Parliamentary procedure on voting and on budgetary matters should facilitate the authorities' future task. The monetary authorities intend to rely more on interest-rate mechanisms than in the past. However, in view of the heavy pressure on foreign-exchange markets and the vigorous expansion in bank lending, some of which was used to speculate against the lira, the monetary authorities twice felt compelled to reimpose direct controls: credit ceilings and exchange control were temporarily reinstated. After these controls were relaxed in Spring 1988, financial markets experienced instability, and funding the Treasury deficit became more difficult, a problem eased only after interest rates were raised in August.

Slow fiscal adjustment

The broad thrust of fiscal policy was analysed in Part I (see also Diagram 1 and Table 2). The following paragraphs explore in more detail recent public finance and policy developments as well as the government's medium-term programme.

Developments in 1987

1986 saw progress in bringing down the deficit, with the budget deficit almost L 1 000 billion down on the previous year, due to a variety of mainly temporary factors, of which the fall in oil prices was among the most important[59]. The authorities sought further fiscal consolidation in 1987. According to the initial draft Finance Act, the central government deficit was budgeted to narrow from L 109 283 billion in

1986 (12.1 per cent of GDP) to L 102 600 billion in 1987 (10.6 per cent of GDP)[60]. This was to be achieved by maintaining current spending, excluding interest payments, at the same real level as in 1986, holding the growth of public sector investment to that of nominal GDP and keeping the tax/GDP ratio unchanged. This package of measures was intended to reduce the primary deficit by L 1 500 billion relative to the actual 1986 outturn, and in view of the decline in interest rates in 1986, the interest burden on government debt was expected to be some L 5 000 billion smaller. This draft Finance Act was part of the medium-term budget strategy to eliminate the primary deficit in 1990, set out by the previous government in 1986. The main measures to achieve the 1987 targets were:

- Limits to increases in civil service contractual pay and curbs on staffing;
- Limits to central government transfer payments, national pension scheme funding, and health expenditure;
- Ceilings on public enterprise borrowing.

Table 22. **Central government budget**

Lire thousand billion

	1987 outturn (1)	1988 initial draft (2)	1988 final estimates (3)	1989 initial draft (4)	Percentage changes (3)/(1)	(4)/(2)
Current revenue	273 991	299 350	306 500	338 250	11.9	13.0
Direct taxes	122 592	131 000	248 000	277 100	14.9	18.4
Indirect taxes	93 173	102 950				
Other	58 226	65 400	58 500	61 150	0.5	-6.5
Current expenditure	326 676	352 500	365 450	394 500	11.9	11.9
of which:						
Transfers	156 107	168 100	177 500	188 700	13.7	12.3
Interest	76 262	78 800	79 200	86 800	3.9	2.7
Saving	52 685	53 150	58 950	56 250		
Capital expenditure (net)	60 729	76 600	73 550	70 050	21.1	-8.6
Investments	3 043	3 200	3 700	3 900	21.6	21.9
Transfers	57 686	73 400	69 850	66 150	21.1	-9.9
Budget balance	113 414	129 750	132 500	126 300		
Treasury operations	-6 069	-28 750	-14 500	-8 950		
Financial transactions (net)	6 214	8 500				
Borrowing requirement	113 559	109 500	118 000	117 350		
Borrowing requirement as percentage of GDP	11.6	10.5	10.9	10.2		
Borrowing requirement (excluding interest) as percentage of GDP	3.8	2.4	3.6	2.7		

Source: *Relazione sulla stima del fabbisogno di cassa del settore pubblico per l'anno 1987*, and information transmitted by the Italian Authorities.

The outturn was far removed from the initial targets, themselves revised as the year progressed. The deficit was L 11 000 billion higher than targeted (1 per cent of GDP), with current expenditure, excluding interest payments, 6.5 per cent higher (4.5 per cent in real terms, using the implicit GDP deflator). Debt interest payments were boosted by the stronger-than-expected growth of the primary deficit and, as in the previous year, amounted to almost 8 per cent of GDP. On the other side, current receipts were 7.1 per cent higher than forecast and their share in GDP expanded by 0.5 percentage points (reaching 27.9 per cent of GDP).

There were several reasons for this overrun:

- First, the 1986 Budget outturn on which the 1987 Budget was based reflected a number of special factors: the appropriation by central government of much of the windfall revenues from the fall in the oil bill, a steep decline in interest rates and exceptional revenue from a fine on unauthorised building;
- Second, the political crisis at the beginning of 1987 prevented the Government from enacting legislation to rein back growth of expenditure on health and retirement benefits. As a result, it was obliged in March to increase its 1987 deficit estimates by L 3 000 billion;
- Third, difficult negotiations on the renewal of the triennial wage agreements concluded with significant pay increases: expenditure on public sector pay rose by 12.4 per cent, of which about half derived from the contractual agreements.

In view of budgetary overruns, some overheating of domestic demand and pressure on the lira, a package of fiscal measures was introduced at the end of August 1987. These consisted of higher excise taxes (taxes on oil products) and a temporary (i.e. to the end of the year) 4-point rise in VAT rates on a number of consumer durables. A number of direct tax receipts were brought forward: by increasing advance payments of corporate taxes and of the withholding tax on bank interest; and by advancing the date for doubling the tax on government securities.

Unlike the central government budget, the general government deficit narrowed in nominal terms in 1987 (Table 23). This discrepancy reflected the transfer of funds from local authorities to central government which lowered the central government deficit in 1986 but not in 1987. Such intragovernmental transfers net out in the consolidated general government account. Thus, for the second year running, the general government borrowing requirement was reduced by 1 per cent of GDP. But the primary structural deficit declined only a little (see Diagram 1): the move towards

Table 23. **Consolidated general government account**[1]

	As % of GDP 1987	Lire thousand billion				Percentage changes		
		1987	1988	1989[2]	1990[2]	1988/1987	1989/1988[2]	1990/1989[2]
Current revenue	**39.6**	**388.8**	**429.9**	**464.9**	**499.4**	**10.6**	**8.1**	**7.4**
of which:								
Direct taxes	13.3	130.4	148.6	160.3	172.8	14.0	7.9	7.8
Indirect taxes	9.5	92.9	104.1	114.4	123.5	12.0	9.9	8.0
Social security contributions	13.9	136.6	147.5	158.5	169.7	7.9	7.5	7.0
Current expenditure	**45.2**	**444.0**	**486.5**	**518.1**	**548.6**	**9.6**	**6.5**	**6.3**
of which:								
Consumption	16.7	163.9	176.9	188.7	200.1	8.0	6.7	6.1
Transfers to households	17.0	166.9	184.6	196.6	210.3	10.6	6.5	6.9
Subsidies	2.6	26.0	27.5	25.8	23.9	6.1	–6.2	–7.6
Interest	8.1	80.1	89.4	98.3	107.0	11.6	10.0	8.9
Current saving	5.6	–55.2	–56.6	–53.2	–51.2			
Capital expenditure (net)	5.1	47.7	50.0	56.0	60.6	4.8	12.0	8.2
of which:								
Investment	3.5	34.6	37.6	41.0	44.5	8.5	9.1	8.6
Borrowing requirement		**–102.9**	**–106.6**	**–109.2**	**–111.8**			
(as percentage of GDP)		**–10.5**	**–10.0**	**–9.5**	**–9.1**			

1. National accounts basis
2. OECD forecasts.

Sources: *Relazione generale sulla situazione economica del paese*, 1988; OECD Secretariat.

restriction in 1987 was therefore decidedly modest. Moreover, the fall in inflation in 1987 meant that the inflation-induced decline in real government debt was reduced. The inflation-adjusted structural budget deficit was virtually constant after falling by around 1¼ per cent of GDP in 1986. Government debt in 1987 totalled L 909 983 billion, up 14.5 per cent on 1986 and equivalent to 92.4 per cent of GDP.

Some 6 per cent of the public sector borrowing requirement (close to the Treasury deficit) was financed externally, mainly through five-year Ecu bonds. Money creation continued to play only a small part in financing the PSBR, accounting for 7 per cent, slightly less than in the previous year. The major source of finance was the issue of government debt. The share of long and medium-term debt fell from 80 per cent of total in 1986 to 55 per cent in 1987, with Treasury-bill financing amounting to 32 per cent[61]. Investors tended to shun medium-term certificates of deposit, because their value had fallen on the secondary market when interest paid to holders became taxable. As interest rates fell worldwide, the effective interest rate on government debt (the ratio of interest payments to total debt) declined in 1987 (Table 1).

Table 24. **Financing of public sector deficit and public debt**

Lire thousand billion

	1982	1983	1984	1985	1986	1987	June 88
Total financing of public sector[1]							
Pair: Bank of Italy	12.1	1.0	13.2	27.4	10.7	7.0	2.4
Foreign borrowing	2.6	1.3	2.3	2.9	0.9	6.1	1.0
Other	63.2	90.2	88.2	92.2	100.7	104.0	54.2
of which:							
Medium and long-term	25.1	69.0	58.0	87.1	79.5	55.3	26.4
Treasury bills	29.0	10.4	14.9	−1.9	8.4	32.2	25.0
Post Office savings deposits	3.7	4.9	6.4	9.1	11.3	12.9	2.9
Public debt outstanding							
Total gross debt[2]	361.6	455.5	560.9	682.6	793.1	909.0	966.6
As percentage of GDP	**66.3**	**72.9**	**77.1**	**83.7**	**87.9**	**92.4**	
Memorandum item:							
GDP at current prices	545.1	633.6	727.8	815.6	902.2	982.6	

1. The public sector refers to the "Settore Statale", see Table A4 in Annex I for definition.
2. End of period.
Source: Banca d'Italia, *Economic Bulletin*.

Problems in implementing the 1988 Budget

When the 1988 Finance Act was being drafted, the institutional and political problems facing the government in implementing its budget strategy became evident. In the initial Finance Act Budget, published in September 1987, the intention was to stabilize the deficit in nominal terms at the level expected at the time for 1987, i.e. L 109 500 billion, narrowing to 10.5 per cent of the official GDP target for 1988 (down by 3/4 of a percentage point from the expected outturn for 1987). This target was based on official forecasts of real GDP growth of 2.8 per cent, the deflator rising by 4.7 per cent. After the October financial crisis, the government adopted more ambitious targets, with the budget deficit scheduled to narrow by a further L 6 000 billion, and hoped to cut it by another L 3 500 billion as a result of new measures to be introduced in 1988, so bringing it down to L 100 000 billion.

The main measures which were supposed to achieve this new target were the following:

- On the tax front, postponing the reforms of personal income tax rates and schedules planned for 1988. It has also been decided to postpone scheduled VAT increases, so that, overall, the two measures partly offset each other, resulting in net receipts of L 800 billion;

- Some social security (cancellation of the reduction in employers' contributions) and health insurance measures (reduced reimbursement of medical prescription charges) were expected to achieve economies of around L 1 300 billion;
- The main contribution to reducing the borrowing requirement was to come from a L 3000 billion reduction in Treasury loans to ENEL (the National Electricity Agency) and the Italian telecommunications corporation.
- Last, debt interest payments were expected to fall by around L 500 billion.

This second draft Finance Act was substantially altered in the course of its discussion in the Senate and Chamber of Deputies. Most of the expenditure-cutting measures were either dropped or amended. On the receipts side, virtually the whole of the initial package was retained, except for the provisions allowing firms to revalue their assets and pay a tax on the revised valuation. By the time the Finance Act was passed in its final form, the deficit had risen to L 122 000 billion. At the end of the months of May and July, the government adopted new measures aimed at pulling the deficit back to some L 115 000 billion. These included advanced or augmented payments of direct taxes and higher stamp duties, an increase in the standard VAT rate from 18 to 19 per cent, higher taxes on fuel and electricity and a greater contribution to medical prescription costs. Estimates made in late summer suggest that the budget deficit for 1988 as a whole could well exceed the revised July target by around L 3 000 billion. However, estimates made since then indicate that the outturn could even be greater: the budget deficit could well be close to L 125 000 billion, bringing in to 11.5 per cent of GDP, as in 1987.

The medium-term plan and the 1989 Finance Act

In March 1988 the government approved a new medium-term fiscal programme[62]. It is designed gradually to reduce the public sector borrowing requirement, excluding interest payments, so as to achieve a small surplus by 1992, and from then on to stabilize (and ultimately reduce) the government debt/GDP ratio (Table 25). The bulk of the adjustment envisaged is to take place between 1990 and 1992. The share of non-interest government expenditure in GDP remains broadly constant, while the share of current receipts rises by 3.5 percentage points and interest payments fall by 1.5 percentage points (comparing 1992 plan with 1987). A comparison of plan targets with "automatic" trends (as defined in the plan) is also shown in Table 25. On the basis of this comparison, the targets would be achieved

Table 25. **Public finance consolidation programme**

Consolidated public sector account as a percentage of GDP

	1987	Consolidation programme		"Automatic" trends	
		1990	1992	1990	1992
Current revenue	40.9	43.3	44.4	42.1	42.6
of which:					
Direct taxes	13.0	13.9	14.6	13.4	14.0
Indirect taxes	10.4	11.7	12.1	11.0	11.0
Social security contributions	12.1	12.1	12.2	12.1	12.2
Current expenditure	47.2	46.4	44.8	47.9	48.7
of which:					
Wage and salaries	14.2	14.0	13.8	14.2	14.2
Transfers	15.7	15.6	15.5	16.0	16.3
Interest	8.1	7.7	6.6	8.5	9.0
Capital expenditure	6.0	6.3	6.4	6.3	6.4
of which:					
Investment	3.6	3.9	4.0	3.9	4.0
Transfers	2.4	2.3	2.3	2.3	2.3
Total expenditure[1] excluding interest	46.0	45.7	45.3	46.3	46.9
Current saving	–6.2	–3.1	–0.4	–5.8	–6.1
Borrowing requirement excluding interest[1]	**–3.5**	**–1.3**	**0.4**	**–3.2**	**–3.2**
Total borrowing requirement[1]	**–11.6**	**–9.0**	**–6.1**	**–11.7**	**–12.2**
Memorandum item:					
Public debt	**92.4**	**104.1**	**106.8**	**108.5**	**120.0**
Nominal interest rate of debt (as a percentage)	8.8	7.4	6.2	7.9	7.5

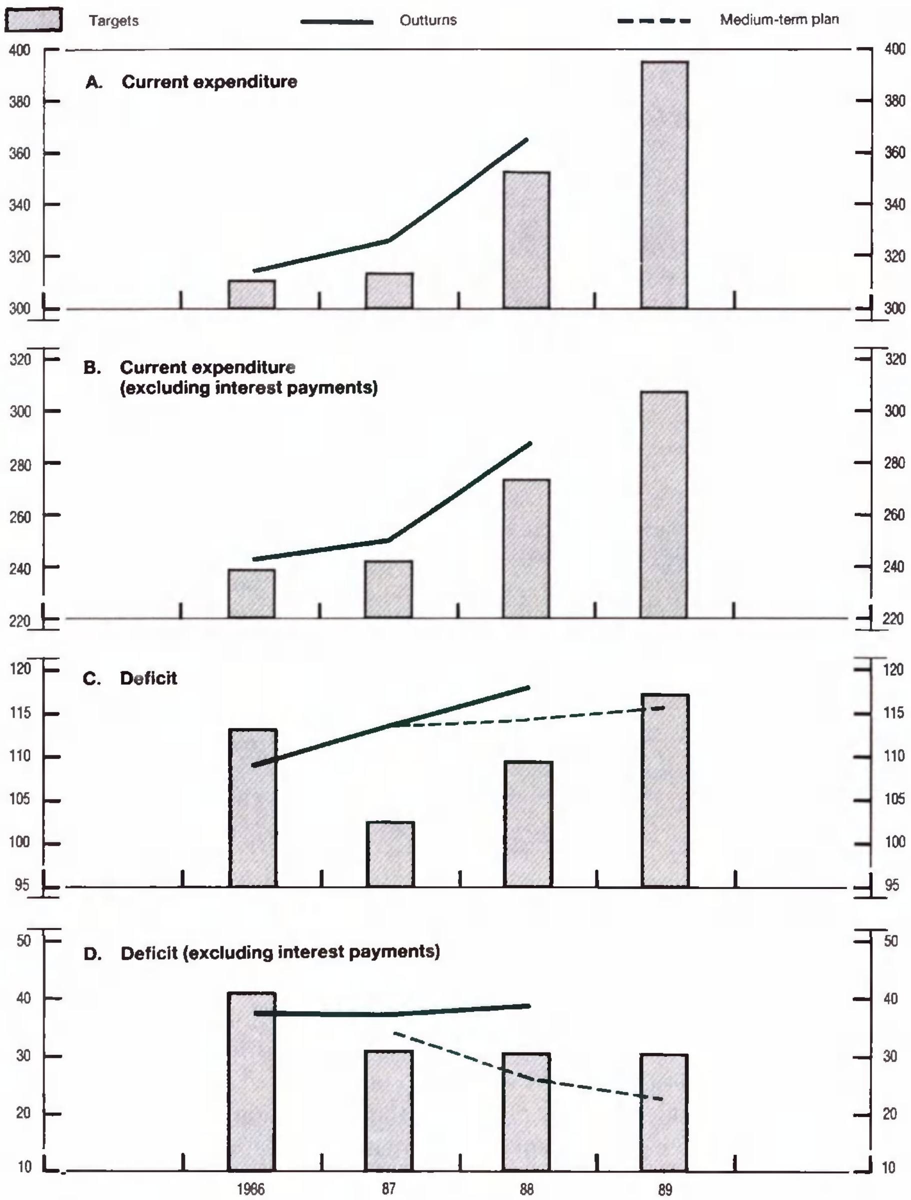
1. Including financial transactions

Source: Finance Act 1988.

more or less equally by higher taxation and by expenditure restraint with the weight of tax revenues in GDP being set to rise between 1987 and 1992 by 1.8 points more than it would automatically and that of current expenditure by 1.5 points less. By 1992 this would produce a current surplus, excluding interest, of around 6.2 per cent of GDP, 3.3 per cent higher than would have come about without policy action. The other major factor in the planned fiscal consolidation is the fall in the interest burden. While part of the decline may be explained by the elimination of the primary deficit and the impact of this on government debt, another factor is the implicit assumption that a fall in the effective debt interest rate from 7.4 per cent in 1992 on the spontaneous projection to 6.1 under the programme. This would imply that interest payments would fall by 1½ GDP points between 1987 and 1992.

