1 *Italy's Parabola, 1861–2022*

There were years in Italy's history when genius and ambition seemed to know no limit. In 1492 Christopher Columbus, a navigator from Genoa, discovered a new continent as he tried to reach India by sailing west. Three years later, between 1495 and 1496, Leonardo da Vinci started painting the Last Supper in Milan. Michelangelo returned to his native Florence and paid his first visit to Rome, where he would create eternal masterpieces. In Venice, the equestrian statue of condottiero Bartolomeo Colleoni was erected as a sign of the Republic's wealth and power. At that time, Venice, Florence and Milan were the wealthiest areas in Europe, and probably the world. According to some estimates, Italians were on average better off by about 30 percent than the rest of Western Europeans. Northern Italy was possibly almost twice as rich as the average region in France, Spain or England.

Being used to dominating seas and trade, in 1495 the Venetians understood that, after Columbus's "discovery" of America, the Mediterranean Sea was bound to lose its centrality. Rumors spread among the Venetian merchants about Portuguese ships preparing to circumnavigate Africa before the end of the century. The Council of Ten, the collegium presiding over government decisions of the Venetian Republic, could not dither. The representatives of the patrician families were summoned to the Palazzo Ducale, which was still under reconstruction after the disastrous fire of 1483. Whoever visits Venice today knows exactly the huge palace standing next to St. Mark's Basilica overlooking the lagoon and decorated with Gothic arches and colonnades. Even today, the Council's strategy seems so daring as to challenge our understanding of those ages: The collegium advanced a proposal to introduce a tax in the following years to finance the digging of a canal between the African and the Asian continents. It is the same canal that would be built centuries later and would become known as the Suez Canal.

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In 1495, Venetian Doge Agostino Barbarigo led a coalition that chased the French forces out of Italy. It was time for Venice to defend its role in global trade. Venetian engineers were sent to Egypt to study the feasibility of the new canal and came back with a favorable opinion: The available technology was sufficient for carrying out the project, that is, connecting a string of local lakes and linking the Mediterranean to the Red Sea. The canal would have shortened the routes to India and China dramatically, more than compensated for Venice's inability to trade with the New World, connected the Middle East to the world's most developed economies, contained the role of the Ottomans, and most importantly, maintained Venice at the center of the world.

The final project was presented on May 4, 1504. Unfortunately for Venice, Egyptian Sultan Qaansuuh al-Gawri opposed the project and on June 11, 1504, the Council of Ten symbolically drew a black cross on the engineers' map (Pedani 2012). The project had to wait 355 years, till the middle of the nineteenth century, to become reality.

To consolidate its power and wealth, Venice had to look back at Italy's mainland. It was Pope Julius II this time to see Venice's expansion as a threat to the secular powers of the Roman Church in Central and Southern Italy. He excommunicated the Venetian Republic and called for foreign military powers to contain it. Soon Italy became a playground for foreign powers. In 1530 Holy Roman Emperor Charles V subjugated the Tuscan republics, the Kingdom of Naples and the Duchy of Milan. The two major Italian seafaring powers, Venice and Genoa, fighting each other in the Mediterranean, were unable to adapt their institutions and technology and seize the opportunities offered to them by the trans-oceanic challenge. They were small and geography, it was said, was against them; also, in the bellicose environment, their defensive mentality prevented them from absorbing new ideas, and techniques and from embracing new challenges. According to various scholars, including Carlo Maria Cipolla (2013), the cultural and institutional resistance to change slowly produced an economic decline.[1] Presumably, foreign domination eroded Italy's social fabric and the relevance of cultural life, as reveals the common dictum "France or Spain, as long as we eat grain,"[2] presciently pronounced by Machiavelli's friend Francesco Guicciardini. The desolating "Spanish" domination of Italy was only one reason for the long period of fragmentation, internal conflicts and foreign invasions that made the

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states of the Italian peninsula, for many centuries probably the wealthiest in the world, one of Western Europe's poorest.

