

ACRI

Association of Italian Savings Banks

74th World Savings Day

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Rome, 31 October 1998

The financial crisis that exploded in Asia in the middle of 1997 and then became global is now affecting the European economy, including Italy's.

Economic activity expanded briskly in Europe in the first half of 1998. Compared with the same period in 1997, GDP grew by 3.2 per cent in France and by 2.9 per cent in Germany.

In Italy it grew by 1.8 per cent.

Investment is still sluggish in Germany, whereas in the United States it is racing ahead at an annual rate of 12 per cent and GDP is growing at a rate of close to 4 per cent.

The underlying cause of the crisis and the reason for its persistence lie in the poor performance of the economy in Japan, where investment is falling at a rate of 8 per cent and GDP at a rate of 2.7 per cent.

Signs of deflation are increasingly visible; the problems of the banking system are growing worse. The intermingling of the financial and industrial sectors has lowered the quality of credit in many Asian countries.

The collapse of commodity prices triggered the crisis of the ruble in August, in an economy suffering from severe structural disequilibria and institutional shortcomings. At times the risk of the crisis spreading to the countries of Latin America has been very great.

The slowdown that occurred in the European economies during the summer has been paralleled in Italy until now by the virtual stagnation of industrial production, which is still below its level at the end of 1997.

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The recovery in economic activity in 1997 has had a positive effect on employment; between January and July of this year there were 80,000 more persons in employment on average than in 1997; most of the increase was in the South of Italy.

The spread of more flexible forms of employment has helped: in manufacturing there has been an increase in the proportion of workers with fixed-term contracts, especially for short periods; in the services sector the use of part-time contracts has grown.

The problem of work is at the centre of attention.

The labour market is highly segmented in Italy. Beside protected workers with regular jobs there are large numbers, especially in the South, with jobs that are irregular with respect to the conditions laid down in collective agreements and often with respect to the laws and regulations concerning social security contributions, taxation and workplace safety.

Official estimates indicate that irregular workers are 31 per cent of the total workforce in the South; this is probably an underestimate. In some sectors of production the proportion of irregular workers tops 50 per cent.

The unemployment rate recorded by Italy's Central Statistical Institute is 6.9 per cent in the Centre and North of the country and 22.5 per cent in the South. Among women it is much higher.

The situation of distress with regard to employment is better expressed by the ratio of persons in employment to those of working age. This index, which includes a large number of irregular workers, is equal to 51 per cent for Italy as a whole and to 40 per cent for the southern regions. It is equal to 63 per cent in France and to 59 per cent in Germany, even though the unemployment rate there is much the same as in Italy. The ratio rises to 73.5 per cent in the United States, reflecting the rapid growth of the economy. Prolonged exclusion from work is harmful to human capital, especially among the young.

The organization of work in firms is gradually becoming more flexible in terms of shifts, working hours and the duration of the relationship.

These changes reduce the time it takes for employment to adapt to demand and link labour costs more closely to seasonal and cyclical fluctuations; they have helped to sustain the level of employment.

Achieving higher and less fitful rates of economic growth remains an essential condition for a large and lasting increase in employment

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The existence of a large proportion of irregular work is first of all evidence that a broad range of activities are not economically viable when carried out in compliance with national labour contracts and the related contributory and tax obligations. The market

tries to find its own equilibrium through grey work. This, however, is deleterious for the efficiency of the economy as a whole because it distorts competition; its effects on civil society are even more pernicious.

Failure to comply with the rules laid down in collective agreements brings workers, especially young ones, into proximity with illegality; it deprives them of the dignity that a legal and lasting employment relationship gives, even when the level of pay is low.

Negotiations between employers and the trade unions must seek to establish, in the first place for the young and in the South, conditions that are less onerous for firms than those agreed at the national level.

In several regions the two sides of industry, with encouragement from the authorities, are already working hard to attain this goal. The significance of a positive outcome to these efforts goes beyond the purely economic sphere; it is valuable for civil society as well.

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For many years unit labour costs rose faster in Italy than in the other industrial countries. The gap widened again in 1996, especially with respect to Germany and France.