Diagram 15. **GOVERNMENT EXPENDITURE AND DEFICITS: TARGETS AND OUTTURNS**

Lire, thousand billion



Source: Figures supplied by the Italian authorities.

The programme relies on heavier indirect and direct taxes. In the latter case, the tax reforms planned for 1988 and postponed to 1989 are to be applied with a view to redefining tax schedules and bands and adjusting them for inflation. The improvement in direct tax yields is expected mainly to come about through redefining income tax criteria for the self-employed and measures to combat tax evasion. The deceleration of expenditure is based on the assumption of tighter curbs on wage expenditure (which accounts for 30 per cent of current expenditure) to prevent it from rising faster than GDP. The workforce is set to expand by 0.5 per cent a year (against 1 per cent between 1981 and 1987) and real wage growth per head is to be brought down to 1 per cent a year[63]. Part of the containment of expenditures reflects higher charges for medical prescriptions and a freeze on the prices received by pharmaceutical companies.

The programme recognises the need to control expenditure better and to enhance its effectiveness. Accordingly, the budget procedures have been altered as from the preparation of the 1989 Act which was conducted according to the new public accounting procedures published in August 1988 (see Annex II). For instance expenditure proposals are to be submitted within the framework of a multi-year plan so that the future budgetary implications of any particular measure can be assessed. New proposals would have to include an estimate of the financial cost; their funding would be provided through a specific law covering the entire duration of the project. Last, any proposal involving new expenditure would also have to include provision for its funding.

The 1989 Budget is the first to be considered under the new public finance consolidation programme. The Finance Act laid before Parliament at the beginning of October under the Programme's new rules is seeking to stabilize the deficit at nearly the same level as in 1988 in nominal terms (L 117 350 billion), 0.8 per cent down as a percentage of GDP. Two measures incorporated in the 1989 Budget will inevitably increase the deficit. First, personal income tax reforms reduce tax rates in all bands (the top rate being brought down from 62 to 50 per cent). The loss in tax revenue from this reform is estimated to amount to almost L 6 000 billion. The second set of measures are the wage increases for school teachers (negotiated in 1988) which affect around half of government employees and will boost wages by 9 to 12 per cent a year over the period 1989-1992. Last, debt interest payments will accelerate as a result of interest-rate increases during 1988. In the absence of discretionary measures, the budget deficit for 1989 was officially estimated at L 147 500 billion. The draft Finance Act had therefore to embody new measures to cut the deficit by some L 30 000 billion.

The tax package to achieve this has three main elements. First, the tax treatment of small and family businesses was reformed, broadly along the lines, but with some variations, of the scheme provisionally adopted in 1985 which introduced lump-sum taxes for the self-employed, traders and small businesses. The earlier scheme's fairly low qualifying thresholds for turnover were raised. Businesses that had underpaid past taxes may benefit from a tax amnesty by paying a predetermined fine. Access to the new scheme is conditional on the regularisation of past tax liabilities and is expected to yield L 5 000 billion. Secondly, the increased rates of indirect taxes introduced on a temporary basis in 1988 will be made permanent. Combined with further increases in VAT, these measures should yield L 5 000 billion. Finally, the increase in each ministry's current expenditure is to be limited to 14 per cent of the effective expenditure in *1987*. This measure is expected to yield L 15 000 billion. However, this ceiling applies on a *commitment basis* (Bilancio di competenza)[64]. The actual reduction in *cash* expenditure (Bilancio di cassa) will be much less, and will be mainly achieved by reducing investment expenditure.

According to Secretariat estimates, general government borrowing requirement (national accounts basis) fell by around ½ per cent of GDP in 1988. On the assumptions that real GDP growth exceeds 3 per cent and that official fiscal policy objectives are in large measure achieved, the deficit could well show a cumulative decline equivalent to 1 percentage point of GDP by the end of 1990.

Monetary policy

In September 1987, the Bank of Italy was obliged for the second time in less than two years to reinstate direct controls. These included the prohibition of advance reimbursement of foreign-currency borrowing and other measures aimed at reducing "leads and lags" and at increasing foreign-currency borrowing (by imposing shorter periods for using or converting foreign currency). Ceilings were also imposed on the growth of lira-denominated bank lending from 13th September 1987 to March 1988. As with fiscal policy, these measures sought to restrain domestic demand and, in addition, to reduce pressure on the lira and to contain a sizeable overrun of monetary targets. The discount rate was also raised from 11.5 to 12 per cent at the end of August. Against a target growth set at 11.1 per cent for 1987, total domestic credit growth to the end of August was running at 13.5 per cent (from the beginning of the year on a seasonally adjusted basis), with lending to the State and non-State (which includes some public enterprises) sectors up 14.5 and 11.8 per cent respectively.

Table 26. **Monetary aggregates**

	Lire thousand billion			Percentage changes from corresponding period of previous year				
	Outstanding at 31/12/1985	Change 1986	Change 1987	December 1986	June 1987	December 1987	June 1988	December 1988
Currency in circulation	45.0	3.2	4.4	7.1	7.8	9.2	8.5	
Sight deposits	258.3	29.2	20.4	11.3	12.2	7.1	6.3	
M1	303.5	32.4	24.9	10.7	11.5	7.4	6.6	
Time deposits	258.9	20.4	26.4	7.8	13.3	9.4	7.8	
M2	562.4	52.7	51.3	9.4	12.4	8.3	7.2	
M3	687.7	56.5	84.7	8.2	9.4	11.5	12.8	
Total domestic credit	1 005.7	152.4	151.6	15.0	15.6	13.1	13.5	
To public sector	605.2	106.7	105.8	17.7	16.5	14.9	14.6	
To private sector	400.5	45.7	45.8	11.0	14.1	10.3	11.6	
Official targets								
Total domestic credit				13.2	–	11.0	–	9.4
To public sector				17.2	–	13.5	–	12.7
To private sector				7.0	–	7.0	–	8.0

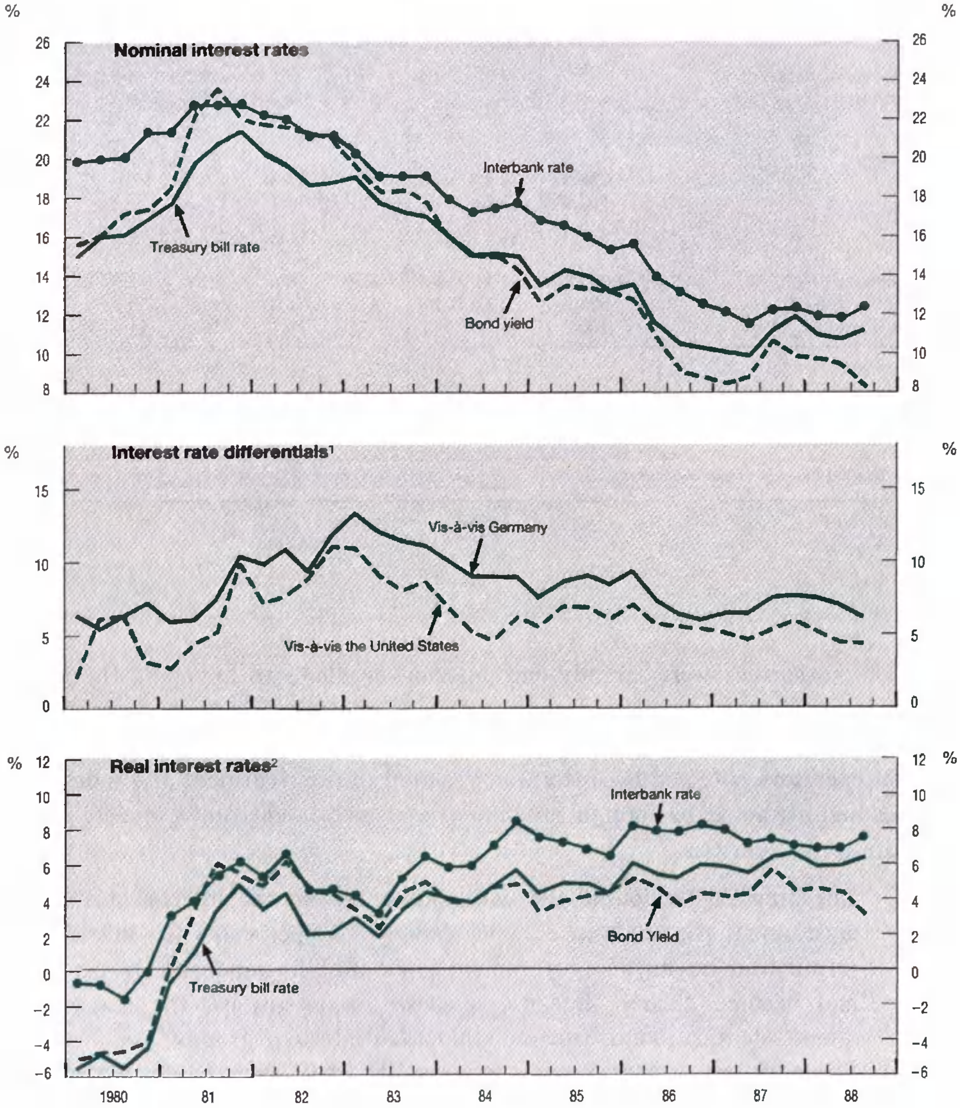
Source: Banca d'Italia, *Economic Bulletin.*

The authorities were already encountering problems in financing the public sector deficit when the measures were introduced. On several occasions from the first quarter, they had raised the rates of return on government securities but financial market operators, affected by uncertainty related to tax treatment and indexation clauses and attracted by foreign investment and investment funds, moved out of medium-term securities.

- The proposal to double the withholding tax on the interest income on government paper (from 6.25 per cent to 12.5 per cent) led investors to refrain from buying new government paper until the impact on pre-tax yields had become clearer. Because of new tax provisions, the market for almost-identical bonds became segmented into four groups[65];
- Secondly, investment funds sought to diversify their assets away from domestic paper to foreign-currency denominated assets.

Selling on the secondary market also took place on a massive scale, leading the authorities to intervene heavily to prop up values in the secondary market and to accelerate reforms of secondary market procedures.

Diagram 16. **INTEREST RATES**



1. Uncovered differential: Italy (Treasury bills, 3 months) *less* Germany (interbank rate, 3 months), *less* United States (Treasury bills, 3 months).
2. Deflated by the consumer price index.
Sources: OECD, Banca d'Italia.

Expectations reversed in the Autumn, the growth of lending slackened and there was a massive inflow of funds, allowing exchange-control measures to be lifted in January 1988. Between August 1987 and February 1988, the rate of growth (over twelve months) of domestic lending to the non-State sector fell back from 12.8 to 9.3 per cent, while growth of lending to the State sector slowed by 1.6 percentage points. Growth of bank lending was certainly boosted by buoyant activity, though speculation against the lira was probably the principal factor. Borrowers, for the most part large enterprises conducting a large number of financial transactions, placed these funds abroad, and major outflows of capital occurred[66].

The targets for growth in domestic lending in 1988 have been set some 2 percentage points below those for 1987, the authorities expecting lending to the public sector to grow somewhat more slowly and lending to the private sector slightly faster. The target range for M2 growth was broadly the same. After the lifting of bank-credit ceilings in March 1988, growth surged again, to 12 per cent in July, against an annual target of 6 to 10 per cent. Since lending to the public sector was expanding at a rate of over 14 per cent, total domestic credit growth was 13.5 per cent year-on-year and 14.5 per cent at an annual rate between January and July 1988, overshooting the annual target by some 4 percentage points. By end-July, M2 growth was running at 8 per cent, within the target range but accelerating rapidly. The considerable disparity between money supply expansion and lending reflects growing financial market liberalisation. For instance borrowing abroad was not subject to reserve requirements until March 1988. Also, the banking sector was able to step up lending more rapidly than bank deposits by selling government securities.

From May onwards, the Bank of Italy has increased its temporary placement of government paper with the banking sector in order to neutralise its liquidity[67]. Monetary policy tightened for both domestic (fear of overheating) and external reasons (figures available in May fed fears that the balance of payments might worsen rapidly). The Bank of Italy applied "moral suasion" to banks to increase their lending rates. This advice was only partly heeded and the interest-rate rises that occurred did not push up the base lending rate.

Although households' demand for government securities remained strong, the sluggishness of demand by the banking sector made it difficult to meet the Treasury's borrowing requirements in June, and the Treasury was again forced to borrow short term, so reducing the maturity of the debt. This situation persisted in July and August when once again it ran into difficulties on the medium and long-term securities market and was faced with the choice of again cutting the average maturity of debt or of raising interest rates and thereby widening the budget deficit. The international interest-rate rises in August impelled the Italian monetary authorities to raise the discount rate by 0.5 percentage points, to 12.5 per cent. This decision was followed by a commensurate readjustment of all market rates, enabling the Treasury to borrow more easily. Auctions in September and October saw a brisk pick-up in the demand for medium-term fixed-interest securities. But this was achieved only by significantly higher yields: between May and October, gross yields on four-year fixed-interest Treasury bonds rose by 1.15 percentage points while those on two-year bonds and five-year variable-rate Treasury credit certificates rose by 1 point.

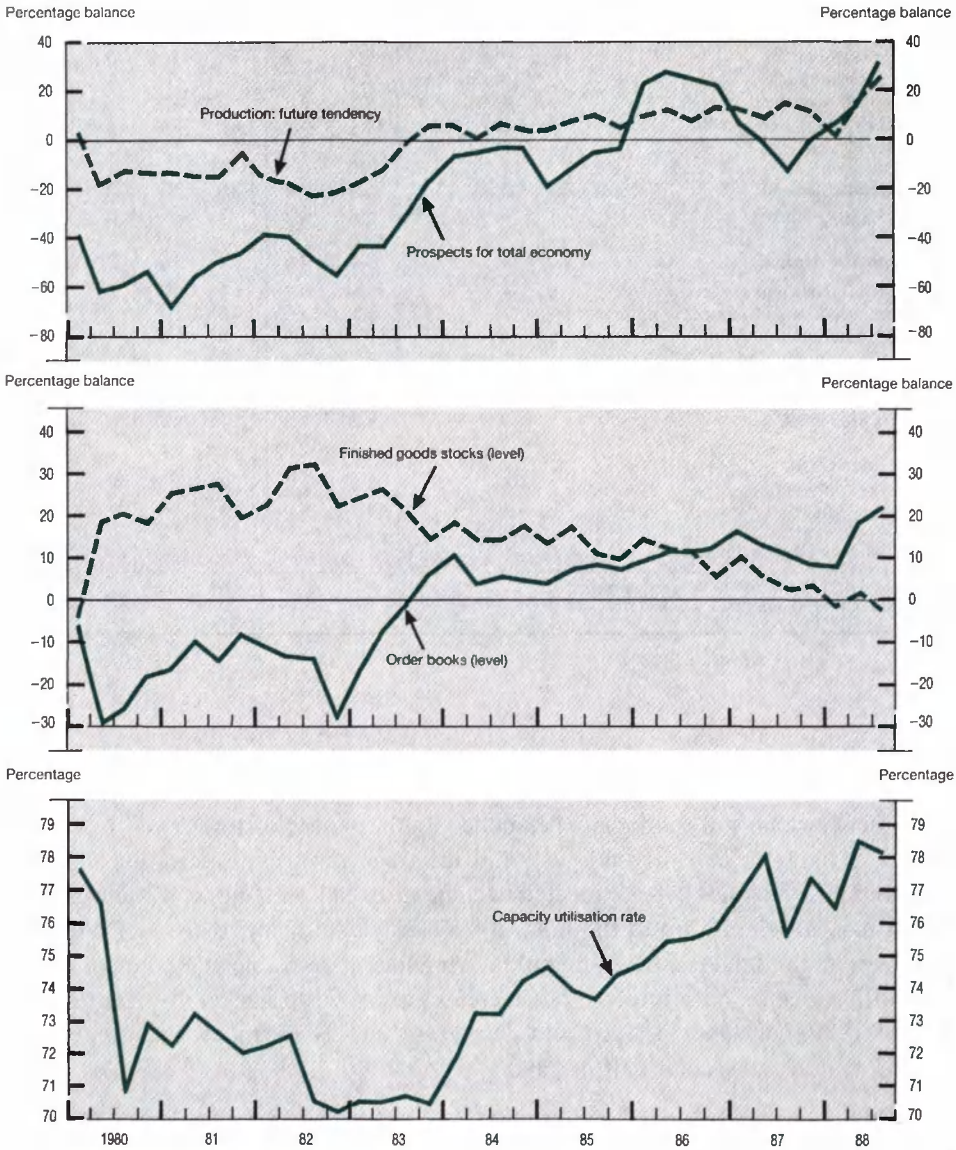
Prospects for 1989 and 1990

The projections presented below are the same as those published in the OECD *Economic Outlook* N° 44 (December 1988). They are based on the following technical assumptions and assessment of international developments:

- The nominal exchange rate assumption, fixed at levels prevailing on 2nd November 1988, is L 1 324 to the dollar in 1989 and 1990. This implies that the effective exchange rate of the lira remains broadly unchanged at its 1988 level during the projection period;
- The fob price per barrel of oil, estimated at $12 in 1988, is assumed to remain constant in real terms over 1989 and 1990;
- Export market growth for manufactured goods is estimated at 7½ per cent in 1989 and 1990.

