Recensione del volume:

Structural Reforms Without Prejudices

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1. - The Issues of Product Market Reform in Europe

Product market reform (*i.e*. liberalization, or deregulation, of product markets) in Europe is considered, in a recent book edited by Tito Boeri *et* al. (2006), from three major perspectives: for its spread and timing (an empirical matter); for its efficiency justification, impact and further potential (a normative — welfare-economic — question); for its political conditions (an issue of public choice and political economy).

Thus, the book considers a number of issues — possibly too large a number, as a vast and complex matter is squeezed into a mid-sized book (336 pages in all). The multiple authorship (involving contributions to the main text and comments on it by a number of academics and researchers) does not help, as it results into uneven treatment and considerable discontinuities.

At the same time, however, the book is interesting and useful, in that it singles out extremely relevant issues, offers new and penetrating insights, and delivers a clear (and, to the present reviewer, convincing) policy message.

In short: in Europe, for a long time, product markets have been made the object of very heavy, inefficient, regulation; their working has thus been constrained and distorted, with damaging

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effects on productivity growth, international competitiveness, and economic growth. In the UK, with the Thatcher reforms of the eighties, a far-reaching liberalization policy was carried out; in the rest of Europe, liberalization measures have also been taken, and some benefits obtained, but on the whole progress has been slow, and successes limited. Then, there is a basic issue (indeed, a challenge) that the policy debate and initiative must confront: how liberalization policy can be revived and re-launched — or, how this policy can be brought to the forefront of the political agenda, gain political support, and find routes to practical implementation.

2. - Growth in Europe and its Determinants, from 2000 Onwards

The poor record of economic growth in Europe, *circa* 2000-2005, is the starting point of the book and dictates the perspective taken. Here and there, a comparison between the growth records of Europe and the US is also touched upon, and the gap between the two — with the first considerably poorer than the second — noticed with concern.

Post-2005 developments, however, have brought about substantial changes, as growth in Europe has become more robust, while growth in the US has slowed down, and the gap in economic performance between the two regions has nearly disappeared; and forecasts suggest that these changes are likely to be lasting, as they can be traced back to changes in economic fundamentals (see, *e.g.*, Cotis, 2007).

But do these changes in the general economic outlook detract from the value of the book, by undermining its basic tenet and starting point?

My tentative answer to this question is, not — or, largely, not. The book addresses real, important, and deeply-rooted weaknesses of the European economy, for which excessive regulation and lack of competition can be blamed. Two examples are emphasized and discussed to some length — the slow development and adoption of new technology and the low growth of service industries.

In addition, at a more general level, the book considers how microeconomic determinants impact on macroeconomic performance. This is an extremely relevant, as well as controversial, issue, and the book, in this respect, offers a number of facts, appraisals, and policy suggestions.

On the one hand, this book can be read as an attempt to redress the tendency of current debates to overlook microeconomic problems and policy measures, as these are considered — at least implicitly — to be of lesser importance, if compared to large-size problems and policy measures, i.e involving sizeable sections of government activity and public finance (this is a criticism that may be directed, for example, to the otherwise important, EC-sponsored, *Sapir Report* on Europe's growth prospects - see Sapir, 2004).

On the other hand, by discussing product market reform, the book contributes an essential component of an argument — and a project — for comprehensive liberalization policy. And it can be argued that this component is of comparable importance to the much more widely discussed reform of the labour market.

3. - The Normative Case for Liberalization (and Privatization)

The first half of the book is devoted to the theory and evidence which can be brought to bear on the normative case for liberalization (and, to some extent, privatization).

The exposition starts from a critical judgement on the current state of knowledge on whether competition can improve economic performance. It is said that theory "does not provide an unambiguous answer" on this issue (p. 21); and it added further that empirical analysis tends to be biased by reliance on simplified modeling. Both points are stressed in the text, and discussed at some length in a dedicated appendix.

In the end, the case for liberalization and privatization is accepted, but with a number of qualifications. Such policies can be — but are not always and necessarily — efficiency-enhancing; distinctions must be made with regard to different situations and policies; and further research is required to gather a full picture of developments and issues.

The book subsequently develops the analysis and reinforces the previous conclusion. A case-study strategy is followed: geographical coverage is limited in the extreme, as only three countries (UK, Italy and Germany) are taken into consideration; on the other hand, sectoral coverage is extensive, as many industries, and most of those which are heavily regulated, are dealt with — the large utility industries (electricity, natural gas, telecommunications, the railways, the posts, and water), plus the professions and retailing.

