

CONFINDUSTRIA'S YOUNG ENTREPRENEURS

Conference

Economic democracy

Open market, the ethics of transparency, the participatory society

Enterprise, democracy and economic growth

Address by the Governor of the Bank of Italy

Antonio Fazio

Capri, 5 October 2002

The 2002 edition of the World Bank Atlas shows that in the three years 1999-2001 Italy ranked 28th among the 207 countries classified according to gross per capita income on a purchasing power parity basis, with \$23,470 per person.

For the United States the figure was \$34,100, for Japan it was \$27,080 and for Germany it was \$24,920.

In absolute terms, excluding China and India, Italy is the sixth world economic power; in terms of per capita GDP it ranks last among the G-7 countries.

I. For Italy 1995 was a particularly difficult year. The financial crisis that exploded in Mexico in the very last days of 1994 hit the dollar, which fell by between 10 and 15 per cent against the other leading currencies between the beginning of February and the end of March 1995. The lira depreciated by as much as 17 per cent. The external value of the Italian currency suffered from the marked uncertainty regarding the domestic political situation; this did not prevent the Government from adopting extraordinary measures to reduce the budget deficit by more than 1 per cent of GDP.

The yen appreciated by more than 20 per cent in just a few weeks; the German mark and the French franc also strengthened; the pound sterling, the Spanish peseta and the Swedish krona followed the dollar and the lira down, but not to the same extent.

Despite the fiscal package, the exchange rate of the lira against the German mark, which for some time had fluctuated around 1,000, fell in March to 1,274; the forward rate reached 1,500.

In expectation of an upturn in inflation and a deterioration in the public finances in a rapidly worsening international environment, we had already begun to tighten monetary policy in August 1994.

The half-point increase in the official rates, after more than a year of successive reductions, had the immediate effect of drawing the market's attention to the difficulties looming for the public finances and inflation, and subsequently for the currency. The lira weakened but stabilized again in the autumn thanks to the progressive tightening of liquidity conditions.

The tensions that developed on international markets in the early months of 1995 found the Italian economy in a delicate situation marked by the need to regain credibility. When the fiscal package was introduced, we did not hesitate in February to raise the rate on advances by 1.25 percentage points and the discount rate by 0.75 points.

In a dramatic meeting of the G-7 Governors and Finance Ministers in Washington on 25 April 1995 it was decided to confront the crisis in order to curb the rise of the yen and strengthen the dollar by means of interventions on the foreign exchange market amounting to some tens of billions of dollars.

The fear was that the dollar would go into a free fall, which would have involved the international monetary and financial system and hence the leading industrial economies. Japan embarked on the policy of lowering interest rates that has led in recent years to their being reduced to zero. Interest rates were lowered in France and Germany as well; they were raised in the weak-currency countries.

In Italy inflation was running at close to 10 per cent, partly as a consequence of the depreciation of the lira; the yields on government securities were rising in response to the difficulty of financing the Treasury. In this situation we tightened monetary policy further by mopping up liquidity and, in May, by raising the official rates by another 0.75 percentage points.

The monetary squeeze and the announcement at the Bank's annual meeting that, if necessary, we would have continued resolutely to raise interest rates and tighten liquidity conditions convinced markets of the Bank of Italy's firm intention to check inflation no matter at what cost. Inflation expectations, measured using

appropriate statistical methods, stabilized in the summer and began to come down in the autumn.

The growth in the money supply was reduced drastically in both 1995 and 1996; over the two years it was almost nil.

Relatively small interventions on the foreign exchange market enabled the lira to stay in the dollar's slipstream and, over a year and a half, to rise with the US currency until it was back at the pre-crisis level.

Expectations of high inflation, which would have overwhelmed the Italian financial system and the economy, were dampened.

II. The appreciation of the lira from the second half of 1995 onwards, after the serious crisis of February and March, has only one precedent, that of the autumn of 1947, when the steps taken by Menichella in the context of the policy pursued by De Gasperi and Einaudi, led to the lira, which had fallen from around 200 against the dollar to more than 900, recovering to less than 600.

For fifty years depreciations of the lira had always been followed by stabilization at close to the lowest value reached during the crisis. In the 1950s the German mark was worth around 150 lire, in the 1990s it reached 1,000. From a value of 625 lire between 1948 and 1971 the dollar rose to more than 1,500 and then close to 2,000.