Business indicators (Diagram 17), still buoyant, no longer point to a further acceleration of final domestic demand: its growth is projected at a rate of 3¾ per cent in the first half of 1989. Household consumption growth could slacken in 1989 and 1990, with wage increases moderating as the effects of the 1987-88 wage agreements gradually wear off. Direct tax payments seem set to rise slightly and the full annual effects of the 1988 VAT increases will be felt. Investment could also ease. The need for rationalisation and modernisation investment could become less pressing, while the prospect of international demand levelling off could also have a damping effect and real interest rates are likely to remain high. The external contribution to growth could remain negative and GDP growth could well decelerate by 1 percentage point between 1988 and 1990 to 2¾ per cent. Employment is unlikely to rise by more than 0.5 per cent, too small an increase to prevent the unemployment rate from moving up again from the first half of 1990.

Diagram 17. **BUSINESS INDICATORS**[1]
Results of business surveys



1. Mining and manufacturing.
Source: OECD, *Main Economic Indicators.*

Table 27. **Short-term projections**

Percentage changes from previous period, seasonally adjusted, at annual rate

	1988	1989	1990	1988 I	1988 II	1989 I	1989 II	1990 I	1990 II
Demand and output									
Private consumption	4.1	3½	3	5.1	3.7	3½	3¼	3	2¾
Public consumption	2.2	2	1¾	1.5	2.8	2	1½	1¾	1¾
Gross fixed investment	5.8	4¾	4.0	8.5	4	5¼	4¼	4	4
Machinery and equipment	7.5	6	5¼	10.4	5.3	6½	5½	5	5¼
Construction	3.8	3	2½	6.2	2.5	3½	2½	2½	2¼
Final domestic demand	**4.2**	**3½**	**3**	**5.3**	**3.6**	**3¾**	**3¼**	**3**	**2¾**
Stockbuilding[1]	–0.1	½	0	–2.1	4.4	–1	0	0	0
Total domestic demand	**4.0**	**4**	**3**	**3.1**	**7.9**	**2½**	**3¼**	**3**	**2¾**
Exports of goods and services	6.6	4¾	5	7.9	0.4	6¾	5½	5	5
Imports of goods and services	7.5	7	5¾	5.5	14.0	4¼	5¾	5¾	5¾
Foreign balance[1]	–0.5	–¾	–½	0.3	–3.5	¼	–¼	–½	–½
GNP at market prices	**3.7**	**3½**	**2¾**	**3.6**	**4.6**	**3**	**3**	**2½**	**2½**
Industrial production	4.5	4	3	8.2	2.2	5¼	3½	3	3
Prices									
GDP price deflator	4.8	4	4	4.6	4.0	4	4	4	3¾
Consumer prices	4.9	4¼	4	4.6	4.4	4¼	4	4	3¾
Current balance (Billion dollar)	–4	–6	–6	–3	–5	–6	–5	–6	–6

1. As percentage of GDP from the previous period
Source: OECD Secretariat estimates and forecasts.

Wages will still be affected at the beginning of 1989 by the 1988 public sector agreements which will continue to be applied. In the private sector, by contrast, wage growth is likely to be fairly subdued and the trend towards working longer hours observed in 1987 and 1988 is expected to come to an end. All told, real wage growth, which may accelerate up to the first half of 1989, could slow thereafter, allowing increases in unit labour costs in manufacturing to remain stable at an annual rate of around 2 per cent. With import price increases expected to slacken from the second half of 1989, consumer prices could decelerate slightly to under 4 per cent at an annual rate in the second half of 1990.

On the usual technical assumption of unchanged exchange rates over the projection period, the slower growth of costs will not be sufficient to prevent Italy's competitiveness from slipping relative to its main European partners. Export performance could thus continue to worsen, but the volume of manufactured exports is nonetheless likely to grow by more than 5 per cent in 1989 and 1990. Import growth will remain high, both because of the decline in competitiveness and strong growth again of aggregate demand. The terms of trade are to improve markedly in the first half of 1989 because of low oil prices. The current account deficit could widen by around $1½ billion between 1988 and 1989, levelling off at close to $6 billion in 1990 (0.7 per cent of GDP) mainly as a result of the projected improvement in the terms of trade.

The main risk affecting these projections is a resurgence of more rapid, and inflationary, growth in domestic demand. Households could maintain rapid consumption growth by continuing to cut their saving ratio or by stepping up wage claims. Investment could increase faster than projected, if enterprises continued to rely heavily on bank credit or increased their profit margins. Should this happen, there could be a resurgence of inflation during 1989 and the current external balance could deteriorate more rapidly than projected.

V. Conclusions

Recent years have seen an impressive degree of industrial restructuring that has sustained Italy's growth despite high real interest rates and a real appreciation of the lira. Since 1983, real GDP has expanded by more than 3 per cent annually, above the average for the rest of OECD Europe. But the regional incidence of stronger growth has been rather uneven, reducing unemployment only in the North and Centre; in the South, the unemployment rate has risen, reaching 20 per cent in the middle of 1988. Price inflation – as measured by the GDP deflator – has come down from 15 per cent in 1983 to a little less than 5 per cent by 1988, the lowest for almost twenty years. While only a rather modest current account deficit has emerged, a significant deterioration in the external balance in volume terms has been partly masked by terms-of-trade improvement.

The policy mix in the 1980s – large budget deficits combined with some tightening in monetary policy – had a significant influence on the pattern of industrial change. The analysis in Part II suggested that the high interest rates and the real appreciation of the exchange rate that resulted from these macroeconomic policies actually spurred the restructuring that led to greater efficiency. In a number of cases, government subsidies made adjustment easier, particularly in large companies. In particular the Wage Supplementation Fund (CIG) – by which the State helped to indemnify workers for loss of earnings due to redundancy or short time in large enterprises that arose from restructuring – and the provision of incentives to scrap obsolete equipment eased adjustment costs both for companies and for their employees. But a number of subsidies designed to be temporary have tended to become permanent, with an increasing budgetary cost. In any case, much of the credit for success belongs to the performance of small and medium-sized enterprises: such companies – which have usually received less State aid and are perhaps less constrained by the extensive regulations that affect large enterprises – responded flexibly to changing conditions. While investment motivated by rationalisation has grown strongly, high interest rates do appear to have restrained capacity-expanding investment. Business construction has remained particularly depressed.

Although State investment and subsidies to industry have been somewhat greater than in other large OECD countries, industrial policy as such has not played a major role in furthering adjustment. Indeed many different policy initiatives have sought to further various goals, and not always very effectively. One important objective has been to increase employment in depressed areas, notably in the South. Earlier attempts relied on subsidising capital-intensive investment, an approach progressively abandoned since the first oil shock in view of the limited employment gains and of the decline in heavy industries. More generally, it is now widely recognised that distorting relative factor prices at the expense of labour – the most abundant factor in the South – was not appropriate. Accordingly, emphasis shifted to reducing state charges on employers. However, large budget deficits and improved terms of trade (which strengthened the financial position of the corporate sector) have recently led the authorities to increase such charges again, reversing much of earlier reductions. Labour-market rigidities are such that regional wage differentials hardly correspond to local labour market conditions: Confindustria calculations even suggest that unit labour costs in the South are actually greater than in the North. It would therefore be appropriate that determination of wage rates take greater account of labour market disparities.

In addition to domestic factors, many of the forces behind the recent stronger growth and lower inflation originated from abroad. Lower oil prices and the depreciation of the dollar provided a terms-of-trade gain of around 3 to 4 per cent of GDP in 1986 and 1987; the fact that import prices in lire are, in 1988, only a little above their 1983 level has obviously helped disinflation. In addition, external demand has grown strongly: the latest OECD estimates suggest that Italian export markets will have grown by more than 30 per cent in real terms in the five years to 1988.

The opportunity provided by such favourable external factors to bring about a major reduction in Italy's large budget deficit was not used as fully as would have been desirable. The general government deficit, estimated at around 10 per cent of GDP in 1988, although down by about 2 percentage points of GDP from the level reached in 1985, is still only a little lower than in the early 1980s. OECD calculations suggest there has been virtually no reduction in the cyclically-adjusted budget deficit. Strong growth and higher tax rates led to a sizeable expansion of tax revenues. Although a significant decline in interest rates worldwide tended to reduce the cost of servicing Italy's public debt, particularly in 1987, the apparently inexorable rise in ratio of the public debt to GDP has continued to increase debt interest expenditure. Also, the rise in interest rates on government bonds – following the taxation of interest paid on new issues of government bonds – inflated gross interest costs. Non-interest expenditure rose faster still. While the average ratio of government expenditure to GDP started to fall in the rest of the OECD from 1983, it has risen almost every year in Italy. Indeed, as noted in the previous Survey, the strong tax revenue growth – partly cyclical but also partly reflecting discretionary increases – has tended to delay the process of reducing government expenditure. Public sector employment has continued to grow and steep wage increases occurred in 1986 and 1987. In the new wage round, one million school teachers were awarded a pay increase of around 30 per cent, spread over the three years 1988-90. In return, an understanding has been reached with the teachers to introduce new mechanisms aimed at increasing productivity and enhancing labour flexibility. In the year to the first quarter of 1988, wages in the public sector rose by 15 per cent. While this can be largely attributed to the timing of three-year wage agreements, the size of recent settlements is a matter of some concern in view of continued high levels of unemployment. It is clearly essential that the general agreement-in-principle to achieve greater efficiency and flexibility in the public sector is actually put into practice. Social security transfers continue to rise strongly, as the real value of some benefits (particularly pensions) has increased.

With the implementation of fiscal consolidation hampered by difficulties often of a political nature, the authorities have had to rely unduly on monetary and exchange-rate policy to support the disinflation process. In the early 1980s, the stance of monetary policy turned restrictive: the higher interest rates and real appreciation of the exchange rate that resulted reinforced downward pressure on inflation. Since then, monetary policy has been heavily influenced by exchange-rate pressures. Periodic realignments within the EMS have led to a significant nominal depreciation of the lira against the ECU, but have not reversed the earlier real appreciation. Although the monetary authorities have placed greater weight on market-oriented instruments, direct controls have been reimposed on two occasions, albeit for short periods of time. Rapid growth in domestic demand and in bank credit during 1987, associated with heavy capital outflows, led the authorities to reimpose, in September 1987, temporary direct controls on both bank lending and on short-term capital outflows. Since credit ceilings were lifted in March 1988, internal credit expansion has been half as fast again as the target and private spending continued to grow strongly. Also, because inflation remained high, the authorities were not, until very recently, prepared to float long-term (i.e. more than five years) fixed-interest debt in lire, creating a significant lacuna in Italian financial markets and making market-oriented monetary policy harder to conduct (see below).

According to preliminary estimates, real final domestic demand grew at an annual rate of over 5 per cent in the first half of 1988. The recovery that started in mid-1986 has therefore strengthened. Employment has increased, stabilizing the unemployment rate. Unemployment remains high, although rates of capacity utilisation have increased markedly, reaching previous cyclical peaks. Wage increases have risen recently; there has been no further deceleration in consumer prices. OECD's estimates indicate GDP growth of 3¾ per cent in 1988. Nonetheless, as tax pressure rises and real interest rates remain high, growth is projected to decelerate to 3½ per cent in 1989, and to 2¾ per cent in 1990. On these projections, and assuming favourable movements in the terms of trade, inflation would ease a little and the deterioration in the external balance would be only modest, with the current deficit rising from about $4 billion in 1988 to about $6 billion in 1990.

But there is a risk that domestic demand will grow more strongly than projected. Continued rapid growth would increase the danger of a resurgence of wage inflation, particularly as the unemployment rate in the North – which tends to determine wages nationwide – is already very low. Moreover, some recent settlements in the public sector, stronger employment growth and the extensive protection enjoyed by those who have jobs may tend to push up wage claims. If such a risk materialises, the Government has announced it would be ready to review fiscal policy applying to different income groups. Also the current external deficit could be larger, putting pressure on the exchange rate and on prices. There has been a loss in external competitiveness since 1986, due to higher wage inflation in Italy than in its trading partners: this could have a greater impact on trade than envisaged in the OECD's projections. During 1986 and 1987 companies were able to absorb higher labour costs partly because of the gains from lower oil prices and partly because of lower profits on export sales: relative export prices remained virtually constant. It may now be more difficult for exporters to absorb further losses of competitiveness.

Dealing with these risks has been made much more difficult by the heavy build-up of government debt. Up to now, increased public debt has been willingly acquired by the private sector: high real interest rates and, until 1986, the shortage of attractive investment opportunities have led companies to reduce indebtedness (and in some cases become real creditors) and households to increase their net financial asset position. According to recent estimates, households net financial assets amounted to almost 150 per cent of household disposable income at the end of 1987, compared with less than 100 per cent at the beginning of the decade. By contrast, investment in real assets – notably housing – has been depressed. Substantial accumulation of highly liquid assets by the private sector has now both increased the vulnerability of the Italian economy and reduced the efficacy of monetary policy.

The economy is clearly particularly vulnerable to attempts by domestic residents – only recently permitted to acquire foreign currency-denominated assets – to diversify from domestic to foreign assets, even though the process of liberalisation may well continue to encourage foreigners to acquire more assets in Italy. Such moves would put heavy pressure on domestic interest rates or on the exchange rate. As about 85 per cent of negotiable government debt either has a maturity of less than twelve months or bears floating rates linked to Treasury bill interest rates, government borrowing operations are particularly sensitive to interest-rate developments. A second source of vulnerability arises from the increased financial wealth of the household sector which may eventually stimulate domestic spending, straining Italy's external position. This risk may well be aggravated by the easier household access to credit that is expected to accompany financial liberalisation.

Monetary policy has been impaired by the fact that households' holdings of short-term and floating-rate public debt are such that higher interest rates rapidly lead to significant increases in household incomes. Estimates suggest that a one percentage point rise in interest rates would increase private sector income by L 7 trillion, subject to a withholding tax of only 12½ per cent. Most of this extra income would go to households. This means that interest-rate increases are much less effective in reducing domestic demand than before. In these circumstances, monetary restriction would work by raising the exchange rate and depressing private-sector investment – private consumption might escape relatively unscathed. The burden of adjustment would thus fall on the open sector of the economy and on real investment, compromising Italy's medium-term growth prospects. The monetary authorities find themselves in this quandary partly because of a failure to diversify debt instruments. When inflation was high, they were naturally reluctant to issue fixed-interest long-term bonds. But now that inflation has come down there is a need to review debt-management policy, with a view to reducing the sensitivity of government interest payments to changes in short-term interest rates. The recent move towards greater reliance on fixed-rate medium-term bonds is therefore to be welcomed as it leads to a more balanced maturity structure of government debt. Consideration should also be given to developing a range of long-term fixed-interest bonds – be they classical, index-linked or convertible (as indeed have just been launched on the market). Nevertheless the fundamental difficulties of monetary policy arise mainly because of the sheer volume of debt accumulated through excessive government deficits over many years. Monetary policy cannot substitute for adequate fiscal action.

At present, the government's medium-term fiscal objective is to reduce the overall deficit by 5.5 per cent of GDP between 1987 and 1992. This would be achieved, first, by eliminating the primary budget deficit (i.e. the deficit excluding interest payments) by 1992, a target the previous plan (adopted in 1986) envisaged reaching in 1990. Secondly, the interest burden is to fall significantly. The bulk of deficit reduction is projected to occur towards the end of the period; as noted more fully in Part IV, the projected decline depends in part on a number of assumptions, in particular that the real rate of interest falls significantly. In addition, the government deficit has persistently exceeded the targets laid down in annual budgetary exercises. However, growth in 1988 and 1989 now seems likely to be stronger than originally envisaged in Plan, generating higher-than-estimated tax revenues. It is clearly important that such higher revenues be used to reduce the deficit, and not to increase expenditure – as indeed prescribed by the Finance Act. Moreover, the recent buoyancy of investment would suggest that measures aimed at reducing the budget deficit quickly would release savings for productive use and would thus be particularly opportune. Rapid and sizeable reductions in the budget deficit would exert downward pressure on interest rates which remain higher than elsewhere, and so reduce the danger of an explosive build-up in public debt and tend to limit the growth in household interest income. Finally the short-run demand-depressive effect of fiscal adjustment would be much more easily absorbed at a time when private demand is growing rapidly as now. Yet the 1989 Budget provides for little reduction in the cyclically-adjusted budget deficit. A more substantial reduction would seem appropriate given the prospects for strong growth in the period immediately ahead. This would permit faster realisation of medium-term objectives, and further subsequent progess.

As noted in Part IV, the authorities intend to reduce the budget deficit by higher taxation and by a reduction in the share of government expenditure in GDP. They attach particular importance to reducing tax evasion, generally held to be more widespread in Italy than elsewhere particularly among the self-employed. Nevertheless the tax/GDP ratio has already risen significantly in recent years, although it is still lower than in many other OECD countries. And high tax rates can weaken economic performance and reduce the tax base: for instance, the relatively heavy social insurance charges on employers in Italy may discourage employment and divert workers to the underground economy. Although the choice between tax increases and expenditure reduction as a means to deficit reduction is partly political, the *quality* of public expenditure is obviously extremely important. The examination of industrial policy in Part II showed that government aid to industry was not always effectively applied. There needs to be greater coherence and transparency in the vast array of taxes, subsidies and other measures that affect industry. Much the same applies to other transfer payments. More seriously, perhaps, government proposals for the much-needed rationalisation of expenditure are rarely enacted intact, measures to increase spending often being more palatable to legislators than measures to cut it – witness attempts to reform pension entitlements in 1986. Moreover, the quality of a number of services provided by the public sector is poor, and productivity low. The need for a more efficient allocation of resources underlines the importance of controlling public spending. Better expenditure control – in the administration and by the legislature – will also be required if early and decisive reductions in the budget deficit are to be achieved. Measures recently adopted, concerning the suppression of secret voting in Parliament, the reform of budgetary procedures as well as of government accounting rules constitute decisive first steps in this direction. Further progress will be essential if overall economic performance is to reflect fully the flexibility and responsiveness demonstrated by the private sector in Italy during the last five years.

