

Luiss

Institute for European Analysis and Policy

If Italy returns to the "zero sum" game

Carlo Bastasin

Policy Brief 11/2023

LUISS



September 20, 2023

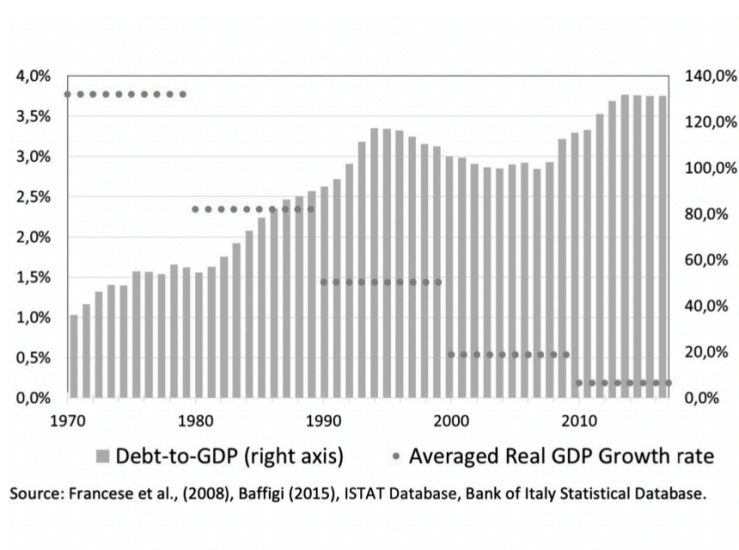
If Italy returns to the "zero sum" game

Carlo Bastasin

The recent downward revisions of the Italian economy's expected growth present serious implications in terms of economic policy: what will happen if Italian economic growth were to return to a condition of stagnation, that is, if the Recovery and Resilience Plan coordinated with the European Union would not change the level of close-to-zero potential growth that has characterized Italy in the recent decades? This policy brief argues that a profound rethinking of a political-economic nature is necessary, one that concerns the most delicate points of the domestic political debate.

Italian public life - the instability and radicality of politics - is linked to Italy being a zero-sum society, a socio-economic system that has not grown for thirty years, one in which the increase in GDP does not depart from the zero-point. In Figure 1, taken from Bastasin-Toniolo *The Rise and Fall of the Italian Economy* (Cambridge University Press – 2023), we can see how Italy's potential growth (calculated on the basis of the average growth rate of the decade) has steadily declined in the five decades before 2020 until reaching a level just above zero.

Figure 1



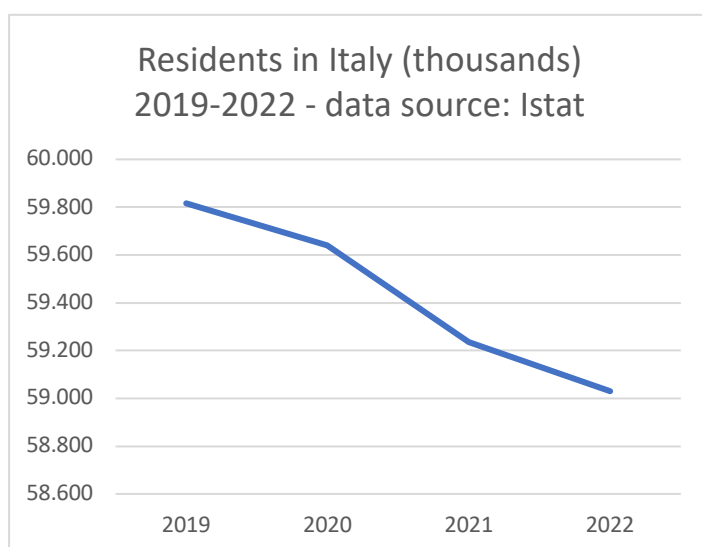
By "zero sum" here we mean only the algebraic observation of who increases and decreases their income, assuming for simplicity's sake the case of a closed economy or one with balanced foreign accounts. If we abstract from the formal theories on the rationality of social actors, as studied in game theory in the context of the "Nash equilibria", we see that it is not only a statistical but a psychological

condition that over time instils in social actors and citizens the belief that one improves one's condition only at the expense of someone else. From this derive the radical "against others" choices in the political vote, the populist appeal, the accumulation of debt to the detriment of future generations, alternating with large, technically-led coalitions called to reset the situation.