The result was that the lira came to be labeled by domestic and foreign economic agents as a weak currency.

The events of 1995-96 confirmed the validity of the theory put forward by Keynes in the 1930s and revived by Friedman in the 1960s. Faced with inflationary expectations, a reduction in long-term interest rates, which are the most important for investment and economic growth, can be obtained only by sharply raising short-

term rates. Such action curbs the inflationary expectations incorporated in nominal long-term interest rates and ultimately causes them to fall.

Towards the end of 1996 and even more clearly in 1997, thanks in part to the political resolve to participate in the single currency, the interest rates on 10-year government securities (which had risen to around 15 per cent in the most acute phase of the crisis and were still 5-6 percentage points higher than those in the other industrial countries in 1994 and 1995) fell nearly into line with the rates prevailing on international markets.

The exceptional size of the public debt meant that the fall in its cost reduced the budget deficit by more than 5 per cent of GDP every year.

The further reduction in the budget deficit in the second half of the 1990s was mainly achieved by increasing taxes and social security contributions in relation to GDP; compared with the second half of the 1980s, the ratio rose by 6 percentage points.

III. The monetary stabilization after the Second World War was followed by a long period of strong economic growth, accompanied, for more than ten years, by completely stable wholesale prices. The expansion was led by Italian exports' growing penetration of international markets; the annual increase in consumer prices of between 2 and 3 per cent was in line with developments abroad and reflected an improvement in the quality of the goods and services produced.

Up until 1960 GDP grew at an average annual rate of 5.6 per cent; employment expanded continuously. The equilibrium of the public finances was accompanied by a high level of investment. An important contribution to the very rapid growth in industrial output in this period came from the substantial increase in productivity.

The strong growth in economic activity and industrial output continued in the 1960s. By the time that decade came to an end, the Italian economy had been

transformed. Unemployment had fallen to a historically low level. The bulk of value added was generated by industry and construction. The expansion of services was accelerating.

The last part of the decade was marked by serious trade union protests that had a major impact on production and led to a structural shift in the distribution of income to the benefit of payroll workers.

The increase in international raw material prices in the years that followed and the first oil crisis between the end of 1973 and the beginning of 1974 drove inflation up to an annual rate of 20 per cent in 1974. The external deficit was equal to nearly 1 per cent of GDP on a monthly basis. The lira weakened, the *scala mobile* wage indexation system amplified the inflationary pressures by passing the increases in prices through to labour costs.

The drastic monetary tightening imposed in 1974, through the introduction of ceilings on bank lending, halved the inflation rate but put a brake on growth; it prevented the collapse of the bond market, which was able to go on financing firms' capital spending.

In a context marked by greater uncertainty, industrial and political strife led to increases in nominal earnings in industry of 25 per cent in both 1974 and 1975; the lira weakened further; drastic exchange controls were imposed; inflation surged, requiring a parallel increase in interest rates. Although calls for a "belt-tightening policy" were not lacking, the theory that wages were independent of the economic context came to hold sway. A growing gap opened between government expenditure and revenue; the public debt took off.

The average annual rate of GDP growth was 2 percentage points lower in the 1970s than in the two preceding decades.

The 1980s opened with another oil crisis, to which the Bank of Italy responded with another monetary squeeze.

The widespread problems of industrial firms, especially those most exposed to increases in energy costs, led to extensive restructuring in the sector with the shedding of large numbers of workers, who ended up by increasing employment in

services. The concept of wages as an independent variable came to be seriously questioned.

Italy's participation in the European Monetary System required a rigorous monetary policy to be maintained throughout the 1980s. Interest rates were regularly raised to keep the exchange rate steady and sell government securities; this caused a further increase in the public debt and limited firms' capital spending.

The restrictive monetary policy and the fall in oil prices in 1986 curbed inflation.

The fall in the cost of energy, industrial restructuring and the reduction in the rate of increase of wages made it possible towards the end of the decade for profits to return to a level closer to that prevailing in the other industrial countries.

The GDP growth rate declined by another percentage point compared with the 1970s, to around 2.3 per cent.

In the early 1990s the Italian economy suffered badly from the crisis of the European Monetary System in 1992, which involved the lira and the pound sterling, and from that in 1993, which led to the generalized widening of the fluctuation band to 15 per cent.