Notes and references

1. For a special study of Italy's medium-term public sector problems, see OECD, *Economic Survey of Italy*, June 1985, Part I, pp. 8-31.
2. Including financial transactions which for the most part consist of subsidies to specialised lending institutions and quasi-public enterprises and changes in local authorities' position *vis-à-vis* the banking sector.
3. See "Il Debito Pubblico in Italia 1961-1987", *Relazione del Direttore Generale alla Commissione parlamentare di vigilanza*, Ministero del Tesoro, Direzione Generale del Debito Pubblico, Rome, 1988.
4. In 1985, the last year for which national accounts are available on the old basis, debt was 92 per cent of GDP (78 per cent on the new basis).
5. See L. Spaventa, "Introduction: Is there a public debt problem in Italy?" in P. Giavazzi and L. Spaventa, *High public debt: the Italian experience*, Cambridge University Press for Centre of Economic Policy Research, 1988.
6. The primary surplus (expressed as a percentage of GDP) must exceed the product of the initial debt/GDP ratio and the difference between the nominal rate of interest and GDP growth, if the debt/GDP ratio is to be reduced. For a fuller discussion of debt dynamics under different assumptions, see Annex II of the OECD, *Economic Survey of Ireland*, December 1987, pp. 101-107.
7. The view that the public sector directly crowded out private expenditure was challenged starting from the late 1970s on the grounds of the positive impact that the government deficit may have had on the financial balances of firms or households. See, in particular: Banca Commerciale Italiana, *Spesa pubblica e sviluppo dell'economia, i problemi dello spiazzamento, in generale e con particolare riferimento all'esperienza Italiana*, Ed. di Communità, Rome, 1983; M. Monti, B. Siracusano and P. Tardini, "Spesa pubblica, finanziamento del disavanzo e crowding-out, l'intermediazione finanziaria privata", Banca Commerciale Italiana, 1983.
8. F. Cavazzuti, "The enlarged public sector deficit: A preliminary analysis of its effects on prices and quantities", *Review of economic conditions in Italy*, No. 2, 1979.
9. See *Ricchezza finanziaria, debito pubblico e politica monetaria*, Ministero del Tesoro, 1987, pp. 83-104.

10. Up to April 1973, fixed-interest nine-year government bonds were regularly issued: none has been issued since with the exception of one issue in October 1978. From April 1973 to June 1977, four-year bonds were issued, followed by five-year bonds from July 1977 to October 1979. Since then fixed-interest issues have been episodic, with five-year bonds being issued in March 1986, January 1987 and November 1988.

11. Nominal interest rates deflated by the consumer price increase from the same quarter of the previous year.

12. From 1978, income from government securities was totally exempt from income taxes, whereas income from bank deposits was taxed, encouraging households to shift savings to the public sector. From 1986, however, interest earned *on new issues* was subject to a flat-rate tax of 6.25 per cent, raised to 12.5 per cent from September 1987. The introduction in 1977 of medium-term Treasury certificates with rates pegged to those of Treasury bills also proved attractive. The Treasury still has an automatic line of credit with the Bank of Italy up to a maximum of 14 per cent of total budget expenditure for the year. It is drawn on at times when the Treasury, which sets a ceiling on the interest rate on its flotations, is unable to place all the securities issued.

13. The impact of the budget deficit on interest rates has been discussed in a number of papers, in particular: Tullio Jappelli, "Risparmio, tassi di interesse" and "Politica fiscale, l'esperienza italiana", *La spirale del debito pubblico*, Il Mulino 1988; F. Modigliani and T. Jappelli, "The determinants of interest rates in the Italian economy", *Review of economic conditions in Italy*, N° 1, January-April 1988.

14. According to Bank of Italy estimates, a 1 percentage point increase in interest rates reduces investment in plant and equipment by 0.7 per cent in the short run.

15. When interest payments are taxable, the condition for a non-explosive development in the debt/nominal GDP ratio is that the growth of GDP exceeds the nominal interest rate *net of tax*. In the absence of full shifting, this is an easier condition to satisfy than the growth of GDP exceeding the nominal interest rate which applies in the absence of taxation.

16. In the context of liberalisation of exchange controls, the compulsory non-interest-bearing interest-exempt deposit requirement (10 per cent before it was lifted) for securities investment abroad was abolished in May 1987.

17. A number of commentators have suggested that alternative instruments could have been used. Index-linked bonds would have protected investors from inflation, while fixing *real* interest rates. Another possibility would be convertible bonds. For a discussion of these issues, see Spaventa (*op.cit*), p. 21.

18. See EEC, "The development of market services in the European Community, the United States and Japan", *European Economy*, N° 25, September 1985.

19. The Wage Supplementation Fund (CIG) is a fund which provides compensation increasingly out of public resources for industrial and construction sector employees who have lost their jobs as a result of temporary difficulties in their firms (ordinary measures), sectoral or local difficulties or restructuring (extraordinary measures).

Those registered with the CIG receive benefits equal to 80 per cent of their contractual wage and often remain legally in the employment of their firm. Registration with the CIG is in principle temporary, though for many wage-earners it has in fact proved to be permanent. The number of hours for which benefit is paid rose first of all in 1975, to the equivalent of 202 000 individuals, and then again as of 1980 – which was the start of the most vigorous restructuring phase in industry – to reach a maximum of 473 000 people in 1984. The role of the CIG will be discussed more fully below.

20. Measurement of TFP is hampered by uncertainty with regard, for example, to the definition of capital stock or the measurement of output in services. With the new technology incorporated in capital having in all probability shortened its useful life, scrapping can be expected to increase, which means that sales of capital stock based on a constant rate assumption are overestimated. For further details, see A. Steven Englander and Axel Mittelstadt, "Total factor productivity: macroeconomic and structural aspects of the slowdown", OECD, *Economic Studies*, N° 10, Spring 1988.

21. See A.S. Englander and A. Mittelstadt, op. cit. in note 20.

22. The upturn in TFP is largely a reflection of the trend in capital productivity which, after falling at an annual rate of 1 per cent between 1973 and 1983, has since been increasing at a rate close to 1 per cent per year. The improvement in TFP was particularly marked in the paper, basic metals, chemicals and machinery and equipment industries, where both labour and capital productivity picked up. In textiles, on the other hand, which is a very labour-intensive industry where modernisation of technology and machinery came late but has been very rapid, both capital productivity and TFP have declined. See Table 21 in OECD, *Economic Outlook*, N° 42, December 1987, and Confindustria, *L'industria italiana*, VII Rapporto, 1986.

23. The impact of restructuring is calculated as the ratio of the effective unit costs to the hypothetical costs which would have been incurred with no change in technology. The change in the indicator reflects the effects of both the new mix of factors of production and technical progress. The estimates are based on the effective cost of inputs and do not take into account the additional savings deriving from the *indirect* effects that a bigger increase in costs in a particular industry would have had on the other stages of production. See I. Cipoletta, A. Heimler, G. Calcagnini, "Restructuring and adjustment in Italian industry", *Review of economic conditions in Italy*, no.3, September-December 1987, Banco di Roma; A. Heimler, "Ristrutturazione e produttività nei paesi industriali", *Rivista di Politica Economica*, 1987.

24. In other industries, such as leather and shoes for example, the fact that costs have fallen very little, or even remained stable, probably masks a shift towards higher quality of production prompted by competition from the newly industrialising countries.

25. For further details of this analysis, see Technical Notes in Annex I.

26. "Revealed" comparative advantage is calculated as the share of a product in the country's total exports divided by the share of the said product in world exports. The analysis is based on the nomenclature used in: OECD, *Structural adjustment and economic performance*, 1987, chapter 7. It singles out industries which are: *i)* resource-intensive; *ii)* labour-intensive; *iii)* have big economies of scale; *iv)* produce differentiated

goods; *v)* are research-intensive. Additional information on the pattern of both production and imports – with the latter a measure of "apparent relative disadvantage" – is contained in Table A2, Annex I.

27. The share of financial investment in total investment by non-financial enterprises has evolved as follows:

	Italy	France	Germany	United Kingdom	Japan	United States
1973-74	37	32	18	..	..	33
1979-80	45	39	26	30	50	34
1984-85	62*	45	28	43	32	21

* 1983
Source: OECD, *Financial accounts of non-financial enterprises, 1987.*

28. Where the Italian productive sector is concerned, it is difficult to establish a relationship between the overall trend of the K/L ratio and the trend in the relative prices of factors of production. During the period 1970-79, the rise in the K/L ratio slowed more markedly than elsewhere, while the increase in labour costs was amongst the highest in the OECD area, and constantly accelerating, and real interest rates remained negative. This phase was in fact the result of the break in the very substantial investment in the South in heavy industry that the authorities had encouraged during the previous period.

29. In some of these sectors, production capacity is calculated indirectly as the index of industrial output *divided* by the degree of factory utilisation. See P. Buygues, P. Goybet, "The determinants of supply in industry in the Community", in EEC, *European Economy* N° 5, September 1985. The estimates of returns on investment contained in this Study show that the gross rate of return on investment (gross operating surplus divided by gross fixed capital stock) fell in the expanding, high-demand sectors between 1972-73 and 1981-82. This phenomenon, which was less marked in Italy than in other European countries, may have discouraged the flow of capital to these industries and reduced firms' investment resources. On the other hand, there was probably a pick-up in the gross return on capital in the traditional sectors, and this would have had a favourable impact on investment.

30. Between 1971 and 1982 the number of SMEs increased by 30 per cent, while enterprises with more than 100 employees grew by only 6 per cent; see Confindustria, "Risorsa Piccola Industria", October 1987. Purchases of raw materials and intermediate products increased as a percentage of turnover. The sectors where sub-contracting is most common are engineering, office equipment, electrical machinery and transportation, and also the traditional industries (shoes, in particular).

31. If the numbers employed who are in fact compensated by the CIG (which is mainly in large enterprises) are excluded, the difference remains of the same order of magnitude.

32. See A. Bianchi, G. Gualtieri, "The external growth of firms through merger and acquisition: the Italian experience, 1983-1986", in Nomisma, Laboratorio di Politica Industriale, *Working Papers*, February 1987.

33. Capital expenditure by general government as a percentage of GDP:

	Total capital expenditure			*of which:* Direct investment		
	1973	1980	1987	1973	1980	1987
Italy	3.3	4.2	5.1	2.6	3.1	3.5
Germany	5.2	5.1	3.6	3.6	3.4	2.3
France	3.6	3.5	3.2	3.3	3.1	3.1
United Kingdom	6.4	3.2	2.5	5.0	2.4	1.6

Sources: ISTAT and OECD, *National Accounts.*

34. The financial contributions that do not appear in the consolidated accounts of general government are shown in the cash budget for the State sector, which comprises central government and certain public sector entities, and records more transactions than the national accounts (For a definition of the different entities of the public sector, see table A4 in Annex I).

35. This analysis is based on studies by the Technical Commission on Public Expenditure of the Ministry of the Treasury, the Nomisma Institute, the Posts and Telecommunications Authority, and the Research Centre of Confindustria, which co-ordinated the research. See *Stato ed Economia – Istituzioni, efficienza, sviluppo,* 3 volumes, Edizioni del Sole 24 Ore, April 1988.

36. This analysis draws upon the findings of the studies of Italian industry and industrial policy carried out by the Centro Europa Ricerche (CER) and the Istituto per la Ricerca Sociale (IRS) published between 1986 and 1988. The main conclusions of the 1986 report are summarised in *Quale strategia per l'industria?* Il Mulino.

37. See EEC, "The Economics of 1992", *European Economy*, No. 35, March 1988.

38. This does not include the reductions in profits tax for enterprises located in the Mezzogiorno, which are difficult to quantify exactly but do not amount to much.

39. See F. Siracusano, C. Tresoldi, G. Zen, *Domanda di lavoro e trasformazione dell'economia del Mezzogiorno*, Temi di discussione, Research Department, Bank of Italy, No. 83, December 1986. For further details on regional intervention see: Pippo Ranci, "Italy, the Weak State" in *Managing Industrial Change*; *I trasferimenti dello Stato alle imprese industriali negli anni settanta*, Il Mulino, 1983, and *Mezzogiorno: a possible take-off*, Confindustria Research Centre, June 1987.

40. Confindustria has estimated the rate of social insurance contributions after subsidies from general revenue by region:

Rate of employers' social insurance contributions in manufacturing

	1981		1985		1988	
	North-Centre	South	North-Centre	South	North-Centre	South
Gross rate	40.8		41.6		45.1	
Rate after general revenue subsidies*	30.2	27.0	32.4	29.8	39.0	37.5

* The rate for 1981 and 1985 is for male workers only; a lower rate existed for female workers until 1985. Since then the rate has been the same for both men and women.
Source: Confindustria.

41. The GEPI manages industrial holdings. It is complemented by the Restructuring Fund set up in 1977 and by the Istituto Mobiliare Italiano (IMI).

42. It is estimated that from June 1982 to June 1985, 576 applications, totalling approximately L 4 500 billion, were submitted to the Fund; 340 projects worth to L 1 700 billion were approved, representing nearly 13 per cent of total expenditure on industrial R & D. However, actual outlays were smaller – less than L 1 200 billion, concerning 268 projects.

43. Over a three-year period, from 1982 to 1984, 627 programmes costing L 5 000 billion were submitted; two-thirds of them were approved, representing 72 per cent of the initial cost. By the end of 1986, approved programmes amounted to over L 7 000 billion, or 1 per cent of GDP.

44. Non-recoverable State grants represented 25 per cent of the cost of machinery (32 per cent for enterprises located in the Mezzogiorno). In 1984 total investment in machinery amounted to L 450 billion, about a quarter of which in the form of State aid. Two years later, at the end of 1986, these amounts had quadrupled. For a detailed assessment of innovation policy, see F. Momigliano, *Le leggi della politica industriale in Italia*, Il Mulino, 1986.

45. See P. Bianchi, "The Privatization of Italian Public Industry" in Nomisma, Laboratorio di Politica Industriale, *Working Papers*, November 1987. This analysis is based on IRI data. The enterprises returned to the private sector by the GEPI are not included in the figures.

46. EEC, 1988, *op. cit.*; see Diagram 13, OECD, *Economic Survey of Japan*, July 1988.

47. The households' appropriation account set out and discussed in the Survey was drawn up by the OECD Secretariat on the basis of ISCO and Bank of Italy estimates. Figures refer to the household sector as defined in the national accounts, including households as such, agricultural enterprises employing less than 20 workers, enterprises with less than 50 workers in the services sector and less than 100 workers in industry.

48. Between the first half of 1984 and the second half of 1986, the inflation rate was brought down from 12.5 to 4.5 per cent, substantially diminishing the erosion of households' financial assets.

49. It is not possible on the basis of the Italian national accounts to break down the volume of gross fixed investment by agents. Gross fixed general government investment reportedly increased by 8.5 per cent at current prices in 1987. If this increase is deflated by total investment (2.8 per cent), the volume of general government investment may be roughly estimated to have grown by 5.5 per cent.

50. In April 1988, the capacity utilization rate reached a historic high of 78.6 per cent. In the chemical industry, precision tools and clothing, it was over 80 per cent.

51. In the Italian national accounts, changes in inventories and the statistical error are merged.

52. The change in the industrial production index excluding construction differs from that of value added in manufacturing. In 1987, the index rose by 3.8 per cent compared with 4.3 per cent for value added.

53. These changes concern the statistics calculated from the censuses (panel A of Table 16), which serve as a basis for the national accounts and relate to the concept of a standard unit of labour (see OECD, *Economic Survey of Italy*, August 1987, Annex I). There is also another series which derives from the quarterly surveys (panel B of Table 16) and concerns an actual number of people surveyed.

54. This rate is calculated on the basis of a survey conducted in the first week without a public holiday in each quarter.

55. The wage equations calculated by the Bank of Italy show that wage developments are more closely related to the unemployment rate in the North-Centre than to the national unemployment rate.

56. Cost-of-living index for manual and non-manual workers.

57. The general government triennial wage agreements covering the period 1986-1988 were not concluded until 1987 and early 1988: they were applied retroactively with effect from 1986.

58. According to Bank of Italy estimates for 1987, tourism receipts were 6.5 per cent down on their 1980 level at constant prices, whereas spending by Italian tourists abroad more than doubled during the same period.

59. See the section on fiscal policy in OECD, *Economic Survey of Italy*, August 1987, pp. 21-22.

60. This percentage is calculated on the basis of the official GDP growth forecast (of a nominal increase of 8.5 per cent) incorporated in the Finance Act.

61. Since, however, the bulk of medium and long-term securities have interest rates indexed on short-term bills, the effects of this change did not have a significant impact on the pattern of interest payments.

62. See the "Economic and financial programming document of the 1988 Finance Act". The ultimate objective of this programme is less ambitious than was the previous programme adopted in 1986, which envisaged achieving primary budget equilibrium in 1990.

63. It is estimated that the purchasing power of per capita wages in the public sector grew by an average of 3.6 per cent per year on average during 1987-88.

64. It should be noted that imposing limits on commitments would eventually constrain *cash* expenditure only if applied each year. In Italy, expenditure committed but not spent in a given year can be actually spent during the following four years.

65. See D. Franco and N. Sartor "Alcune considerazioni sugli effetti di capitalizzazione determinate dalla tassazione dei titoli di Stato", Banca d'Italia, *Temi di discussione*, N° 102, July 1988.

66. It would seem that a number of these establishments were able to negotiate bank loans at below base rate and then reinvest on the market at base rate the funds raised.

67. The amount of these repurchase agreements was particularly high, reaching L 10.7 billion during the first 20 days of May, while end-June saw a further L 11.5 billion of repurchase agreements. These transactions were temporary and they ended on the date of auction of the securities.

Annex I

Industrial adjustment: background information

TECHNICAL NOTES

1. Export performance: constant market share analysis

The constant market share analysis for Italy was carried out for trade in manufactures and was based on current-price data for the period 1966-1986[1].