As to the issues tackled, liberalization, and its intended offspring, competition, take the centre-stage; but also the associated policies of privatization and re-regulation (new, efficient, regulation taking place of old, inefficient, one) are examined. All case studies are conducted with an eye to the influence of EU policy and are equipped with summary assessments of what has been, and what remains to be, done.

On all this, I have a few comments, but little or no real criticism. Firstly, it seems to me that, in the available literature, the normative case for liberalization, while possibly not clarified in all the relevant aspects, is however less dubious than the book suggests. In particular, I have in mind the convergence of analyses which has come from the British discussion over the merits and problems of introducing competition in the utility industries. Summarizing, and simplifying, public policy should adhere, as to a basic guiding principle, to the *dictum* "competition where possible, regulation where necessary": giving free rein to competition is the best option to discipline markets and activate efficiency incentives; but regulation is required when, due to the presence of market power (natural monopoly), competition cannot be introduced (salient references are Vickers and Yarrow, 1987; Armstrong, Cowan and Vickers, 1994; Newbery, 2000).

Secondly, I wonder whether some nuances should be added to the conclusion offered on the merits and problems of privatization. On these, the book has reasonable and cautionary remarks; in particular, it looks to privatization policy in the light of the discussion over the relative performance of publicly and privately owned companies, to suggest that no general, empirically-based, conclusion has taken shape. This is hardly disputable, as different studies have produced widely differing pictures; but there are perhaps effects of privatization policy which are not as negative as (or less negative than) the book asserts. Productivity gains were obtained (often) before privatization — but would they have materialized, were not for the expectation of privatization? After privatization, productivity gains have been highly dependent on labour shedding — but was not this required as a remedy to previous — almost general — situations of overmanning? Privatization has lead to increases in profits (and, I would add, executive salaries) — but was not this also required, as a remedy to low profitability and executive pay levels?

Thirdly, I would have liked to find something more, in particular an examination of the French case, and a comprehensive and unified treatment of (transport) infrastructure industries. On the one hand, France has been traditionally, and remains presently, the stronghold of *étatisme* in the management of the economy, as important markets and industries are addressed by government industrial policy, much more than they are entrusted to competition (and privatization and regulation); so, it would be of some interest to have an overall assessment of the performance of this formula — something which, as far as I know, the literature has not made available. On the other hand, transport infrastructure industries (airports, ports, motorways, tunnels), have become increasing similar to public utility industries due to the privatization and marketization practices which have gained popularity. This development, which has involved the various aspects of investment planning, investment funding, profitability requirements, charging, and regulatory concerns, has not escaped attention (see, *e.g.*, Guasch 2004; Kessides, 2004); but it is nevertheless true that significant gaps remain, with regard both to knowledge of facts and understanding of issues.

But, for the rest, I find the exposition convincing. The main conclusions do not come as a surprise: the UK has embraced an approach to liberalization which has not only been original and groundbreaking, but also comprehensive and systematic, and, in the end, considerably successful; compared with the UK experience, those of Italy and Germany are largely unsatisfactory, as a consequence of the compound effect of insufficient liberalization and defective regulation. However, and this is the worth of the exposition, these conclusions are supported by detailed analyses, in which the relevant events — the policy actions and the industrial and market developments — are examined and evaluated.

4. - Favourable and Unfavourable Political Conditions

The second half of the book is devoted to a discussion of the political conditions and strategies which can help or hamper the adoption and progress of policy reforms — including, but not solely, liberalization.

The discussion follows various threads. To succeed, reform plans must get over the *status quo* bias which is inherent in the pre-reform situations, as a consequence of the asymmetry between costs which are visible, certain, immediate, and, very often, concentrated on particular groups, and benefits which are spread over large sections of society and long spans of time, and thus uncertain and blurred. Governments that have the backing of large and steady majorities are in the condition to enact one-off, far-reaching reforms. But the road to reforms is not forbidden to governments that can only count on narrow (or, due to the fragmentation and strength of interest groups, unstable) majorities: they can enlarge political support for reforms by addressing compensating measures to large and powerful stakeholders (in particular, the trade unions and the employers' organizations); or they can follow a "divide and rule" strategy by targeting reforms on few and (relatively) small groups at a time; or they can even take advantage of external constraints (as those following from IMF conditionality, or EU membership), by leaning on them to push reforms forward.

On these points I have two specific comments. The first relates to the idea that compensating measures can enlarge support for reforms. This is indeed a possibility, and one which has often been exploited in practice; but it translates in a watering down of reforms themselves. The book recognizes this, but, in my opinion, does not stress it sufficiently: the discussion of the Italian pension reforms of 1992 and 1995, which tends to play down the criticisms which have been directed to such reforms, is a case in point.