Starting from the late sixteenth century, the economy of the Italian states declined in relative terms. According to some estimates, in the seventeenth century, the decline turned into an absolute loss of income (Malanima 2003, Broadberry 2016). Economic primacy in Europe passed to the United Provinces of the Netherlands, which had their own "golden age" until the mid-eighteenth century when that primacy passed to the British Isles, which maintained it until WWI. Already in the late nineteenth century, per capita income in the United States, the lands discovered by Columbus, exceeded that of the United Kingdom (Kindleberger 1996).

In the second half of the eighteenth century and the first two decades of the nineteenth century, Italy's per capita income did not grow and probably shrank. At the end of the Napoleonic Wars, real wages were lower than they had been around 1700, one of every four newborns died in his or her first months, and even the height of the average Italian male noticeably shrank from 167 cm in the mid-eighteenth century to 164 cm at the beginning of the nineteenth. There was some progress but, at the time of unification in 1861, Italy's economic misery had not changed much for the better.

Declines can last for a long time, centuries in this case, before they reverse course. The renewed attention to the Italian economy focuses on the second decline that occurred in the first decades of the twenty-first century, one, however, caused by factors that bore resemblance to those that caused the first: global competition, political uncertainty and economic regression. After the protracted and impetuous growth between the end of the nineteenth century and the end of the twentieth, Italy's economy, surprisingly, became poorer again, first in relative terms and, after the Great Recession of 2008–2013, even in absolute terms. There is no other instance of an advanced industrial economy experiencing a similar decline, and no other democratic nation has had to cope with the impoverishment of its new generations. As scholars debate the possible decline of the West and of western democracies, Italy seems to have preceded the trend, testing the resilience of its liberal democracy.

Italy has often anticipated social and political phenomena that later appeared in other countries: the decline of liberalism and the emergence of fascism; geographical polarization; mistrust in public institutions; recourse to public debt; secular stagnation; populism. Italy, however, has also been a laboratory in the constant attempt to amend these phenomena: the antifascist resistance; massive interregional aid; widespread entrepreneurship; uninterrupted reforms of the political system; the accumulation of private (and public) savings; the judiciary fight against the Mafia or corruption; the support for European sovereignty and supranational cooperation; and the correction of populist choices through non-partisan governments. Ironically, if Austrian philosopher Karl Popper was right in defining democracy not as the way to elect the best of governments, but as the way to take down the bad ones, by changing sixty-seven governments between WWII and 2022, Italy's democratic credentials must be at the forefront.

The reasons why Italy tends to anticipate the phenomena associated with a fragile democracy are conventionally ascribed to the fact that, since its foundation, the Kingdom of Italy's political–institutional order has been perceived as weak, particularly in comparison with the neighboring foreign powers. In the early nineteenth century, while Friedrich Hegel was chanting the quintessential link between Spirit and Power, more humbly, Alessandro Manzoni, the author of the novel *The Betrothed*, which is compulsory reading for all young Italian students, observed how the weakness of the state was "a more famous than understood trait of homeland history." This book sheds light on the interaction between economic choices and the peculiar relationship that runs between Italians and their state.

Italy's recent decline has elicited standard narratives reconnecting its recent impoverishment with the experience of the known past. Political instability and foreign domination between the seventeenth and the nineteenth centuries, at a time when beyond Italy's borders the great nation-states were being strengthened, have long been the preferred explanations of Italy's economic decline. In the following pages, we will trace the fault lines running through Italian history that may resonate with contemporary political–economic analysis in other countries. We identify several divisions in Italy's society that have been overcome by using state finance while that was possible. Rather than changing its incentives for the population, the government chose public debt to preserve the status quo, which has emerged as a political preference or necessity in a fragmented and polarized country. The consequence has been the crystallization of structural problems.

It is our tenet that domestic divergences, political inefficiency, public debt, financial instability and lower quality in investment have represented the links of the same causality chain. Among the internal divisions, the regional divergence between North and South was the most persistent, often coinciding with different levels of education and technological advancement. Other differences have played a major role in individual historical periods: for instance, popular estrangement from the process of constitution of the unified state; the drastic ideological polarization after WWII; the winners-vs.-losers of several monetary shocks; or an exacerbated level of popular suspicion of seemingly corrupt elites. Moreover, weak statehood and structural cleavages were mutually reinforcing.