The following main findings (summarised in the Table below) emerged:

- The differential between the growth of world imports and that of Italian exports was positive up to 1979, except between 1972 and 1974 when it became negative as a result of the first oil shock, whose effects were reflected in a substantial negative residual. Nonetheless, product specialisation and geographical distribution were still satisfactory. From 1979 to 1984, the differential has been almost always negative, denoting losses in market share (in nominal terms).
- The geographical distribution effect was distinctly positive up to 1979-1980. Italian exporters thus seem to have taken full advantage of demand growth in those areas where it was most buoyant. After 1982, however, there was a trend reversal and the geographical distribution effect became strongly negative.
- The commodity composition effect was on the whole weaker[2]. Positive up to 1979-1980, it has since been negative, suggesting that Italian exporters have been unsuccessful in channelling production towards goods for which world demand was most buoyant. In 1985-1986, the commodity composition effect becomes positive again, revealing that the industrial restructuring undertaken in the early 80's has brought about an adequate change in the specialisation of exports.
- The trend of the residual reflects the impact of other factors on export performance, such as overall production efficiency and, inter alia, the competitive position of Italian goods in terms of prices and relative costs, along with non-quantitative factors.

Closer analysis of geographical distribution shows that growth of exports to developing countries, and in particular the OPEC countries, had a markedly positive impact from 1973 to 1981. During this time, Italian exporters were able to exploit the expansion in these markets

Constant market share analysis

Percentage changes and percentage points, annual rates

	Italian export growth[1]	Market growth[2]	Difference	Geographical distribution effect	Commodity composition effect	Residual[3]
1971-1972 / 1966-1967	14.6	14.6	2.0	1.4	0.8	–0.2
1974-1975 / 1971-1972	24.8	27.0	–2.2	1.2	0.3	–3.7
1979-1980 / 1974-1975	18.6	16.2	2.3	1.6	0.3	0.4
1981-1982 / 1979-1980	–0.7	1.1	–1.9	0	–0.3	–1.5
1983-1984 / 1981-1982	–1.0	0.6	–1.6	–2.0	–0.8	1.2
1985-1986 / 1983-1984	10.0	8.8	1.2	–1.0	0.5	1.8

1. In value terms.
2. Export markets for manufactures.
3. The residual reflects *inter alia* changes in overall competitiveness (in terms of prices, costs and non-quantitative factors).
Source: OECD Secretariat.

generated by major resource transfers between the industrialised and oil-producing nations. At the same time, the share of this group in total Italian exports went up from 20 to 30 per cent. Since 1982 the positive contribution has become weaker.

The contribution of Italian exports to Italy's three main trading partners – Germany, France and the United States – which together accounted for an average of 40 per cent of total exports over the period 1966-1985 – was positive over the whole period, except in 1981-1982 when these countries' responded to the second oil shock by reining back imports. The positive effect of this component was also significantly reduced at the time of the first oil shock.

Exports to a third group of partner countries – Austria, Switzerland, United Kingdom, Belgium, Netherlands and Spain, which between them accounted for 24 per cent of total exports – had a markedly negative impact throughout the period.

Breaking down the effect of the commodity composition of exports poses problems because of the great diversity of the products included in the main categories. The growth of exports of a first category of products – cars, chemicals, oil refinery products – made a positive contribution throughout, but a much smaller one over the 1980s. On the other hand, a second group of products – textiles and non-electrical machinery – made a negative contribution almost throughout, which reveals the unfavourable effect of the specialisation of Italian exports in products for which world demand is not very buoyant.

There is a strong positive correlation between changes in Italian export shares and changes in the relative expansion of Italy's export markets, testifying to the flexibility of the geographical pattern of exports. But the correlation is much weaker in the case of the commodity structure of exports, suggesting that commodity composition was not adjusted on the same scale to changes in demand. This is clearly because it is more difficult and more costly for an economy to change the structure of production than to alter the geographical pattern of exports.

II. Local public transport

The poor quality of local public transport in Italy is primarily due to the low level of investment and the deterioration of labour productivity.

Investment in local public transport in fact declined in real terms over the period 1982-86 because of financial and institutional constraints, and the quality of supply suffered accordingly. Long lags occurred between the allocation of investment resources by the National Transport Fund and their disbursement by the Regions. There are several reasons for this: the majority of regions have not developed the medium-term infrastructure plans needed in order to invest the resources allocated by the National Transport Fund. Moreover, until the institution of a centralised exchequer account, the regions delayed disbursing these resources for as long as possible so as to boost their finances.

The lack of a proper investment policy along with a decline in the efficiency of labour between 1982 and 1986 meant that labour productivity fell in most urban areas, except Milan, as a result of the shorter working hours negotiated in wage bargaining agreements. At the same time, the proportion of administrative employees expanded. The capital stock (i.e. vehicles in circulation) was, however, used more intensively. All in all, the cost per vehicle-km and per passenger rose in all the regions in the 1980s.

Productivity and profitability of public transport in selected Italian towns

Ratio 1986/1982

	Firenze	Milano	Vicenza	Palermo	Taranto
Km travelled/vehicles	101	109	90	113	90
Km travelled/nos. employed	95	113	100	97	97
Administrative personnel/Travelling personnel	109	116	97	82	90
Total cost/km travelled	119	123	111	107	103
Total cost/no. of passengers	129	134	125	181	126
Revenue/no. of passengers	90	94	89	134	93

Source: Centro Studi Confindustria, *Stato ed Economia – Istituzioni, efficienza, sviluppo*, Edizioni del Sole 24 Ore, April 1988.

A comparison of the profitability of local public transport in Rome and Milan with that in other major European cities suggests that Italy's poor performance may largely be due to the low fares charged in Italy. This raises the question of pricing policy. It is important to make a distinction in the management of public transport between economic and political considerations. Economic criteria must clearly be paramount with a view to curbing costs and allowing investment resources to be raised partly on the financial markets. Subsequently, the cost of fares policy to the public purse would need to be properly quantified.

Notes and references

1. For a description of the methodology followed, see Leamer-Stern. In the present case, fourteen areas of export destination have been selected for each of the twenty-two industries chosen according to the ISIC classification, category 3, comprising a wide classification of manufactured goods. The table gives the average rates of growth of Italian exports and world imports and a breakdown of the changes over the periods under review.
2. These results echo the findings of earlier similar analyses. See Savona, Rebecchini, "Il declino della CEE nel commercio internazionale: La dimensione del fenomeno ed alcuni fattori strutturali", *Contributi alla ricerca economica*, Banca d'Italia, 1983; and *Rapporto sulle esportazioni italiane*, Credito Italiano, 1983.

Table A1. **Structural shifts 1968-1987**

Annual averages

	GDP growth[1]			Employment growth[2]			% of total GDP[3]				% of total employment[2]			
	Old basis		New basis	Old basis		New basis	Old basis		New basis		Old basis		New basis	
	1973/1968	1983/1973	1987/1983	1973/1968	1983/1973	1987/1983	1973	1983	1983	1987	1973	1983	1983	1987
Agriculture	0.1	2.0	0.1	–4.9	–2.5	–2.1	7.8	6.0	5.3	4.0	16.4	11.9	12.3	11.0
Total industry	5.2	1.3	2.4	0.2	–0.3	–2.0	42.2	40.1	35.7	33.7	37.9	34.4	32.9	29.7
Manufacturing	6.1	1.9	3.5	1.0	–0.4	–2.0	30.0	27.1	24.6	23.2	27.9	25.3	24.1	21.7
Construction	1.2	–0.2	–2.2	–2.0	–0.3	–2.3	7.5	7.8	6.6	5.4	9.1	8.2	8.0	7.1
Traded services	5.2	2.7	4.2	1.6	2.4	3.1	38.3	40.7	44.8	48.0	29.8	35.5	37.4	41.2
Non-traded services	3.5	1.6	1.5	3.6	2.1	1.5	11.7	14.1	12.9	12.9	13.5	15.7	17.4	18.0
Total economy	4.6	1.9	3.0	0	0.6	0.6	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Note: Old national accounts basis : 1970 prices.
New national accounts basis : 1980 prices.

1. In volume.
2. On the new basis, employment is expressed in "labour units".
3. At current prices.

Sources: ISTAT; OECD, *National Accounts.*

Table A2. **Structure of output and imports of main OECD countries**

A. Relative structure of output[1]

	Italy		Germany	France	United Kingdom	United States	Canada	Japan
	1970-72	1984-86	1984-86	1984-86	1984-86	1984-86	1984-86	1984-86
Industry[3]								
Resource-intensive	0.76	0.78	0.64	1.00	0.93	0.83	1.09	0.72
Labour-intensive	1.21	1.47	1.20	0.94	1.06	1.07	0.96	1.02
Scale-intensive	1.05	1.01	1.17	0.91	0.90	0.97	1.13	1.08
Differentiated goods	1.14	1.13	1.25	1.09	1.13	1.12	0.59	1.55
Research-intensive	1.31	0.99	1.34	1.31	1.43	1.65	0.87	0.98

B. Relative structure of imports[2]

	Italy		Germany	France	United Kingdom	United States	Canada	Japan
	1970-72	1984-86	1984-86	1984-86	1984-86	1984-86	1984-86	1984-86
Industry[3]								
Resource-intensive	1.14	1.35	1.18	1.05	1.08	0.84	0.42	1.70
Labour-intensive	0.79	0.74	1.14	1.01	0.96	1.03	0.69	1.01
Scale-intensive	0.94	0.95	0.85	0.98	0.83	1.10	1.52	0.63
Differentiated goods	1.02	0.85	0.86	0.93	1.02	1.14	1.07	0.64
Research-intensive	1.08	1.03	1.11	1.05	1.34	0.77	1.10	1.19

1. The relative structure of output is the share of product i in total output of country j *divided by* the share of that product in the output of 13 OECD countries.
2. The relative structure of imports ("revealed" comparative disadvantage) is the share of product i in total imports by country j *divided by* the share of that product in OECD area imports.
3. Examples of products falling into the above categories are: food products, aluminium smelting *(resource-intensive)*; textiles and clothing *(labour-intensive)*; chemicals, steel *(scale-intensive)*; machine tools *(differentiated goods)*; electronics, aeronautical construction *(research-intensive)*.

Source: OECD Secretariat.

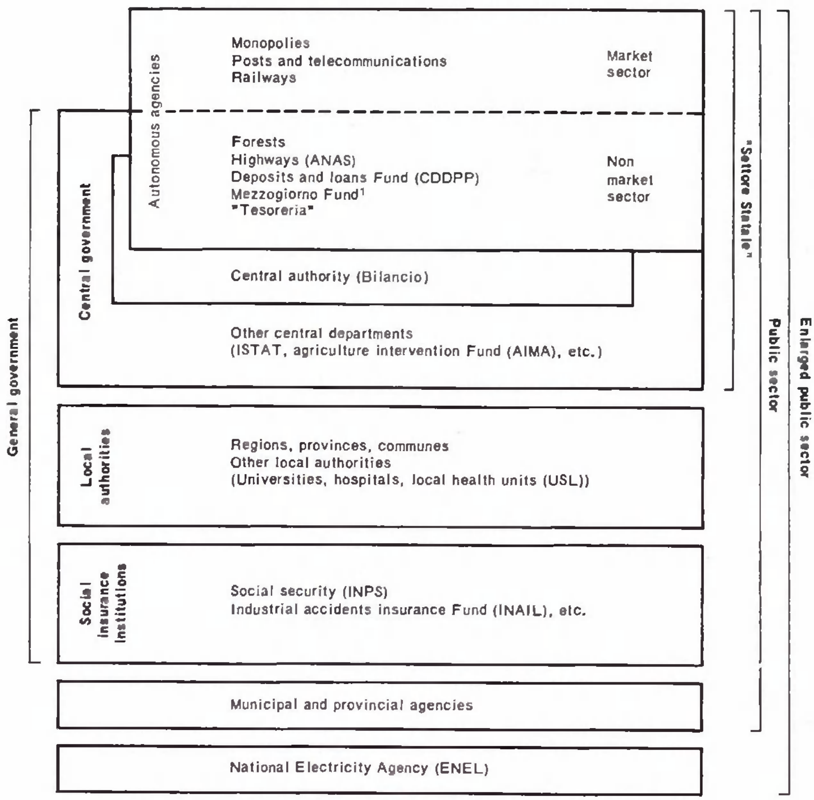
Table A3. **Adjusted intra-industry trade index, all products (averages)**

	1964	1967	1973	1979	1986	1987
Italy	**48**	**45**	**54**	**47**	**53**	**56**
Average for 5 European countries	53	59	64	66	71	71
Germany	45	53	59	59	70	72
France	61	65	68	67	72	74
United Kingdom	43	53	68	75	77	78
Belgium-Luxembourg	59	62	63	67	67	67
Netherlands	59	62	62	62	67	65
United States	46	47	45	48	71	..
Canada	34	43	53	53	60	61
Japan	19	22	22	20	28	29

Note: This table shows the percentage of intra-industry trade in total trade with the rest of the world. Calculated on SITC (Rev. 2) 3-digit level; adjustment is made for aggregate trade imbalances of the respective country. For a more detailed analysis see OECD, *Structural Adjustment and Economic Performance*, 1987, Chapter 7, Annex B.

Source: OECD Secretariat.

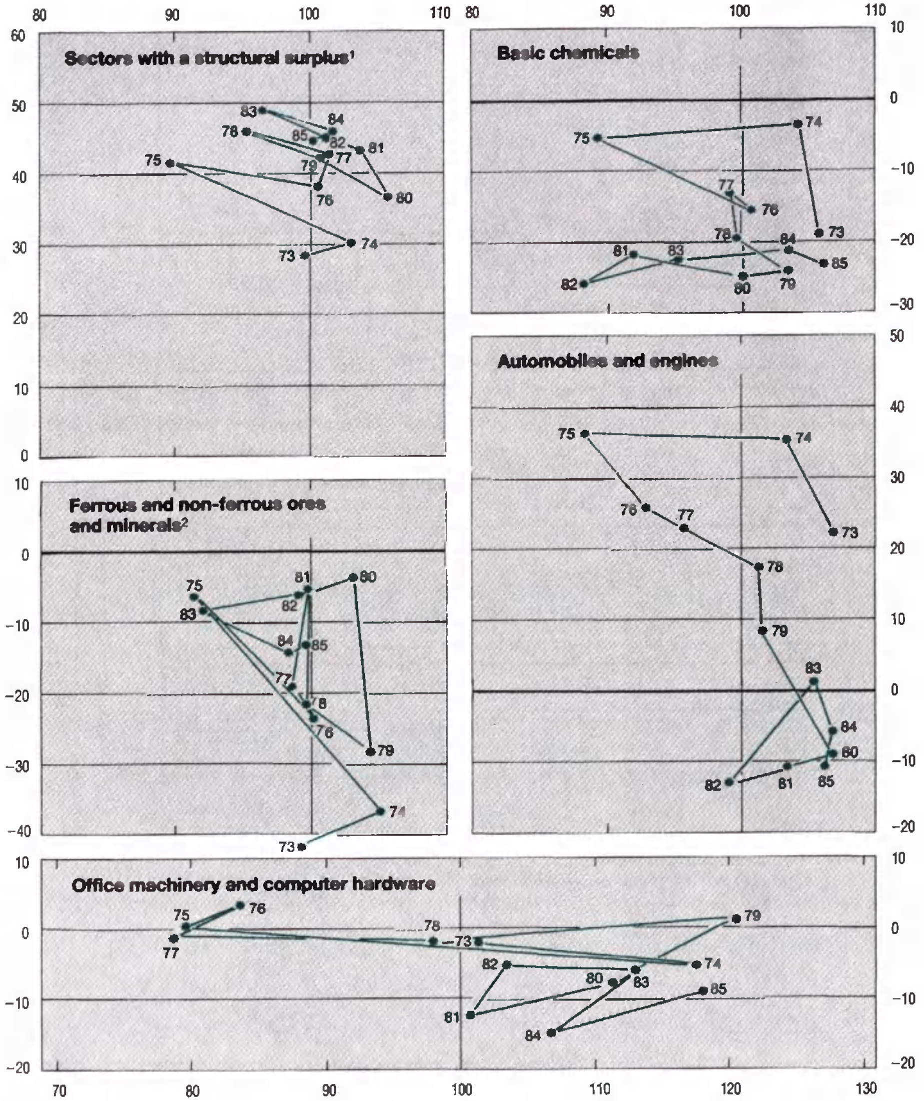
Table A4. **The public sector in Italy, definitions**



1. The Mezzogiorno Fund was wound up in 1984.

N.B. Public administrations on a national accounts basis exclude the "Tesoreria", the Deposits and Loans Fund and the Mezzogiorno Fund.

Diagram A.1. **TRADE BALANCES AND CAPACITY UTILISATION BY SECTOR**

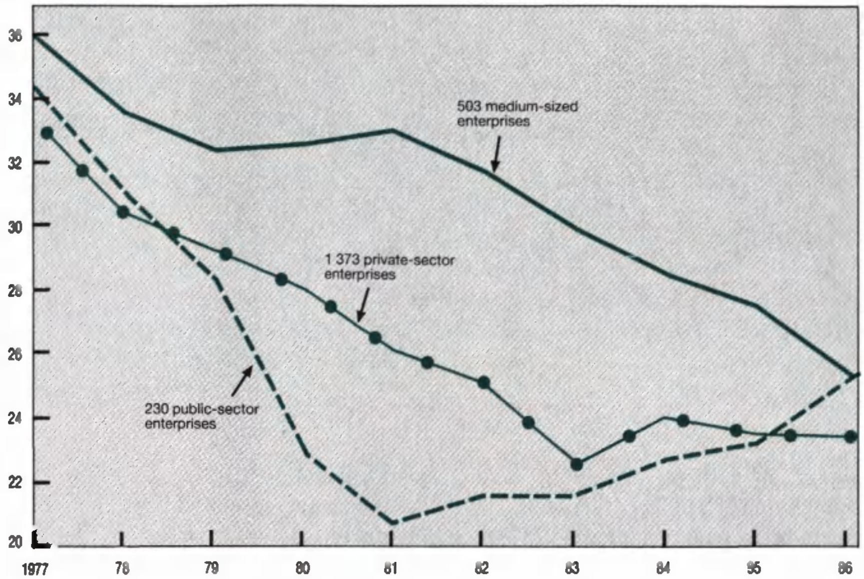


Note: *Abscissa:* Index of capacity utilisation by sector, average 1966-85 = 100.
Ordinate: Sectoral trade balance as percentage of total trade balance, at current prices.