The second comment relates to the possible exploitation of external constraints. While this is indeed a realistic possibility, it is not without drawbacks. On the one hand, super-national decision making is often difficult — exposed as it is to tactics and bargaining (this is well-exemplified by European negotiations and agreements — with their skirmishes and compromises). On the other hand, reference to a super-national authority allows politicians to say that their policies are dictated by necessity, not discretion; but this leads to delays and laxity in both the shaping and the implementation of national legislation (and, often, also to nationalistic resentment).

But there is, possibly, a further and more general difficulty, with the analysis of the book. Political expediency, on which the book concentrates, can well be vital for the initiation and advancement of reforms, but its exercise requires, as a preliminary condition, firm political commitment to such reforms on the part of governments and their supporting majorities.

Such a commitment, however, is not found frequently. Liberalization and privatization tend to be felt, by many politicians, governments, and parliaments — in many countries — as policy approaches leading to a loss of power, that is, to self inflicted damage. The same applies also to regulation, when this is taken care of (as it is in the current fashion) by independent authorities, isolated, to a large extent, from political interference. These attitudes may mix with other ones, dictated by considerations of a different — normative — character, as to the requirements of an efficient management of the economy; but it is nevertheless the case that these circumstances tend to translate overall in a half-hearted political endorsement for liberalization and regulation by independent authorities.

Then, the question arises as to what are the fundamental conditions for reform, and how they are determined in concrete situations.

Two possibilities come to mind. One possibility is that reforms are felt as unavoidable and unprocrastinable — indeed, as solutions to emergency situations. Italian reforms of the 1990s offer two examples of this, the pension reforms decided in 1992-95, already referred to, and privatization policy, initiated in 1992. Both were triggered by the contemporary, critical condition of public accounts, which required public expenditure cuts and revenue increases; and both took advantage of a relaxation of political constraints, in a political climate largely shaped by the scandals of that period.

Another possibility is that political leadership, and political entrepreneurship, can obtain political support for reforms, thanks to an ability, in part to convince, and in part to gain the trust of, the electorate. The Thatcher reform are an obvious case in point; but another important case can be found, in the US experience of deregulation of the late 1970s and early 1980s, which was championed by a few political leaders (the names which are usually made are those of Edward Kennedy and Ralph Nader see Levine, 1989; Noll, 1989).

But it is easily seen that these possibilities depend on rather unusual circumstances. Or: reforms can be studied, explained, advocated; but political commitment — on which reforms depend crucially — is far from warranted, and, possibly, unfrequent.

5. - The View From Italy

Seen from an Italian perspective, the reasoning and the conclusions of the book convey an especially telling message.

It is a message that resounds with a remainder of Luigi Einaudi and Guido Carli's apprehensions for, and polemics against, the *lacci e lacciuoli* (the fetters and constraints) which stifle and distort private economic effort: thus it points to a critical aspect of the Italian social and economic organization which has been known for a long time, always commented upon as extremely worrying, but never seriously tackled, and even less mended. Indeed, a long string of parliamentary majorities and governments, (publicly committed to liberalization and simplification) has done relatively little to reduce and restructure the regulatory burden on economic activity — a possible exception being that of capital markets, where, however, liberalization has been largely driven by external forces, relating to the growing interconnectedness of the world economy, and re-regulation has shown uncertainties and delays.

More specifically, as far as product market reform is concerned, the message delivered by the book fits with (and adds substance to) the largely prevailing opinion — among commentators — that the current Italian situation characterizes for many and serious shortcomings.

The book suggests that liberalization of markets is a largely unachieved goal, and their regulation a defectively performed task. Many aspects are touched upon, including the timidity of the initial reforms directed to the structure of industries and the weakness of the apparatuses set in charge of regulation. For these, two main examples are given: the limited measures of vertical and horizontal separation of public utility industries (especially the energy industries); and the incomplete design of a system of independent authorities, whereby no such body has been established with respect to the transport industries. *Ad adjuvandum*, and as a concluding observation, I would note further that evidence is accumulating as to a very slow development of competition in public utility industries: for example, the railways have seen no competitive challenge for the incumbent operator in the transport of passengers (Macchiati *et* al., 2007); while the electricity and natural gas industries fare poorly in international benchmarking exercises as to the degree of market competition which has been achieved (see Oxera, 2006; also European Commission, 2007).

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