However, one crucial argument in our reconstruction of Italy's economic evolution is that factors of political weakness have often coexisted with the strength of the economy. The apparent distance of citizens from public life runs parallel to the vibrancy of local communities and social structures and the worldliness of a part of the country's elite, which emerged through non-political "technocratic" government formations. Throughout its history Italy has often engaged non-political personnel in the highest public offices: Orlando, Nitti, De Stefani, Rocco, Beneduce, Menichella, Badoglio, Einaudi, Amato, Ciampi, Monti and Draghi, among others. Openness to the external world was a constant necessity for an economy depending on foreign provisions for raw materials or financial capital: non-partisan leadership often went hand in hand with the voluntary acceptance of external economic constraints or, as erstwhile Bank of Italy governor Guido Carli theorized, spontaneous limitations of national sovereignty and discretional policies, which, in turn, may have contributed to "horizontal legitimacy," that is, strengthening the country's credibility in its interaction with the international community.[3]

Italians' ambivalence toward the state was probably sedimented by centuries of foreign domination. Between the seventeenth and nineteenth centuries, the fatalism of subjection, liable to vary over time according to those who exercise it, generated passivity and extraneousness from public life, long dominated by local princes and foreign lords engaged in opportunistic behavior and obscure games of alliances and betrayals. In the conventional sociological interpretation, the individual had little other option but to leverage the relationship of personal devotion, a patron/client relationship, or to break rules and even laws.

Once the possibility of engaging in public affairs had been banned, all that remained was to devote oneself to private trade.

We see a dialectic tension between Italians' economic commitment and their political disenchantment. Throughout Italy's history, the two planes, political and economic, moved at different speeds. But in the 1990s a profound crisis in the state coincided with economic decline. Financial and political instabilities concurred to hamper Italy's development exactly in the years when new and groundbreaking global technological paradigms required investment in the future. A whole chapter is devoted to the multiple crises of the early 1990s, as we see them being the root of the subsequent economic decline.

We will argue that political uncertainty spiked in 1992, affecting Italy's outsized public debt and financial system, resulting in growing interest rate differentials with other European economies. Our findings indicate that the divarication of Italy's financial conditions had a major impact on the quantity and quality of investments. For these reasons, Italy partly missed the train of the technological revolution of the 1990s. Since then, Italy's productivity has diminished, bringing the economy into a vicious circle of lower growth, higher debt and increasing political instability.

In terms of the decline, institutional, political and economic factors have frequently interacted with each other. In a system of global competition, public powers are not irrelevant, and a vibrant economy is not self-sufficient. A democratic state and an open economy rest on a government's ability to respond to issues coming from both the domestic society and the external world. In short, the evolution of Italy's economy in the twenty-first century is also an anticipatory example of democracy's complex adjustment to globalization.

Considering the precarity perceived in many other democracies, under the pressure of globalized markets, internal divergences, political polarization, high public debts or autocratic temptations, Italy's experience tells a revealing story of the West resisting its own decline.

At the time of Italy's political unification, in March 1861, the shining lights of the Renaissance were long gone. The ages when Venice and Florence were leading European civilization had faded into poverty and backwardness. For centuries, regional divisions and hostilities among local autocrats or feudal elites, steered also by foreign domination, had eroded Italy's physical wealth and human prosperity (Table1.1).

Table 1.1 *GDP per person 1500–1870 (US dollars at 1990 purchasing power)*

Year	Italy	UK	France	Germany	Japan	12 Western European countries	Italy's GDP per capita in % of Western Europe
1500	1100	714	727	676	500	796	138
1820	1117	1706	1230	1058	669	1270	89
1870	1499	3191	1876	1821	737	2086	72

Source: Maddison (2010)[4]

In 1861, despite some progress made since the 1820s, the average gross domestic product (GDP) per inhabitant, that is, the present-day quantity of goods and services produced on average for one year by each citizen, did not exceed 70 percent of Western Europe's average and was less than 50 percent of the United Kingdom's, the most economically advanced country of the era. To get an idea of the poverty plaguing Italy at the time, one may consider that the average annual income of an Italian around 1870 was about 2,050 present-day euros, that is, 170 euros per month, an income not higher than that of most of today's sub-Saharan countries. Moreover, given the extremely uneven income distribution, the living standard of most inhabitants of the Italian peninsula was not far from, and sometimes below, mere subsistence: forty-four percent of the population had to live on less than 83 euros per month, which is below the threshold of absolute poverty (Vecchi 2017: 359).