1. Non-metallic minerals, metal products, agricultural and industrial machinery, textile products and clothing, leather and footwear, wood and furniture, rubber and plastic products, household electrical appliances and television sets.
2. Excluding gold imports.

Source: Banca d'Italia, *Relazione Annuale,* 1985.

Diagram A.2. **VALUE ADDED AS A PERCENTAGE OF OUTPUT**
(Percentages at constant prices)



Source: MEDIOBANCA, *Dati cumulativi di 1 603 Società Italiane*, 1987.

Annex II

Main policy measures

1987

FISCAL POLICY

7th January

Signing of a three-year public sector pay agreement for the period 1986-1988 and concerning some 250 000 civil servants. It provides for pay increases of 8 per cent a year, with 65 per cent being paid in January 1987 (including the retroactive payment for 1986). Fewer increments for length of service to be awarded automatically.

22nd January

Government proposal to reform personal income tax (IRPEF) scales, starting in 1988. The tax concessions would amount to L 4 700 billion in that year and L 6 500 billion in 1989, to be financed from the new tax on government securities and a 25 per cent flat-rate tax on revalued company assets. These measures would more than compensate for fiscal drag effects since the last rate adjustment, with the bulk of the benefit going to to individuals with middle and high incomes. Corporate depreciation allowances would also be improved.

27th August

Decree implementing a series of restrictive budget measures:

- Prices of oil products to be increased (with gasoline up L 60 a litre, and domestic heating fuel up L 20 a litre);
- VAT raised by 4 points on cars, furniture, household electrical appliances, and by 2 points on television sets, radios, and hi-fi, camera and photographic equipment, these increases to remain in force until 31st December.
- Advance payments of corporation tax (IRPEG) and local income tax (ILOR) raised from 92 to 100 per cent and payable by 30th November (instead of 31st December). The date for payment of the advance on tax on bank interest brought forward from 30th November to 31st October, and payment must now be in full.

24th September

The draft Finance Act for 1988 approved by Parliament. The main provisions are as follows:

- One-point rise in VAT rates from 1st January 1988;
- Road tax and supertax on diesel fuel to rise by 25 per cent from 1st January 1988;
- 25 per cent rise in insurance tax;
- Renewal of the law on VAT liability of all automobile purchases;
- Stamp duty on stockmarket transactions to be doubled;
- Personal income tax (IRPEF) rates to be revised to benefit single-income households;
- Renewal of the law lowering tax on the purchase and sale of real estate;
- The deficit on the sickness insurance scheme (INPS) to be cut by L 3 500 billion: the health tax to remain at 7.5 per cent, but with 2.5 per cent thereof to be considered as an advance on the 5.5 per cent set for 1988.

10th November

Several amendments to the 1988 Finance Act laid before the Senate, with the aim of cutting the Treasury deficit targeted in the September draft by L 6 000 billion, to L 103 500 billion (9.9 per cent of GDP). This is to be achieved mainly by savings in health expenditure, reducing budgetisation of social security contributions and above all by lending at concessional rates to public enterprises. But VAT rates will not after all be raised, ruling out much of the proposed reduction in the progressiveness of direct taxes (IRPEF).

1988

18th March

Pension contribution rates and pension ceilings for senior executives raised. The daily unemployment benefit, set at L 800 since the end of World War II, raised to 8 per cent of the average wage, pending the reorganisation of all the schemes.

31st May

Presentation of the government's *medium-term fiscal programme*, aimed at stabilising the public debt as a percentage of GDP by 1992. Relative to the spontaneous trend, the proposed measures are designed to boost revenue by 1.8 per cent of GDP (of which 1.1 per cent from direct taxes and 0.7 per cent from indirect taxes) and to cut spending by 1.5 per cent of GDP. The total tax take over the next four years is targeted at L 45 000 billion. It is planned to reduce the interest burden by 2.5 per cent of GDP. Under the proposed Programme the sector most affected will be social security; the retirement age will be raised to 65 for men and 60 for women; the minimum number of contribution years will be 20, instead of 15 as now; and it will no longer be possible to combine a retirement pension and earned income. Pension rights are to be calculated on the basis of 10 years (instead of 5 as now); the amount of overtime counting towards pension rights is to be reduced. The health insurance system is to be reformed: patients will once again have to contribute to the cost of medical tests; an indirect health insurance scheme is to be set up for people with high incomes; medicines will be packaged in "therapeutic doses", i.e. in smaller quantities. The railways and postal services, which generate very sizeable deficits, are to be restructured. Local authorities will be given greater freedom in their tax policies. A programme is to be launched to enhance the productivity of the civil service. Last, the government plans to sell off assets to raise between L 9 000 billion and L 15 000 billion.

30th July

Adoption of a package of economic measures to curb the budget deficit:

- Raising of the central VAT rate from 18 to 19 per cent;
- Natural gas and fuel oil prices raised by L 50 per litre;
- Local authorities to be empowered to levy a surtax of L 5 per kwh on electricity consumption to boost their revenue;
- Patients to bear a portion of medical prescription costs.

September

Reform of budget procedures. This constitutes the second phase of the 1986 reform limiting the Finance Act to a few major objectives and making the structural reforms needed to achieve them the subject of separate legislation. Under the new procedure, the government will submit the forecasts and assumptions underlying its budget policy before Parliament in *mid-May* of the preceding year. *The annual budget*, which simply sets out the spontaneous public finance trends for the year ahead on unchanged tax assumptions, will now be presented in *July*, while the *Finance Act* and the *Medium-term Fiscal Programme* are to be presented in mid-September. The Finance Act will not include new expenditure or new taxes. It will simply adjust the parameters of existing legislation (e.g. income tax scales), set out the amount of expenditure in the coming year under existing multi-year appropriations and the expenditure ceilings with respect to civil service pay. All new measures will have to be the subject of separate legislation specifying the multi-year expenditure programme and the nature and amount of new resources required to fund it.

5th September

The 1989 Finance Act and accommodating legislation. Under the Act, the deficit is budgeted at a maximum of L 117 350 billion; the accommodating measures must thus achieve a reduction of L 20 000 billion relative to the spontaneous trend. This is to be achieved as to 50 per cent by revenue-boosting measures with the remainder coming from expenditure cuts.

Revenue-boosting measures include:

- A tax amnesty for small enterprises and family concerns. To qualify indefinitely for flat-rate tax treatment, they must pay a pro rata fine according to the amount of unpaid tax due;

- Consolidation in 1989 of the indirect tax increases introduced on a temporary basis in 1988;
- The cost of lowering personal income tax rates to be met almost entirely by closing tax avoidance loopholes.

Measures to cut spending include:

- Limiting the carryover of expenditure from one financial year to the next (residual liabilities) which should help rein back current spending growth in each ministry (in terms of budget commitments) to 14 per cent between 1987 and 1989;
- A partial price freeze on medicines to curb growth of health spending;
- Central government transfers to public transport enterprises to remain at present levels.

October

Abolition of secret Parliamentary ballots, notably with respect to voting on the Finance Act.

MONETARY, FINANCIAL AND EXCHANGE CONTROL POLICY

1987

February

Measures to deregulate the banking system:

- Banks to be authorised to buy and sell branches among one another;
- Subsidiaries of foreign banks authorised to operate freely throughout the territory;
- Bank specialisation eased; all banks empowered to lend funds for over 18 months. Removal of the administrative obstacles to the development of investment banks.

13th March

- Discount rate lowered from 12 to 11.5 per cent.
- Introduction of a reserve requirement on foreign currency bank deposits; 25 per cent of the increase in deposits, net of the proportion reinvested abroad or reallocated to other credit institutions, to be deposited in lire with the Bank of Italy; 5.5 per cent interest to be paid on reserves thus constituted.

13th May

Exchange control liberalized

- Compulsory non-interest-bearing deposits for investment abroad in securities abolished but authorisation still required for investment in non-EEC countries.

- Abolition of compulsory foreign currency financing of advance payments on imports.
- Period for holding foreign currency accounts doubled from 60 to 120 days for currency obtained directly from transactions with non-residents (exports), and from 30 to 60 days for foreign currency purchased against lire for transactions with non-residents (imports).
- Period doubled (from 15 to 30 days) for changing foreign currency holdings of residents into lire.
- Penalties on non-authorised debt position of non-residents' lire-denominated accounts abolished.
- Liberalisation of tourism; ceilings raised on foreign currency purchases and the amount of Italian banknotes that may be exported (in line with OECD Code).
- Liberalisation of imports of Italian banknotes. Proof of origin and use may be required for amounts over L 500 000 in case of residents, L 5 million in case of non-residents.
- Introduction of measures aimed at facilitating transactions with new residents, such as raising threshold requirements for foreign exchange forms; possibility of block foreign exchange financing for several commercial transactions (instead of for each individual transaction).
- "Consolidated foreign currency accounts" introduced for large groups, allowing debit and credit positions of foreign currency accounts to be cleared among companies within the group.

26th June

Rules on capital movements altered. Safeguards may only be invoked in case of temporary suspension of exchange market quotation. The safeguards consist in restrictions on bank transactions and in partial foreign-currency financing. They are applicable only pending completion of the Single European Market.

Yield on 3-year Treasury bills raised by 1 point and on medium-term Treasury certificates (CCTs) by ½ point.

28th August

Discount rate raised from 11.5 to 12 per cent. The 6.25 tax on yields on government securities raised to 12.5 per cent on 1st September, one month earlier than planned.

13th September

- Bank lending ceilings reimposed until March 1988: credit growth to be held down to 2.5 per cent in September 1987, 4 per cent in October 1987, 8 per cent in November 1987, 7.5 per cent in December 1987, 6 per cent in January 1988 and 6.5 per cent in February 1988.
- Introduction of restrictive foreign exchange measures applying only to export and import transactions to reduce leads and lags (100 per cent of advance payments on imports and 75 per cent of deferred payments on exports must be financed in foreign exchange).

1988

20th January

Exchange control measures lifted ahead of schedule.

4th February

Adoption of provisions implementing the exchange control liberalisation measures to come into effect on *1st October 1988.*

- Italian tourists may export all means of payment, provided these have been properly obtained from an authorised bank; the amount that can be taken out in banknotes raised from L 500 000 to L 1 000 000; no ceiling on credit card use for purposes of tourism, health, cultural activities, etc.
- Use of cheques drawn on Italian accounts authorised without any special formalities; amount of transfers by international postal order raised from L 2 million to L 5 million. Foreign securities bought by residents to be deposited with banks as before.

11th March

Provisions on reorganisation of stock market to achieve greater transparency.

30th March

Bank credit ceilings lifted with growth set within a target range of 6-10 per cent until end of year.

18th June

Residents authorised to make out cheques drawn on Italian bank accounts, in Italy or abroad, to non-residents, under the following conditions:

- The name of the non-resident must appear on the cheque;
- The cheque must be transferable;
- The amount must not exceed L 5 million.

Tourists are free to spend up to a total of L 3 million (of which L 2.1 million in foreign currency); they may use credit cards freely and, if necessary, cheques drawn on their Italian accounts under the conditions specified above, provided they retain evidence of expenditure.

26th August

Central bank discount rate raised from 12 per cent to 12.5 per cent. According to the Treasury Minister, this decision was taken both to take account of international trends and to curb the growth of domestic credit demand.

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STATISTICAL ANNEX

Selected background statistics

	Average 1978-87	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987
A. *Percentage changes*											
Private consumption [1]	2.9	3.0	5.3	4.3	1.5	1.1	0.7	2.4	3.0	3.5	4.3
Gross fixed capital formation [1]	2.0	-0.1	5.8	9.4	-2.3	-5.7	-0.1	5.3	2.5	1.4	5.2
Public investment [1]	4.1	-4.3	3.7	14.3	12.4	1.3	0.2	-0.6	8.2	2.6	4.8
Private investment [1]	1.7	0.5	6.1	8.7	-4.5	-7.0	-0.2	6.4	1.5	1.1	5.3
Residential [1]	0.1	1.2	3.0	4.9	-0.1	-5.0	3.9	0.7	-1.7	-1.7	-3.6
Non-residential [1]	2.4	0.2	7.7	10.4	-6.5	-8.0	-2.3	9.6	3.1	2.5	9.4
GDP [1]	2.6	2.7	4.9	3.9	1.1	0.2	1.1	3.2	2.9	2.9	3.1
GDP price deflator	13.3	13.9	15.9	20.6	18.5	16.2	15.0	11.3	8.9	7.5	5.6
Industrial production	1.6	1.9	6.7	5.5	-2.2	-3.1	-3.2	3.4	1.2	2.7	4.0
Employment	0.7	0.7	1.0	0.8	0.5	0.6	0.6	0.4	0.8	0.9	0.2
Compensation of employees (current prices)	15.5	16.9	19.8	23.5	22.4	17.3	15.4	11.9	12.2	8.1	8.9
Productivity (real GDP/employment)	1.9	2.0	3.9	3.1	0.7	-0.3	0.4	2.8	2.0	1.9	2.9
Unit labour costs (compensation/real GDP)	12.6	13.8	14.2	18.9	21.0	17.0	14.2	8.5	9.0	5.1	5.6
B. *Percentage ratios*											
Gross fixed capital formation as percent of GDP at constant prices	22.6	22.9	23.1	24.3	23.5	22.1	21.8	22.2	22.2	21.8	22.3
Stockbuilding as percent of GDP at constant prices	1.1	0	1.0	2.5	0.5	1.0	0.4	1.3	1.4	1.6	1.9
Foreign balance as percent of GDP at constant prices	-2.0	-0.5	-1.5	-4.2	-1.7	-1.8	-1.0	-1.7	-1.9	-2.2	-3.8
Compensation of employees as percent of GDP at current prices	47.0	48.1	47.4	46.7	47.7	48.0	47.7	46.5	46.5	45.5	45.5
Direct taxes as percent of disposable income	11.5	8.1	8.0	9.6	11.1	12.2	13.3	13.0	13.1	13.3	13.6
Household saving as percent of disposable income	25.6	29.3	29.2	28.0	26.7	25.9	24.5	24.0	23.4	23.0	21.9
Unemployment rate	8.7	6.8	7.2	7.1	7.9	8.5	9.2	9.3	9.3	10.3	11.0
C. *Other indicator*											
Current balance (billion dollars)	-1.7	6.2	5.5	-10.0	-9.1	-6.2	1.5	-2.5	-3.7	2.5	-1.0

1. At constant 1981 prices.

Table A. **Expenditure on gross domestic product, current prices**

Trillion lire

	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987
Private consumption	160.7	194.6	244.1	291.6	342.5	396.5	453.5	510.0	559.2	611.6
Public consumption	36.9	45.8	58.1	75.4	88.8	105.2	120.0	135.8	147.9	166.7
Gross fixed investment	58.7	72.0	94.8	111.6	121.7	135.0	154.9	171.7	180.3	195.1
Final domestic demand	256.3	312.5	397.0	478.6	553.0	636.6	728.5	817.4	887.3	973.4
	(15.8)	(21.9)	(27.0)	(20.6)	(15.6)	(15.1)	(14.4)	(12.2)	(8.5)	(9.7)
Stockbuilding	–1.4	1.2	9.7	4.7	6.5	3.0	12.5	13.5	11.4	11.4
	(–0.2)	(1.0)	(2.7)	(–1.3)	(0.4)	(–0.6)	(1.5)	(0.1)	(–0.3)	(0)
Total domestic demand	254.9	313.7	406.7	483.2	559.5	639.6	741.0	830.9	898.7	984.8
	(15.7)	(23.1)	(29.6)	(18.8)	(15.8)	(14.3)	(15.8)	(12.1)	(8.2)	(9.6)
Exports	54.2	68.5	77.3	100.1	114.2	126.9	150.7	169.0	167.2	177.2
Imports	53.0	70.8	93.6	115.3	128.6	132.9	163.9	184.3	163.7	179.5
Foreign balance	1.3	–2.3	–16.2	–15.2	–14.4	–6.1	–13.2	–15.3	3.5	–2.2
	(1.1)	(–1.4)	(–4.5)	(0.3)	(0.2)	(1.5)	(–1.1)	(–0.3)	(2.3)	(–0.6)
GDP (market prices)	256.2	311.4	390.4	468.0	545.1	633.6	727.8	815.6	902.2	982.6
	(16.9)	(21.6)	(25.4)	(19.9)	(16.5)	(16.2)	(14.9)	(12.1)	(10.6)	(8.9)

Note: Figures in parentheses are annual growth rates; for stockbuilding and the foreign balance they are contributions to GDP growth.
Sources: ISTAT; 1978 and 1979, Secretariat estimates.

Table B. **Expenditure on gross domestic product, constant 1980 prices**

Trillion lire

	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987
Private consumption	222.3	234.1	244.1	247.8	250.4	252.1	258.2	265.8	275.2	287.1
Public consumption	55.9	56.9	58.1	59.6	61.3	63.1	64.7	67.0	69.1	71.4
Gross fixed investment	81.9	86.6	94.8	92.6	87.3	87.2	91.8	94.1	95.4	100.4
Final domestic demand	360.1	377.6	397.0	400.0	399.0	402.3	414.6	426.9	439.7	458.9
	(2.2)	(4.9)	(5.1)	(0.8)	(–0.2)	(0.8)	(3.1)	(2.9)	(3.0)	(4.4)
Stockbuilding	–0.1	3.7	9.7	1.8	4.0	1.5	5.2	5.9	6.9	8.5
	(0.2)	(1.1)	(1.6)	(–2.0)	(0.6)	(–0.6)	(0.9)	(0.2)	(0.2)	(0.4)
Total domestic demand	360.0	381.3	406.7	401.8	403.0	403.8	419.8	432.8	446.6	467.4
	(2.4)	(5.9)	(6.7)	(–1.2)	(0.3)	(0.2)	(4.0)	(3.1)	(3.2)	(4.7)
Exports	74.1	80.9	77.3	83.1	82.2	84.1	90.5	93.9	97.2	100.6
Imports	75.9	86.4	93.6	90.0	89.4	87.9	97.6	102.1	107.0	117.6
Foreign balance	–1.8	–5.5	–16.2	–6.9	–7.2	–3.9	–7.1	–8.2	–9.8	–17.0
	(0.3)	(–1.0)	(–2.8)	(2.4)	(–0.1)	(0.8)	(–0.8)	(–0.3)	(–0.4)	(–1.6)
GDP (market prices)	358.2	375.7	390.4	394.9	395.8	400.0	412.7	424.6	436.8	450.4
	(2.7)	(4.9)	(3.9)	(1.1)	(0.2)	(1.1)	(3.2)	(2.9)	(2.9)	(3.1)

Note: Figures in parentheses are annual growth rates; for stockbuilding and the foreign balance they are contributions to GDP growth.
Sources: ISTAT; 1978 and 1979, Secretariat estimates.