The rigorous stance of monetary policy and resolute action to curb the budget deficit have succeeded in bringing inflation expectations down towards the levels prevailing in the countries with more stable currencies. This has had a beneficial effect on labour cost dynamics, with contract renewals tending to limit wage settlements to the lower expected rise in the cost of living and to focus increasingly on regulating the manner in which work is performed.

The growth of the Italian economy nonetheless continues to fall short of that achieved by the other countries of continental Europe, the United Kingdom and the United States. The gap has its origin in factors that discourage investment.

The growing tendency for Italian firms to move production to areas and countries where taxation and labour costs are lower is symptomatic. In some sectors such action nonetheless has a positive side, insofar as it contributes to the defence of market share and domestic employment by permitting a more efficient specialization of production.

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The Italian banking system, on a par with its counterparts in other industrial countries, has withstood the wave of instability provoked by the international financial crisis.

The system's solid capital base, its limited exposure to emerging economies and the Bank of Italy's careful supervision have all played a part. Aside from internal inefficiencies, the instability endemic to southern banks is to be attributed to the serious crisis that has afflicted the economy of the Mezzogiorno in recent years.

Between 1992 and 1997 the GDP of the southern regions grew by only 1.7 per cent; public and private investment contracted; employment fell sharply and consumption slowed.

The major banks, already burdened by high costs and suffering from organizational and operational deficiencies, were unable to cope with the difficulties engendered by the sudden ending of special development measures and the fall in industrial activity.

The action taken by the Bank of Italy and the Treasury, in some cases with the intervention of Parliament, prevented the crisis of the southern banking system from precipitating and has laid the foundations for a recovery of its efficiency.

With the complete opening of banking and financial markets in Europe, numerous foreign intermediaries, mostly from other European countries, have entered the Italian market and are providing innovative corporate finance and asset management services. The ability of Italian banks to provide new services in other European countries remains limited.

There has been a growing tendency for important foreign banking groups to acquire significant equity interests in Italy's leading banks.

On more than one occasion we decided not to allow investments in excess of 5 per cent of the bank's capital in order to ensure its sound and prudent management or to prevent the letter and the spirit of its bylaws from being violated. Larger acquisitions would have hindered reorganization plans aimed not only at improving efficiency but also at allowing banks to achieve a size that would enable them to compete more effectively in the new conditions of international openness.

Where the presence of significant foreign shareholdings fostered or strengthened plans for the consolidation of Italian banks, the initiatives have been welcomed. Three important merger operations involving major banks have already been completed in this way, leading to the creation of groups whose size is also satisfactory from the standpoint of international competition. Plans for further aggregations, constantly monitored by the Bank's Supervision Department, are being drawn up.

The privatization of the banking system is moving ahead rapidly; the share of publicly-owned capital in the banking system as a whole has fallen from 60 per cent at the

end of 1993 to 25 per cent today. Operations now under way will further reduce this figure.

Acting in accordance with the repeated promptings of the supervisory authority, banking foundations have taken the initiative in promoting the creation of stable groups of Italian and foreign core investors to which to sell significant portions of their shareholdings.

The first benefits of the reorganization of the banking system are beginning to appear in banks' profit and loss accounts. Basically stable earnings from credit business have been accompanied by a sharp rise in income from services.

The action taken to curb costs has improved overall profitability. Although net interest income declined with the narrowing of the spread between lending and deposit rates, the return on equity improved considerably in the first half of 1998 compared with the same period in 1997, rising from 1 per cent to nearly 8 per cent on an annual basis. Some of the improvement, however, was due to temporary factors connected with the favourable performance of financial markets; income from asset management could decline in the second half of the year. The strong growth in revenues resulted in the ratio of total labour costs to gross income falling significantly.

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The robustness of the Italian economy has its origins in the high level of actual and potential saving. An efficient banking and financial system is essential in order to transform saving into domestic investment, to the benefit of growth and employment, and to prevent an excessive share of resources from being channeled to other economies.

Between 1993 and 1997 a string of balance-of-payments surpluses allowed Italy to repay its net foreign debt completely. This is one of the fundamental factors in the return to monetary and financial stability.