The objective of the Next Generation-EU Program was not only to save the Italian economy from the very serious recession caused by the 2020 Covid pandemic, but to escape from the cage of zero growth by permanently raising the level of future development. To this end, reforms (which are no longer called "structural", but must be so) were agreed upon and included in the NRRP, as well as the enormous investments generously financed by the European Union.

According to Italian government documents, "the NRRP will increase potential growth and productivity through innovation, digitalisation and investments in human capital."¹ According to a report² from the Parliament's study center, the government estimates the impact of the NRRP on Italy's economy with a growth of 0.8%, bringing the potential growth rate in the final year of the plan to 1.4%. However, these are optimistic estimates, especially when evaluating the starting conditions of the economy. A slightly more realistic assessment, based on past growth, estimates Italy's potential level as slightly lower than 0.5%. Thanks to the NRRP, it was estimated that an economy that had become dynamic again thanks to reforms, one that was equipped with greater capital could have increased its annual growth rate by around 0.6%, bringing it closer to 1 percent. It may seem like a modest level, if compared with that of the first decades of the Italian Republic, but it is not a given that the demographic decline - very significant in recent years as seen in Figure 2 (Istat data) - implies that per capita the income of Italian families would increase substantially.

Figure 2



¹ <https://www.governo.it/it/approfondimento/pnrr-gli-obiettivi-e-la-struttura/16702>

² <http://documenti.camera.it/leg18/dossier/pdf/DFP28.pdf>

The recent downward revision of growth estimates has clouded the hopes that had been raised by the launch of the European Program, but even more worrying is the feeling that the reforms are not as effective as hoped and the quality of the new investments is not such as to guarantee a leap in the country's capital endowment. The most disturbing phenomenon is that, based on the estimates available for 2023-2026, the more the public investments in the Plan increase and the less the private ones grow.

Istat recently revised its growth estimates for the year in which the confidence effect aroused by the NRRP was greatest with an upward revision of the 2021 GDP, calculated in nominal terms, "between 1.8 and 2.1 percent compared to the estimates released on March 1, 2023 and, consequently, an increase in the growth rate of the same year." However, after the truly exceptional boom in investments in 2021, companies once again seem to be in a waiting position. There is a problem - perhaps of trust or perhaps of the quality of production and services - which should not be underestimated. In this case, in fact, even in the long term, Italy's economic growth would return to the levels prior to 2020, not much higher than stagnation.

In the 1960s, anthropologist George Foster had identified the problem in some undeveloped societies by noting the relationship between zero growth and social and ethnic antagonism, defining the perception of the world that resulted from it as an image of "limited good", where the good is understood as the outcome of every social interaction. This is a primitive vision of societies that probably dates back to when material resources were strictly limited, as in the case of arable land within a given border. "Zero-sum" thinking is common to many societies and also to some views of international relations, among which are "mercantilism" and numerous interpretations of human mobility, including that of "ethnic substitution" where each additional migrant implies one less indigenous person.

Phases of strong economic development were necessary to make citizens aware of the possibility that everyone could benefit from mutual development. This has changed the approach of the great ideological interpretations of the past two centuries. The Marxist reading of history as a class struggle introduced a factor of dynamic development force into the antagonistic condition of a zero-sum society that reflected the industrial development at the turn of the 20th century. The liberal vision has instead highlighted the dynamics of capital accumulation as a path to making even different degrees of inequality tolerable. However, when the economy stops, the antagonistic component in society takes on corporate connotations and the liberal one tends to be suffocated. Protectionist temptations and the closure of society inevitably emerge.