Table C. **Gross domestic product, by kind of activity**

Trillion lire and percentage changes

	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987
At current prices										
(Trillion lire)										
Agriculture	..	..	22.3	24.8	27.9	33.3	33.9	36.6	38.9	39.4
Industry[1]	..	..	124.6	142.1	163.0	184.6	210.4	232.5	257.3	277.5
Energy	..	..	15.1	16.2	22.0	29.0	33.8	37.2	44.4	49.9
Manufacturing	..	..	109.5	125.9	141.0	155.7	176.6	195.3	212.9	227.6
Construction	..	..	28.0	34.2	37.9	41.8	45.7	48.7	51.4	53.5
Services	..	..	212.2	263.4	309.7	365.5	427.0	487.6	546.4	598.6
Market services	..	..	166.5	203.6	240.0	284.0	334.4	384.0	433.2	471.5
Public administration	..	..	45.7	59.9	69.7	81.5	92.6	103.6	113.3	127.1
Subtotal	..	..	387.0	464.6	538.6	625.2	717.0	805.3	894.0	969.0
GDP (at market prices)	..	..	390.4	468.0	545.1	633.6	727.8	815.6	902.2	982.6
At 1980 prices										
(Percentage changes)										
Agriculture	..	..	..	0.6	–2.6	8.3	–3.6	0.4	2.3	1.3
Industry[1]	..	..	..	–0.3	–1.6	0.1	3.6	2.3	3.4	4.0
Energy	..	..	..	–0.7	–2.3	–5.1	0.3	1.3	4.3	1.5
Manufacturing	..	..	..	–0.3	–1.5	0.8	4.0	2.4	3.3	4.3
Construction	..	..	..	–1.9	–3.5	–2.4	–3.0	–2.4	–1.0	–2.2
Services	..	..	..	2.2	2.0	1.4	4.2	4.2	3.0	3.2
Market services	..	..	..	2.2	2.1	1.4	4.8	4.8	3.4	3.7
Public administration	..	..	..	2.2	1.7	1.4	1.9	1.6	1.4	1.0
GDP (at market prices)	..	..	..	1.1	0.2	1.1	3.2	2.9	2.9	3.1

1. Including mining.

Source: ISTAT.

Table D. **Household appropriation account**

Trillion lire

	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987
Compensation of employees	123.3	147.7	182.5	223.3	261.9	302.2	338.3	379.4	410.2	446.8
Property and entrepreneurial income	118.5	147.5	186.8	209.9	246.4	277.9	319.3	350.4	390.7	423.5
Transfers received	40.1	46.8	58.4	77.4	95.4	116.6	128.5	148.1	162.7	173.7
Gross total income	281.9	342.0	427.7	510.6	603.7	696.7	786.1	877.9	963.6	1 044.0
Direct taxes	18.4	22.0	32.6	44.3	56.3	70.0	77.8	87.2	96.6	106.6
Social security contributions	36.2	45.1	56.2	68.4	85.1	101.9	111.8	124.9	140.5	153.9
Disposable income	227.4	274.9	339.0	397.8	462.2	524.8	596.6	665.9	726.4	783.5
Consumption	160.2	193.9	243.3	290.6	341.3	395.1	449.8	504.9	553.1	611.6
Savings ratio[1]	29.6	29.5	28.2	26.9	26.2	24.7	24.6	24.2	23.9	21.9
Real disposable income, (percentage change)	4.6	5.1	2.5	–0.3	0	–1.3	1.8	2.2	3.0	2.9

1. As a percentage of disposable income.

Sources: OECD Secretariat, based on ISCO and Bank of Italy estimates.

Table E. **General government account**

Trillion lire

	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987
Current receipts	81.0	97.5	129.3	159.5	197.5	240.5	274.0	311.0	352.1	388.8
Direct taxes	22.0	26.1	37.3	50.9	64.5	78.4	91.4	105.5	115.5	130.4
Social security contributions	31.6	39.8	49.7	59.8	74.9	89.2	98.5	110.1	125.2	136.6
Indirect taxes	22.0	24.9	33.5	38.3	46.6	58.0	67.3	72.7	81.7	92.9
Other current receipts	5.5	6.6	8.7	10.4	11.4	14.9	16.7	22.7	29.7	28.8
Current expenditure	97.3	116.2	146.9	192.3	236.2	283.9	325.6	366.9	410.8	444.0
Expenditure on goods and services	36.1	45.0	57.0	74.2	87.4	103.2	118.0	133.2	145.1	163.9
Subsidies	7.8	9.6	11.1	13.3	16.9	18.1	22.2	22.5	27.3	26.0
Interest paid	13.0	15.7	21.1	28.8	39.3	48.0	58.1	65.5	76.4	80.1
Social benefits	37.6	43.6	55.0	73.1	88.9	109.7	121.6	139.2	154.8	166.9
Other current transfers	2.7	2.3	2.7	2.9	3.6	4.9	5.7	6.4	7.2	7.2
Saving	–16.3	–18.7	–17.6	–32.9	–38.7	–43.4	–51.6	–55.8	–58.8	–55.2
Fixed investment	7.4	8.9	12.3	16.9	20.3	23.5	26.2	30.6	32.0	34.7
Capital transfers, net	–3.4	–4.6	–4.3	–4.9	–4.1	–2.3	–7.9	–17.2	–14.8	–15.8
Consumption of fixed capital	0.6	0.7	0.9	1.1	1.3	1.4	1.7	2.0	2.3	2.7
Net lending	–26.5	–31.5	–33.3	–53.6	–61.9	–67.7	–84.0	–101.7	–103.3	–102.9
(as a percentage of GDP)	–10.3	–10.1	–8.5	–11.5	–11.3	–10.7	–11.5	–12.5	–11.4	–10.5

Source: Relazione generale sulla situazione economica del paese (1987); 1978 and 1979, OECD Secretariat estimates.

Table F. Prices and wages

	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987
Indices, 1980=100										
Consumer prices										
Total	71.9	82.5	100.0	117.8	137.2	157.3	174.3	190.3	201.4	211.0
Food products	76.0	86.5	100.0	116.1	133.8	149.5	163.2	177.6	187.1	193.9
Non-food products	70.0	80.7	100.0	118.5	138.6	160.6	179.0	195.7	207.4	218.1
Services (excluding rent)	72.4	82.9	100.0	122.0	144.1	166.7	186.8	208.2	234.4	249.8
Per capita compensation										
Total economy										
Nominal	..	..	100.0	122.6	142.4	165.1	184.2	203.5	218.7	238.2
Real	..	..	100.0	104.0	103.8	104.9	105.7	106.9	108.6	112.9
Industry										
Nominal	..	..	100.0	122.1	143.2	165.9	188.6	210.0	225.3	243.1
Real	..	..	100.0	103.6	104.3	105.4	108.2	110.3	111.9	115.2
Percentage changes										
Consumer prices										
Total	12.1	14.8	21.2	17.8	16.5	14.6	10.8	9.2	5.8	4.7
Food products	13.0	13.8	15.7	16.1	15.3	11.7	9.2	8.8	5.3	3.6
Non-food products	11.7	15.2	23.9	18.5	17.0	15.9	11.4	9.3	6.0	5.1
Services (excluding rent)	13.8	14.6	20.6	22.0	18.2	15.7	12.0	11.5	12.6	6.6
Per capita compensation										
Total economy										
Nominal	..	..	..	22.6	16.2	15.9	11.6	10.5	7.5	8.9
Real	..	..	..	4.0	–0.3	1.1	0.7	1.2	1.6	4.0
Industry										
Nominal	..	..	..	22.1	17.3	15.9	13.7	11.3	7.3	7.9
Real	..	..	..	3.6	0.7	1.1	2.6	2.0	1.4	3.0

Sources: ISTAT; OECD, *National Accounts.*

Table G. **Employment indicators**

Labour units, thousands

	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987
Total employment	..	..	22 062	22 060	22 182	22 324	22 413	22 597	22 810	22 859
Dependent employment	..	..	15 409	15 301	15 337	15 210	15 188	15 391	15 465	15 470
Agriculture	..	..	936	875	848	827	792	784	765	753
Total industry	..	..	6 584	6 380	6 205	5 970	5 699	5 614	5 541	5 483
of which: Manufacturing	..	..	5 136	4 918	4 767	4 565	4 343	4 281	4 230	4 197
Construction	..	..	1 259	1 270	1 248	1 217	1 166	1 141	1 115	1 088
Market services	..	..	4 242	4 312	4 473	4 532	4 737	4 955	5 075	5 110
General government	..	..	3 646	3 734	3 811	3 882	3 959	4 037	4 085	4 123
Self-employment	..	..	6 653	6 759	6 845	7 114	7 225	7 206	7 345	7 389
of which: Agriculture	..	..	2 057	1 970	1 835	1 918	1 894	1 796	1 787	1 771
Total industry	..	..	1 334	1 354	1 378	1 378	1 306	1 300	1 327	1 301
Market services	..	..	3 262	3 436	3 632	3 818	4 025	4 110	4 231	4 317

Source: ISTAT.

Table H. **Money and credit**

a) The monetary base

Changes in billion lire

	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987
Origin of liquid assets										
Net impact of the foreign sector	5 911	2 868	708	25	–5 647	8 840	5 141	–13 677	3 543	6 756
Net impact of the public sector	4 984	760	9 740	14 233	12 676	4 514	10 027	27 519	10 994	9 240
Banks	–56	2 624	–2 576	119	638	–3	– 218	5 881	–4 333	– 730
Other sectors	– 979	689	–2	–5 739	2 670	– 747	–1 103	– 647	–1 004	–1 321
Total net impact	9 860	6 941	7 869	8 639	10 336	12 604	13 847	19 076	9 200	13 946
Use of liquid assets										
Liquidity in the hands of the public	2 936	2 631	3 670	4 430	3 528	4 081	3 861	4 002	3 143	4 386
Compulsory bank reserves	5 076	5 508	3 046	2 946	8 544	9 092	8 855	12 213	9 022	8 740
Bank liquidity	1 848	–1 198	527	442	–1 218	359	1 133	2 860	–2 965	162
Compulsory bank deposits	..	..	626	821	– 519	– 927	–2	..	..	657
Total	9 860	6 941	7 869	8 639	10 336	12 604	13 847	19 076	9 200	13 946

Source: Banca d'Italia, *Annual Report.*

Table H. **Money and credit**

b) Selected indicators

Billion lire, outstanding end of year

	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987
Money[1]										
Currency in circulation[2]	18 533	21 000	24 544	28 839	32 308	36 256	39 922	43 730	46 839	51 146
Sight deposits	87 159	110 057	125 777	143 822	170 500	190 022	217 125	238 986	270 530	289 198
Saving deposits	87 111	100 837	112 163	124 214	151 744	169 687	188 198	207 866	217 675	231 780
Post office saving deposits	20 307	24 755	28 450	30 366	33 262	36 952	42 924	50 712	61 265	73 364
Money supply M2	213 110	256 649	290 934	327 241	387 814	432 917	488 169	541 294	596 309	645 488
Treasury bills	9 788	18 007	33 737	57 983	70 024	85 561	107 550	123 224	127 179	159 798
Money supply M3	222 898	274 658	325 805	387 071	459 310	519 579	596 262	664 865	723 789	806 245
Central bank										
Credit to Treasury	40 234	40 508	50 320	63 738	75 135	76 399	90 127	117 588	128 531	135 106
Credit to banking sector	309	3 602	496	971	2 020	4 788	1 238	6 912	3 552	3 880
Banking sector										
Credit	86 834	105 673	126 693	142 455	155 312	178 800	215 596	244 225	266 035	288 823
Government securities, shares and bonds	88 363	102 112	115 559	123 875	157 109	186 694	195 637	208 679	222 873	234 965
Special credit institutions										
Credit	57 208	63 091	72 175	86 104	101 515	115 354	130 653	140 575	156 854	178 785
Total domestic credit	294 967	348 790	412 024	485 360	586 097	706 726	850 759	1 004 481	1 156 888	1 308 497
Private sector	150 325	175 586	204 805	232 903	264 507	299 939	352 264	398 705	444 399	490 174

1. Data refers to households and firms only.
2. Excluding banking sector.

Source: Banca d'Italia, *Annual Report*.

Table I. **Foreign trade by main commodity groups**

Million US dollars

	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987
Imports, total	55 353	76 474	98 443	88 999	83 818	78 323	81 998	88 144	99 775	122 211
Food, drink and tobacco	8 838	10 851	11 793	10 192	10 839	10 285	9 703	11 443	13 931	16 513
Crude oil	10 787	14 716	20 166	22 202	18 924	15 904	13 259	13 339	8 341	8 888
Other fuels	2 612	3 749	7 312	8 676	8 324	8 753	10 039	10 457	9 093	8 157
Metals, ores and scrap	4 923	7 593	9 573	5 786	5 554	5 133	6 111	6 221	7 308	8 579
Textile materials and products	2 839	4 178	4 517	3 702	3 636	3 553	4 221	4 525	5 258	6 702
Chemical products	4 729	6 992	7 993	7 020	6 890	7 307	7 813	8 476	11 001	13 689
Motor vehicles and parts	3 292	4 600	6 810	5 937	5 444	4 152	4 633	5 190	7 366	10 572
Machinery and other transport	7 403	9 635	12 835	11 352	10 368	9 633	11 172	12 619	16 787	22 791
Wood and products	1 320	1 998	2 606	1 856	1 535	1 323	1 423	1 304	1 601	2 119
Miscellaneous manufactures	4 849	6 898	9 170	7 996	7 682	7 346	7 947	8 764	12 117	16 477
Other imports	3 760	5 263	5 667	4 279	4 621	4 934	5 677	5 805	6 972	7 724
Exports, total	57 124	73 250	78 530	75 303	73 551	72 670	73 358	78 682	97 815	116 582
Food, drink and tobacco	3 766	5 419	5 286	5 415	5 299	4 724	4 805	5 562	6 221	7 243
Refined petroleum products	3 155	4 591	4 164	4 494	4 822	3 667	3 103	3 460	2 616	2 695
Mineral manufactures	4 586	5 839	6 851	6 364	5 865	5 983	5 686	5 657	7 349	8 841
Metals, ores and scrap	3 835	4 289	4 747	4 978	4 619	4 135	4 250	4 448	4 815	5 316
Textile materials and products	3 623	4 465	4 466	4 511	4 398	4 628	4 868	5 207	6 917	7 915
Chemical products	3 710	5 810	5 505	5 214	5 296	6 116	6 203	6 608	7 060	8 745
Motor vehicles and parts	4 542	5 425	5 483	4 590	4 033	4 183	4 080	4 242	6 139	8 007
Machinery and other transport	12 746	15 349	18 256	18 229	17 806	18 086	17 727	19 500	25 506	31 136
Clothing and shoes	5 925	8 120	8 205	7 444	7 890	7 949	8 300	9 038	12 323	14 303
Miscellaneous manufactures	8 085	10 901	11 315	11 134	11 095	10 745	11 547	12 432	15 763	19 073
Other exports	3 149	3 042	4 251	2 930	2 428	2 455	2 789	2 527	3 105	3 308

Source: OECD, *Foreign Trade Statistics, Series B.*

Table J. Geographical breakdown of foreign trade

Million US dollars

	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987
Imports, total	55 353	76 474	98 443	88 999	83 818	78 323	81 998	88 144	99 775	122 211
OECD countries	35 625	48 968	62 004	52 781	50 796	47 969	51 994	56 990	73 253	92 614
EEC	26 354	36 308	45 845	38 349	37 460	35 638	38 100	42 628	55 951	70 611
of which: Germany	9 774	13 351	16 473	14 190	13 813	12 743	13 397	15 033	20 415	26 308
Belgium-Luxembourg	1 885	2 778	3 536	2 815	2 774	2 716	3 098	3 359	4 639	6 217
France	8 219	10 967	13 807	11 358	10 774	10 112	10 468	11 275	14 582	18 248
Netherlands	2 368	3 265	4 133	3 763	3 724	3 911	4 116	4 605	6 450	6 991
United Kingdom	2 250	3 141	4 393	3 508	3 386	3 115	3 665	4 466	5 092	6 562
USA	3 816	5 312	6 912	6 137	5 789	4 751	5 121	5 349	5 645	6 653
Canada	553	749	1 013	867	740	522	583	525	573	812
Japan	678	885	1 299	1 261	1 096	1 112	1 348	1 479	2 092	2 676
Non OECD countries	19 466	27 204	36 080	36 190	33 008	30 279	29 830	30 848	26 160	29 421
COMECON	2 831	3 761	5 290	4 738	5 194	5 251	6 110	4 883	4 798	5 131
OPEC	8 254	12 864	16 988	18 477	14 235	11 972	11 182	12 619	9 377	8 904
Others	8 382	10 578	13 803	12 975	13 579	13 056	12 537	13 345	11 985	15 386
Exports, total	57 124	73 250	78 530	75 303	73 551	72 670	73 358	78 682	97 815	116 582
OECD countries	39 251	51 762	53 337	47 653	49 116	49 741	51 944	57 749	76 272	93 402
EEC	29 022	38 642	40 126	34 309	35 596	35 267	34 802	37 975	52 392	65 403
of which: Germany	10 667	13 663	14 212	11 679	11 467	12 053	11 817	12 705	17 742	21 667
Belgium-Luxembourg	1 927	2 467	2 583	2 073	2 132	2 089	2 123	2 335	3 260	3 936
France	7 993	10 696	11 757	10 222	11 184	10 687	10 280	11 040	15 283	19 041
Netherlands	2 297	3 311	2 864	2 294	2 258	2 175	2 109	2 434	3 201	3 596
United Kingdom	3 394	4 720	4 723	4 358	4 605	4 615	4 955	5 475	6 931	8 672
USA	3 995	4 670	4 124	5 109	5 182	5 605	7 989	9 645	10 503	11 201
Canada	430	502	485	562	558	636	807	982	1 204	1 356
Japan	517	784	705	667	791	790	843	928	1 323	1 863
Non OECD countries	16 231	19 651	23 200	26 655	23 387	22 146	20 685	20 152	20 999	22 659
COMECON	2 525	2 748	2 824	2 532	2 501	2 753	2 553	2 699	2 955	3 673
OPEC	5 895	7 289	9 175	11 956	9 793	8 852	7 529	6 552	5 428	5 230
Others	7 811	9 615	11 200	12 167	11 093	10 542	10 603	10 901	12 616	13 755