Italy is about to become a net creditor. The major improvement on this score has been achieved in a context marked by a lack of effective demand, sub-optimal growth and high unemployment.

The meeting of the Group of Seven Finance Ministers and Governors held in Washington at the beginning of October produced a commitment to stimulate economic activity in Japan and to sustain and strengthen growth in North America and Europe.

In the United States the economy and employment continue to expand in conditions of monetary stability. I have already mentioned the rapid rise in investment, a key aspect of confidence in the prospects for growth. The US economy suffers from a persistent shortfall of saving, but it is able to attract enough from the rest of the world to finance its investment.

The European Union has an external current account surplus on the order of \$100 billion, more than 1 per cent of the area's GDP. The growth in investment, although not negligible, is showing signs of faltering as the world financial crisis continues and deepens. Employment is stagnant and unemployment rates are still high.

Support for domestic demand drawing on the excess of actual and potential saving is desirable and possible, without running counter either to the objectives of monetary control or to the reduction in public debts.

In Japan economic activity and investment are contracting, prices are falling and the balance of payments continues to register growing surpluses. Domestic demand needs to be stimulated with expansionary fiscal measures; the Japanese authorities have made explicit commitments in this respect. Halting the decline in economic activity and reviving growth will also benefit the public finances; it will help to shore up the value of a growing proportion of bank credit, which risks becoming uncollectible, and to raise the level of economic activity in numerous neighbouring countries.

Monetary policy's ability to stimulate the area's economy has already been exhausted. Further monetary expansion, although of help in meeting the banking system's liquidity needs, would have no effect on consumption or investment since interest rates are already close to zero. The plan, on a huge scale, aimed at defending the solvency of the banking system has bolstered the yen but, in the absence of a recovery in economic activity, is not sufficient to guarantee the objective of restoring the banks' accounts to health.

Just over a year ago, in the spring of 1997, the IMF predicted that the world economy would expand by around 4.2 per cent in 1998; today, the growth expected is less than half that figure.

North America, Europe and Japan account for about half the world economy. A prompt and effective translation into action of the commitments entered into by governments at the international level can prevent a widespread decline in economic activity.

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The outlook for the Italian economy, which has so far performed unevenly and less well than expected, depends to a significant extent on how the international situation develops. The existence of idle resources and an excess of saving means there is scope for faster growth.

The expansion in investment appears to be smaller than forecast in the spring. This could lead to a slowdown in consumption and a worsening of the outlook for employment.

In the areas where youth unemployment is highest the action to promote contracts that substantially reduce labour costs with respect to the national average must be stepped up.

New impetus must be given to public works and infrastructure investment, which has been seriously held back in the last few years by problems related to the emergence of episodes of corruption, the inadequate project development capability and the shortage of financial resources. Appropriate initiatives on the part of local and central government could stimulate the participation of private capital in the financing of public works.

The results of a recent Bank of Italy survey of a sample of manufacturing firms indicate that the conditions will be right, as early as the first quarter of next year, for a recovery in production from the state of stagnation in which it has so far languished.

The economy's development necessarily depends on the entrepreneurial and innovatory drive of private firms. The cost of labour, the level of taxation, conditions of security and the quality of public services must be such as will permit profitability and competitiveness.

Confidence has its roots in stability and expectations of growth in demand beyond the short term. The fall in interest rates and the launch of the monetary union bode well

for the availability of finance at low cost. The efforts to improve the efficiency of government, already begun with the reforms that have been introduced, must be carried forward. Certainty must be given to the prospect of a reduction, in the medium term, of the main items of public expenditure and the burden of taxation.

In the new phase of economic policy it will be necessary to strengthen the commitment of the authorities, organized labour, private enterprise and the banking and financial system to transform the existing potentialities into an increase in investment and employment.

This must be the hope on the day devoted to the celebration of savings, which are the fruit of man's industry and foresight, in order to dispel the uncertainties weighing on the future of so many families and young people looking for work, and to ensure the steady advance of Italy's economy and civil society.