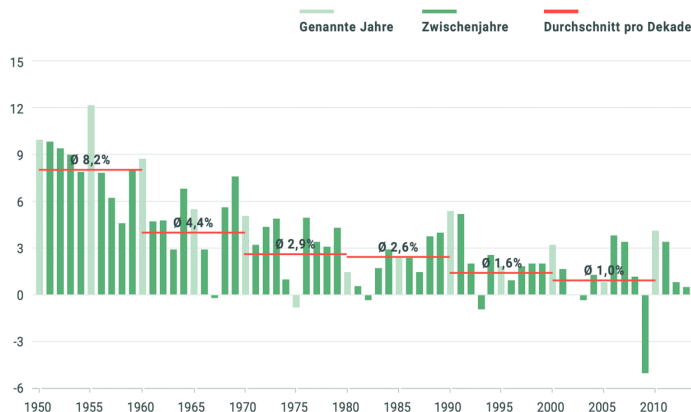
A recent study published by Nber.org shows that a non-marginal part of the Democratic voters who in 2012 voted for Barack Obama and in the 2016 primaries for Bernie Sanders but who then gave their vote to Donald Trump had the "zero-sum" mentality. More generally, zero-sum societies are opposed to immigration, redistributive policies and the fight against climate change.

These are mental attitudes that are sometimes contrary to the interests of those who harbor them and which are therefore difficult to combat with rational arguments alone. Whites in provincial America,

where the economy is languishing, vote against the medical care they would benefit from out of suspicion that other ethnic groups could benefit even more, while in areas with a vibrant economy there is strong support for social care for the entire benefit of others. Even the young French people who defend the pensions of the elderly are victims of an optical inversion.

Italy, with its often radical and populist electoral choices, is an anticipatory case of what can happen in many other advanced societies where productivity and economic growth are slowing down and approaching stagnation (i.e. the risk of zero-sum). In Figure 3 we can see how the German economy is also approaching a condition of stagnation. Significantly, the level of coordination of political forces has also decreased in Germany and political antagonism and social fragmentation have increased.

Figure 3



If the European recovery plan does not have the desired effects, Italian society would once again find itself in conditions favorable to radical and antagonistic choices, no longer counting on further help from partner countries, in particular if the other partner countries also found themselves in similar conditions.

In zero-sum societies, the conventional trick is to make future generations pay the costs, increasing state debt. It is likely that this temptation will prevail again, particularly in a society like Italy which, since its unification in 1861, has always had a level of public debt higher than that of other large economies (with the brief exception of the post-World War II period). If, in a non-cooperative condition of relations with other European countries, Italy aimed to increase, rather than reduce, its level of public debt, it is likely that it would end up clashing head-on with its partners and the European institutions. The first signal is Italy's isolation in the context of the plans to reform the European governance rules. The Italian position is inclined to relax the limits of fiscal discipline as much as possible.

For now, Italy's return to stagnant growth is only a scenario which, everyone hopes, will not come true. But the political implications that would arise from such a scenario represent such a serious risk that a self-conscious reflection on the conditions of the country should be a duty on the part of those who bear political responsibilities today.

The first step should be to take note of the complexity of Italy's social and international interactions, which cannot be reduced to a simplistic representation such as that of antagonism between national systems. According to "zero-sum society" scholars, the very complexity of societies increases the ability to obtain profits not only at the expense of others. There are at least four considerations that should be absorbed into public discourse:

- 1) Openness to trade is a fundamental condition for European prosperity and the hypothesis that Europe as a whole must move away from the German export-led model is in this sense contradictory. For a continent approaching secular stagnation, being able to export is one of the few channels available to avoid zero growth. For this to be possible it is also necessary to develop a European model of global cooperation.
- 2) European public debt is another instrument that can attenuate the social constraints and antagonistic logic that prevail in a society with flat growth, but to be effective it must correspond to a use of resources in favor of future growth, i.e. investments rather than increasing current spending margins at national level.
- 3) Research and investment in technology must be shared between different countries so as not to create "beggar thy neighbor" conditions and to take advantage of economies of scale. Furthermore, the need for technological progress requires us to address the problem of sharing the benefits of increased productivity. Without a reflection on the conditions of inequality, a new antagonistic potential would be created between the "advanced" part of society and the "left behind" part.
- 4) Finally, immigration policies would make it possible to increase the supply of human capital in societies such as Europe, where demographic trends are negative.

It is clear that the political implications of these choices are extremely relevant in a phase in which nationalist rhetoric is resonant in Europe. Italy, with its vulnerabilities, is perfectly at the center of this contradiction.