Italians' average lifespan did not reach thirty years (Vecchi 2017: 90), while in France and Sweden it was forty-five. This was due mainly, but not only, to the second highest infant mortality rate in Europe, after the German one (Vecchi 2017: 108): Over a quarter of newborns did not reach their first birthday. Even in today's poorest countries, the average lifespan is considerably longer. In what was the cradle of the Renaissance and humanism, education was the privilege of a few. In 1861, only 26 percent of Italians over the age of fifteen could read and write. In 1870, Italians on average had less than one year of formal education, compared to four years for British citizens and six years for Americans (Vecchi 2017: 176). The new kingdom, therefore, was born poor and was under the burden of significant inequalities both in income and wealth.

The composition of employment in Italy was also typical of a backward economy, with 63 percent of the labor force employed, often underemployed, in agriculture. The industrial sector accounted for only about 17 percent of total employment (Baffigi 2013). Manufacturing activities took place mostly in small enterprises and workshops, normally employing all the members of a family[5] and producing little more than the common goods of daily life: food, apparel and furniture. In the mid-nineteenth century, one-third of the Italian manufacturers produced food, another third furniture and construction, and one-fifth apparel. The silk products supplied by the small firms in the Alpine regions, from Piedmont to Friuli, formed the basis of the local productive bourgeoisie and capital accumulation. Italy's exports covered most of the European demand for sophisticated textiles. The industry was beginning to produce substantial revenues to pay for the raw materials with which the country was poorly endowed. Infrastructure was also considerably less developed than in the advanced countries of Northwestern Europe. In 1861, the Italian peninsula had only 2,404 kilometers of railway, mostly located in the North, while Great Britain had 14,603 and the area of the future German Reich 11,603.

At the end of 1858, just before the beginning of the Second Italian War of Independence,[6] which led to the birth of the Kingdom of Italy, the Italian peninsula was divided into eight states (Fig. 1.1).

More than fifteen centuries of political disunion, often marked by fierce fighting among cities and states, had resulted in deeply rooted cultural, institutional–political and economic differences across the various parts of the peninsula. Tullio De Mauro (1963), a leading glottologist, estimated that, around the time of the proclamation of the new unified kingdom, only 2.5 percent of its citizens could shed their local dialect and communicate in Italian.[7] French was the working language in the Turin Parliament, the only elected legislative body on the peninsula.

Given that the "Southern question," or, generally speaking, the economic, social and cultural gap between the various areas of the country, is to this day the most salient feature of Italian society, it is worth considering these gaps at the beginning of our story. In fact, the issue of the "initial conditions," that is, the real economic backwardness of the Southern regions at the time of unification, still looms large in the debate on regional disparities today. Since the beginning of the century, a considerable amount of quantitative research has improved our knowledge of the main economic aggregates by region and province. A consensus seems to emerge pointing to smaller income gaps around the time of unification than existed in later years. Daniele and Malanima (2007) plausibly argue that, with average income levels close to subsistence, regional disparities could not have been large. In fact, Felice (2007) puts Southern GDP per capita in 1871 to 10 percent below the national average, with a wide within-South variance. Iuzzolino et al. (2013) estimate manufacturing output per capita to have been 30 percent lower in the South relative to the Northwest, but only 10 percent below the national average. Fenoaltea (2007) identifies

Figure 1.1 Map: The Italian peninsula before unification (1848)
Source: Toniolo, 2013

an East–West gap in addition to the traditional North–South rift. In fact, geographical analysis at a more disaggregate level than the regional one shows that economic and social divisions ran deep even within relatively limited areas.

Income and production data, however, are not entirely consistent with the well-being indicators that are normally significantly correlated with GDP per capita. In 1861, the height of the military recruits, quite

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a good comprehensive indicator of well-being, was 163.7 centimeters in the Northwest as against 160.9 in the South (Vecchi 2011: 57). The educational gap was even wider: Only 15 percent of the population over fifteen years of age could read and write in the South versus 48 percent in the Northwest. Likewise, Vecchi and Toniolo (2007) found a higher incidence of child labor in the South than in the Central and Northern regions.