Source: OECD, *Foreign Trade Statistics, Series B.*

Table K. **Balance of payments**
Million US dollars

	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987
Current account										
Merchandise exports	55 433	71 340	77 031	76 272	72 695	72 056	73 790	75 686	96 395	116 000
Merchandise imports	52 534	72 292	93 952	87 936	81 537	74 500	79 627	81 933	92 181	115 891
Trade balance	2 898	– 952	–16 921	–11 664	–8 842	–2 444	–5 837	–6 247	4 214	109
Services, net	3 683	5 978	5 501	1 702	1 499	2 525	1 754	1 466	–64	– 103
Travel	5 079	6 695	7 006	5 889	6 601	7 211	6 496	6 474	6 944	7 634
Investment income	–1 101	– 543	– 655	–3 194	–3 923	–3 896	–3 902	–3 979	–6 210	–6 610
Other services	– 295	– 174	– 850	– 993	–1 179	– 790	– 840	–1 029	– 798	–1 127
Transfers, net	– 383	453	1 458	899	1 110	1 449	1 627	1 056	–1 608	– 997
Private	1 106	1 416	1 372	1 442	1 469	1 403	1 455	1 323	1 458	1 286
Official	–1 489	– 963	86	– 543	– 359	46	172	– 267	–3 066	–2 283
Current balance	6 198	5 479	–9 962	–9 063	–6 234	1 529	–2 456	–3 724	2 543	– 992
Capital account										
Long-term capital, net	1 079	– 314	3 281	8 353	5 176	657	1 486	2 445	–2 693	2 080
Private, direct	342	– 183	– 167	– 258	– 389	– 936	– 705	– 815	–2 676	1 733
Private, portfolio	–88	111	– 926	– 404	– 376	232	99	375	–1 043	–7 416
Public[1]	1 400	1 426	3 597	4 439	2 369	1 836	2 542	2 300	1 833	3 699
Short-term capital, net	– 774	–1 332	7 741	185	–3 791	3 696	1 475	–1 973	4 202	5 054
Private non monetary	482	–2 573	– 356	1 526	–1 527	406	–1 450	802	– 127	757
Private monetary institutions	–1 256	1 241	8 097	–1 341	–2 264	3 290	2 925	–2 775	4 329	4 297
Miscellaneous official accounts	–3 261	– 494	224	–4	– 276	98	– 208	181	210	– 115
Allocation of SDRs	0	167	160	139	0	0	0	0	0	0
Errors and omissions	484	– 368	– 272	536	721	–97	2 452	–3 898	–1 712	– 919
Change in reserves	2 866	– 378	1 998	57	–2 738	4 586	2 647	–4 124	– 437	4 573

1. Excludes special transactions.
Sources: OECD Secretariat.

BASIC STATISTICS :

INTERNATIONAL COMPARISONS

BASIC STATISTICS: INTERNATIONAL COMPARISONS

	Units	Reference period[1]	Australia	Austria	Belgium	Canada	Denmark	Finland	France	Germany	Greece	Iceland
Population												
Total	Thousands	1987	16 249	7 575	9 868	25 803	5 130	4 932	55 627	61 149	9 998	245
Inhabitants per sq.km	Number		2	90	324	3	119	15	102	246	76	2
Net average annual increase over previous 10 years	%		1.4	0.0	0.0	1.0	0.1	0.4	0.4	0.0	0.7	1.0
Employment												
Total civilian employment (TCE)[2]	Thousands	1987	7 079	32 997	3 645 (86)	11 954	2 630 (86)	2 414	20 988	25 456	3 601 (86)	117 (86)
of which: Agriculture	% of TCE		5.8	8.6	2.9	4.9	5.9	10.4	7.1	5.2	28.5	10.3
Industry	% of TCE		26.6	37.7	29.7	25.3	28.2	31.2	30.8	40.5	28.1	36.8
Services	% of TCE		67.6	53.7	67.4	69.8	65.9	58.4	62.1	54.3	43.4	53.0
Gross domestic product (GDP)												
At current prices and current exchange rates	Billion US$	1987	193.7	117.2	138.9	410.9	101.3	89.5	879.9	1 117.8	47.2	5.3
Per capita	US$		11 919	15 470	14 071	16 019	19 750	18 151	15 818	18 280	4 719	21 813
At current prices using current PPP's[3]	Billion US$	1987	204.9	88.4	116.5	444.5	68.4	63.3	712.2	814.7	63.6	3.8
Per capita	US$		12 612	11 664	11 802	17 211	13 329	12 838	12 803	13 323	6 363	15 508
Average annual volume growth over previous 5 years	%	1987	3.7	1.8	1.5	4.2	2.7	3.2	1.6	2.1	1.4	3.1
Gross fixed capital formation (GFCF)	% of GDP	1987	23.8	22.6	16.3	21.0	18.8	23.5	19.4	19.4	17.4	18.8
of which: Machinery and equipment	% of GDP		11.5 (86)	9.7	7.0 (86)	6.9 (86)	7.8	9.7	8.3	8.4	7.1	6.5
Residential construction	% of GDP		4.7 (86)	4.6 (86)	3.4	6.4 (86)	4.4	55	5.2	5.2	4.6	3.5
Average annual volume growth over previous 5 years	%	1987	1.7	2.3	2.0	4.8	6.5	1.9	0.6	1.8	–2.2	1.8
Gross saving ratio[4]	% of GDP	1987	20.3	24.1	17.6	18.8	15.5	22.5	19.6	23.9	14.7	15.2
General government												
Current expenditure on goods and services	% of GDP	1987	18.2	19.0	16.3	19.5	25.4	20.7	19.1	19.8	19.5	17.7
Current disbursements[5]	% of GDP	1987	35.0 (86)	46.6 (86)	51.6 (86)	43.3 (86)	53.4 (86)	38.2	48.4	43.0 (86)	42.9 (86)	27.3 (86)
Current receipts	% of GDP	1987	34.7 (86)	47.9 (86)	45.0 (86)	39.4 (86)	58.0 (86)	39.6	49.4	44.9 (86)	36.6 (86)	32.1 (86)
Net official development assistance	% of GNP	1987	0.33	0.17	0.49	0.47	0.88	0.50	0.74	0.39	..	0.05
Indicators of living standards												
Private consumption per capita using current PPP's[3]	US$	1987	7 389	6 535	7 593	10 059	7 236	6 966	7 796	7 374	4 273	9 930*
Passenger cars, per 1 000 inhabitants	Number	1985	..	306 (81)	335 (84)	421 (82)	293	329 (86)	369 (86)	441 (86)	127	431
Telephones, per 1 000 inhabitants	Number	1985	540 (83)	460 (83)	414 (83)	664 (83)	783	615	614 (86)	641 (86)	373	525 (83)
Television sets, per 1 000 inhabitants	Number	1985	..	300 (81)	303 (84)	471 (80)	392	370 (86)	394 (86)	377 (86)	158 (80)	303
Doctors, per 1 000 inhabitants	Number	1985	..	1.7 (82)	2.8 (84)	1.8 (82)	2.5 (84)	2.3 (86)	2.3 (86)	2.5 (84)	2.8 (83)	2.4 (84)
Infant mortality per 1 000 live births	Number	1985	9.2 (84)	11.0	9.4	9.1 (83)	7.9	5.8 (86)	7.0 (86)	9.1	14.1	5.7
Wages and prices (average annual increase over previous 5 years)												
Wages (earnings or rates according to availability)	%	1987	5.7	4.9	3.4	3.6	6.1	8.5	6.4	3.6	17.4	..
Consumer prices	%	1987	7.0	3.0	3.5	4.2	4.7	5.0	4.7	1.1	19.3	25.7
Foreign trade												
Exports of goods, fob*	Million US$	1987	26 484	27 084	82 824[7]	94 320	25 632	19 404	147 936	293 424	6 516	1 368
as % of GDP	%		13.6	23.0	59.8	22.8	25.3	22.1	16.8	26.2	13.9	25.8
average annual increase over previous 5 years	%		4.4	11.6	9.6	6.5	11.1	8.2	9.0	10.7	8.7	13.7
Imports of goods, cif*	Million US$	1987	26 964	32 580	82 992[7]	87 528	25 452	18 828	153 204	227 916	13 116	1 584
as % of GDP	%		13.9	27.7	59.9	21.1	25.1	21.4	17.4	20.4	27.9	29.9
average annual increase over previous 5 years	%		2.8	10.8	7.4	9.7	8.8	7.0	6.7	6.5	5.6	10.8
Total official reserves[6]	Million SDR's	1987	6 441	6 049	7 958[7]	5 778	7 153	4 592	26 161	58 846	2 007	221
As ratio of average monthly imports of goods	Ratio		3.4	2.6	1.4	0.9	4.0	3.5	2.4	3.7	2.2	2.0

	Ireland	Italy	Japan	Luxembourg	Netherlands	New Zealand	Norway	Portugal	Spain	Sweden	Switzerland	Turkey	United Kingdom	United States	Yugoslavia
Population															
Total	3 542	57 331	122 091	372	14 671	3 284	4 184	10 280	38 830	8 399	6 610	52 010	56 890	243 915	23 410
Inhabitants per sq.km	50	190	328	143	432	12	13	112	77	19	160	67	232	26	90
Net average annual increase over previous 10 years	0.8	0.3	0.7	0.3	0.6	0.5	0.3	0.5	0.7	0.2	0.5	2.2	0.1	1.0	0.8
Employment															
Total civilian employment (TCE)[2]	1 068 (86)	20 584	59 110	164 (86)	5 135 (86)	1 517 (86)	2 090	4 156	11 370	4 337	3 219 (86)	15 632 (86)	24 987	112 440	..
of which: Agriculture	15.7	10.5	8.3	3.7	4.9	10.5	6.7	21.9	16.1	4.2	6.5	55.7	2.4	3.0	..
Industry	28.7	32.6	33.8	32.9	25.5	28.9	27.0	35.8	32.0	30.2	37.7	18.1	29.8	27.1	..
Services	55.5	56.8	57.9	63.4	69.6	60.6	66.3	42.3	51.8	65.6	55.8	26.2	67.8	69.9	..
Gross domestic product (GDP)															
At current prices and current exchange rates	29.4	758.1	2 376.5	6.0	213.2	35.1	82.7	36.7	289.2	158.5	171.1	67.4	669.8	4 472.9	61.7 (86)
Per capita	8 297	13 224	19 465	16 138	14 530	10 620	19 756	3 761	7 449	18 876	25 848	1 296	11 765	18 338	2 652 (86)
At current prices using current PPP's[3]	26.7	702.5	1 609.4	5.5	179.7	35.3	64.5	61.4	337.1	115.7	104.9	220.9	702.5	4 472.9	..
Per capita	7 541	12 254	13 182	14 705	12 252	10 680	15 405	6 297	8 681	13 771	15 842	4 247	12 340	18 338	..
Average annual volume growth over previous 5 years	1.8	2.6	3.9	4.0	2.1	2.1	4.1	2.1	2.9	2.4	2.3	6.0	3.2	4.3	
Gross fixed capital formation (GFCF)	17.4	19.9	28.9	22.6	20.3	21.2	28.0	25.3	20.7	19.0	25.2	24.5	17.3	17.3	21.6 (86)
of which: Machinery and equipment	9.4 (86)	10.0	10.5 (86)	9.0 (82)	10.0	13.1 (85)	7.9 (86)	14.7 (81)	6.4 (86)	8.5 (86)	8.8	8.6 (84)	8.1 (86)	7.6	..
Residential construction	4.6 (86)	5.2	5.0 (86)	4.7 (82)	5.2	4.6 (85)	5.0 (86)	6.4 (81)	4.0 (86)	3.8 (86)	16.4 (9)	2.7 (84)	3.8 (86)	5.0	..
Average annual volume growth over previous 5 years	–3.7	2.8	5.3	0.8	4.8	2.0	4.1	–0.7	3.8	3.6	6.0	7.3	4.7	7.0	..
Gross saving ratio[4]	18.6	20.9	32.3	56.5	21.8	20.3	23.4	27.5	21.9	18.0	31.7	24.1	17.2	14.7	..
General government															
Current expenditure on goods and services	18.0	16.7	9.6	16.7	16.1	17.6	20.9	14.4	14.4	26.7	12.8	9.1	20.9	18.6	14.3 (86)
Current disbursements[5]	49.2 (84)	45.2	27.4 (86)	45.3 (84)	54.0 (86)	..	47.8 (86)	37.6 (81)	36.1 (86)	60.0 (86)	30.1	..	42.9 (86)	35.5 (86)	..
Current receipts	43.3 (84)	39.3 (86)	31.3 (86)	54.1 (84)	52.8 (86)	..	56.5 (86)	33.3 (81)	35.0 (86)	61.6 (86)	34.5	..	41.6 (86)	31.2 (86)	..
Net official development assistance	0.20	0.35	0.31	0.10	0.98	0.26	1.09	0.08	0.06	0.88	0.31	..	0.28	0.20	..
Indicators of living standards															
Private consumption per capita using current PPP's[3]	4 378	7 543	7 623	8 694	7 461	6 236	8 155	4 167	5 521	7 273	9 349*	2 844	7 731	12 232	1 335 (86)*
Passenger cars, per 1 000 inhabitants	206 (83)	355 (84)	221 (83)	439 (87)	341	455	382 (86)	135 (82)	252	377	402	18 (82)	312 (83)	473 (84)	121 (83)
Telephones, per 1 000 inhabitants	235 (83)	448 (84)	535 (83)	425 (86)	410 (86)	646	622 (84)	166 (83)	381 (86)	890 (83)	1 334	55 (83)	521 (84)	650 (84)	122 (83)
Television sets, per 1 000 inhabitants	181 (80)	244 (84)	250 (80)	336 (83)	317 (86)	291	346 (86)	140 (80)	256 (82)	390	337	76 (79)	336 (84)	621 (80)	175 (83)
Doctors, per 1 000 inhabitants	1.3 (82)	3.6 (82)	1.3 (82)	1.9 (86)	2.2 (84)	2.4	2.2	1.8 (82)	3.4 (86)	2.5	1.4 (84)	1.5 (83)	0.5 (83)	2.0 (85)	1.6 (82)
Infant mortality per 1 000 live births	8.9	10.9	5.9 (84)	9.0	9.6 (86)	10.8	8.5 (86)	17.8	7.0 (84)	6.8	6.9	..	9.4	10.4 (86)	31.7 (83)
Wages and prices (average annual increase over previous 5 years)															
Wages (earnings or rates according to availability)	8.8	10.5	2.6	..	2.3	7.4	10.2	17.9	10.3	7.6	..	..	8.5	3.1	..
Consumer prices	5.2	7.6	1.1	2.2	1.3	12.6	7.0	17.2	8.5	5.9	2.1	41.6	4.7	3.3	56.3
Foreign trade															
Exports of goods, fob*	15 948	116 004	230 220	..[8]	92 592	7 164	21 804	9 144	33 972	44 388	45 312	10 344	130 632	254 124	11 425
as % of GDP	54.8	15.4	9.7	..	43.1	20.1	26.2	25.3	11.8	27.9	26.6	15.7	19.7	5.7	16.3
average annual increase over previous 5 years	14.6	9.6	12.1	..	6.9	3.4	4.4	17.0	10.4	10.6	11.8	12.1	7.7	3.7	2.2
Imports of goods, cif*	13 620	124 596	150 300	..	91 068	7 224	22 428	13 248	48 816	40 596	50 424	14 460	153 768	424 440	12 603
as % of GDP	46.8	16.6	6.3	..	42.4	20.2	27.0	36.7	17.0	25.5	29.6	21.9	23.2	9.6	18.5
average annual increase over previous 5 years	5.9	7.7	2.8	..	7.2	4.6	7.8	6.9	9.1	8.0	12.0	9.7	9.1	11.7	–3.1
Total official reserves[6]	3 393	23 631	57 925	..	12 818	2 298	10 105	3 047	22 035	5 974	22 283	1 254	30 070	33 657	557
As ratio of average monthly imports of goods	3.5	2.7	5.5	..	2.0	4.5	6.4	3.3	6.4	2.1	6.3	1.2	2.8	1.1	0.6

* At current prices and exchange rates.
1. Unless otherwise stated.
2. According to the definitions used in OECD *Labour force Statistics.*
3. PPP's = Purchasing Power Parities.
4. Gross saving = Gross national disposable income *minus* Private and Government consumption.
5. Current disbursements = Current expenditure on goods and services *plus* current transfers and payments of property income.
6. Gold included in reserves is valued at 35 SDR's per ounce. End of year.
7. Including Luxembourg.
8. Included in Belgium.
9. Including non-residential construction.

Sources:
Population and Employment: OECD *Labour Force Statistics.*
GDP, GFCF, and General Government: OECD *National Accounts.* Vol. I and OECD *Economic Outlook, Historical Statistics.*
Indicators of living standards: Miscellaneous national publications.
Wages and Prices: OECD *Main Economic Indicators.*
Foreign trade: OECD *Monthly Foreign trade Statistics, series A.*
Total official reserves: IMF *International Financial Statistics.*

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