In 2007, about a century and a half after Italy's political unification, the quantity of goods and services (GDP) available on average to each Italian was roughly twelve times greater than in 1861. The average lifespan (life expectancy at birth) was about eighty-two years, higher than in any other European country and the second highest in the world, after Japan. Only 27 out of 10,000 children did not reach the first year of age, a much lower number than in the United States. Income distribution was much more egalitarian than at the time of the unification; five percent of the population lived in absolute poverty, a number that is still too high for a G7 country but far from the 40 percent that characterized the Italian peninsula around 1861. Illiteracy had (almost) been completely eradicated, even if – as we will see – the quantity and quality of education did not live up to that of other countries with a similar income per capita and was still inadequate to allow Italy to take full advantage of the new technologies. All Italian regions had participated in this extraordinary process of economic growth and collective well-being, although not uniformly. The poorer areas did not reduce the income gap between themselves and the most prosperous ones, something that was already evident in the early twentieth century.

The revolutionary process that forever changed the living conditions of Italians was common to that of the many countries that took the path of "Modern Economic Growth" (MEG) between the nineteenth and twentieth centuries. Nobel laureate Simon Kuznets (1966) characterized MEG as the "epochal revolution," by far the most important in the whole history of humanity, not only because it relieved the vast majority of the world's population from the poverty of the previous millennia, but also because it allowed this majority to realize dreams that seemed unrealistic until the mid-nineteenth century: not only freedom from hunger but longer and healthier life, shorter and less tiring working schedules, education, geographical and even social mobility – the latter being almost unimaginable for millennia. If Italy's MEG is not an exception within the "club" of countries that undertook the process sometime in the nineteenth century, her early participation in the "club" was not discounted at the time of unification by both Italian and foreign observers. In the early twentieth century, neither British Prime Minister Arthur Balfour, nor Giovanni Giolitti, his Italian counterpart, would have bet a bottle of claret on Italy's GDP per capita being higher than Britain's eighty years afterward.

Economists and economic historians expect initially lower-income countries to "converge" (catch-up) with the more developed ones. There are good reasons for such expectations: Technologies are cheaper to copy than to develop, affluent foreign markets are good outlets for cheap (labor-intensive) products of poorer countries and the evidence of MEG benefits provides social and political motivation to follow the same route. Nonetheless, history shows that the eventuality of poorer countries catching up with richer ones is far from being a universal phenomenon. In fact, for most of the past two centuries, it was the exception rather than the rule. Catching up (or convergence, in economic jargon) requires "social capability for growth" to sustain apt policies over the long run (Abramovitz 1986). Such capability is built on a mix of cultural, social and institutional factors. They are not endowed by nature but need to be created and maintained. Our history will focus on how and when Italy generated and sustained growth-enhancing conditions. For roughly a century (from the mid-1890s to the mid-1990s) such conditions were maintained, although with different degrees of success at different times. This long catching-up epoch in Italy's economic history is encapsulated between two periods of "falling behind" the more advanced countries of the time, each period lasting about thirty years. Italy's economic history is therefore interesting for studying the reasons for both how a poor country started and sustained its MEG and how it lost a part of its "social capability for growth." The latter question, as we will see, is particularly intriguing for the thirty-odd years following the early 1990s.

Before describing and analyzing the various phases of Italy's economic history since the unification, it may be useful to examine the overall quantitative picture. Between 1870, the first year for which internationally comparable data exist, and 2007, Italy's real GDP per capita grew at an annual rate of about 1.9 percent, slightly higher than the average of the other Western European countries and roughly equal to the growth rate of the United States. As mentioned above,

Table 1.2 *GDP and well-being indicators 1861–2007*

	1861	2007
GDP per capita (euros at 2007 prices)	2,190	26,457
Life expectancy at birth (years)	30	82
First-year death rate (per 1000)	289	4.5
Income distribution (Gini coefficient)	0.50	0.33
People in absolute poverty (% of resident population)	40	5
Literacy rate (% of resident population)	22	98

Source: Toniolo (2013:4)

however, this overall picture is the result of a long period of "convergence" framed between two periods of "divergence." Table 1.2 provides a rough idea of the orders of magnitude of both phenomena. Using the United Kingdom (the pioneer in MEG) as a benchmark, Italy's GDP per capita lost considerable ground during the first thirty years after its political unification. Only at the end of the nineteenth century, after overcoming a serious economic, political and social crisis, did the economy of the new kingdom accelerate the pace of its development. We will see the non-linear dynamic of the long convergence that brought Italy's income per capita, which in 1896 was about 60 percent of that of Germany and France, to be roughly equal to that of these two countries at the end of the twentieth century (Table 1.3). Even more impressive was the "catching up" with the United Kingdom, which at the end of the nineteenth century enjoyed a per capita income of about two and a half times the Italian one. A century later, Italy's GDP per capita was equal to, and by some measures even higher than, that of the "first industrial nation."

Between 1896 and 1995, the convergence of labor productivity was even more evident than it was for GDP per capita. By the mid-1990s production per hour by an Italian worker was very close to that of his or her American peer (Fig. 3.1). We will see in Chapter 3 the main features of this long convergence process, detailing the moments when it was more or less rapid, its weaknesses alongside its strengths.

As the result of previous growth, in 1995 Italy's economic problems were no longer those typical of a relatively backward country. In most respects, Italy was part of the club of advanced countries, albeit with more relevant structural problems than other economies. From that

Table 1.3 *Italy's GDP per capita as percentage of GDP per capita in four developed countries (US dollars at 1990 purchasing power)*

Year	USA	Germany	France	United Kingdom
1871	61	91	82	50
1896	46	59	61	38
1913	46	70	70	52
1938	54	66	74	53
1973	64	89	83	90
1995	70	89	94	98
2007	62	96	88	85
2016	53	77	78	72

Sources: from 1861 to 1973: Maddison 2010, Historical Statistics of the World Economy, 0–2008, OECD, Paris (2010); from 1995 to 2016, The Conference Board (www.conference-board.org/data/).

moment on, it was a question of keeping up with the others. To do so, Italy could no longer count on the "advantages of backwardness" and on the business and economic policy strategies associated with them. A change of pace, both in the private and the public sector, was necessary. However, it did not take place, or at least there was not enough of it. The economy stalled. By 2007, the gap with the more advanced countries had returned to the levels of the 1970s. Convergence had given way to divergence. In the decades before 2020, Italy's growth tapered off and eventually came to a halt. In living memory, no other advanced economy in a democratic country has ever experienced a similar ebb of its economic dynamism.

According to Acemoglu and Robinson (2012),[8] inclusive institutions, democratic and pluralistic states, guarantee the rule of law and promote economic prosperity by appreciating and giving free rein to talents and creative ideas. They provide what economists call an incentive structure for individuals, a framework that acknowledges and rewards individual initiative. On the contrary, extractive institutions, those that permit the ruling elite to exploit the majority of the population, deter economic growth. Italy's post-1995 decline, which we will try to describe, is of a different kind. It resembles a democratic country that lost itself after vibrant century-long economic development. After achieving economic convergence with the most advanced societies, when democratic participation was strongest and a robust self-critical analysis was underway, Italy's economic growth slowed dramatically, and eventually stopped altogether. At that juncture, political life lost credibility and uncertainty clouded the future of a large majority of Italians.

Italy's institutional problems were not those of a backward society. In the 1990s Italy was a fully accomplished democracy, with voting participation of almost 90 percent. Its level of income was as high as in Britain, Germany or France. Italy's institutional problems were of a different kind, and they may serve as a lesson for other advanced democracies. The cause of Italy's prolonged economic stagnation was an unusual alchemic combination of multiple explosive crises that might represent a cautionary tale for other advanced societies complacent about their welfare and their democratic development. The mysterious "Italian disease" started to take root at the peak of Italy's economic miracle less than twenty years after WWII, long before the onset of the economic decline of the 1990s. Since then, we have seen similar symptoms – geographic divergences, growing debts, populist policies, political instability, degradation of public discourse and sentiments of mistrust in the civic community – spread all over the western world at an alarming and accelerating pace. Italy's history shows that, at some stage, a slowly developing and long ignored disease reaches a tipping point.