In 1993 the international economy performed poorly, but the Italian economy even worse because it was necessary to undertake a major fiscal adjustment in order to counter the continuous deterioration in the external accounts, the weakness of the exchange rate and the increase in prices. The fall in domestic demand and investment was very sharp. There was a substantial reduction in employment and unemployment increased.

The lira depreciated and at the end of the year the exchange rate against the German mark was more than 900.

Inflation was held in check by yet another monetary squeeze and the agreement on an incomes policy that was reached between employers, trade unions and the Government.

The depreciation of the lira led to a strong recovery in Italian exports in 1993 and 1994.

IV. In 1995 Italy's GDP, boosted by the expansion in exports generated by the further fall in the exchange rate, grew by 2.9 per cent.

In the years that followed the stabilization of prices, the strengthening of the lira, the fall in interest rates and the reduction in the budget deficit were not accompanied, in contrast with what happened after the Second World War, by an upturn in growth. Exports slowed; the increase in output was inadequate.

Between 1995 and 2001 Italian exports of goods and services expanded by 25 per cent in real terms; Germany achieved an increase of 58 per cent, France one of 48 per cent. Italy's share of world trade in manufactures contracted by 20 per cent.

In the same period Italian GDP grew at an average annual rate of 1.9 per cent, Germany recorded a rate of 1.6 per cent, France one of 2.5 per cent. Italy's result was well below the average annual rate of the European Union, 2.4 per cent. The growth of the seven leading industrial countries averaged 2.6 per cent.

Italy has lost ground in terms of per capita GDP, in Europe and among the other industrial countries. The performance of the economy in 2002 will not improve the situation.

The analysis of per capita GDP shows a variegated picture for the regions of the Centre and North and those of the South. Some of the former can be classified among the most advanced in Europe; some of the latter are economically backward.

Three quarters of Italian manufacturing capacity is located in the regions of the Centre and North.

Compared with the average level in 1995, the index of industrial production in the 15 euro-area countries had risen by 14 per cent in the middle of 2002; in France it had risen by 17 per cent, in Germany by 16 per cent.

In the United States the index rose over the same period by 23 per cent; in Japan, embroiled in serious structural difficulties, it fell by 3 per cent.

In Italy comparison of the average value of the index in 1995 with its level in the middle of this year shows a rise of 4 per cent, one third the European average.

V. In my Concluding Remarks to the Bank of Italy's annual meeting on 31 May I examined at length the Italian economy's loss of competitiveness in the second half of the last decade.

That period saw the correction, at least in part, of imbalances in the public finances accumulated in earlier decades, but, in the absence of growth, a high price was paid in terms of private-sector disposable income. Profits, although down compared with the late 1980s, remained satisfactory. Thanks to the flexibility introduced into the labour market, the reduction in the number of persons in work in the first half of the decade was more than offset, but at the margin the quality of employment deteriorated.

The banking system has been privatized; extensively restructured. It has improved its ability to compete abroad and the support it provides to economic activity within Italy.

The stabilization of the exchange rate, the curbing of inflation, the decrease in interest rates and the large reductions in the budget deficit, which enabled Italy to adopt the single European currency, have not been matched by the ability of the private sector to reap the benefits of monetary and financial stabilization, with growth rates in line with the European averages.

We have not kept up with the other industrial economies.

Labour productivity, although high on the basis of hours worked, and total factor productivity have increased less than in the other leading countries. The average size of firms has undergone a significant contraction; measured by the number of employees, it is about half the European average.

There are only a few large firms and only a limited number of medium-sized firms. A birth rate for firms comparable with that of the other industrial countries is coupled with an inability to grow.

In industry firms with more than 500 employees account for less than 15 per cent of the sector's total employment. The corresponding indicators are on the order of 40 per cent in France, 50 per cent in the United Kingdom and more than 60 per cent in the United States.

The presence of Italian firms in high-tech sectors is scant. In terms of value added such firms account for 6 per cent of the total, compared with 10 per cent in France, 26 per cent in the United States and 14 per cent in Japan.

World demand for high-tech products is growing twice as fast as that for other goods. The reduction in Italy's share of world trade is largely due to the composition of our output.

There has also been a steady loss of share for medium-technology goods, both in international markets and in the domestic market.

The weakness of Italian industrial production, underscored by the stunted growth of recent years, is an indicator of the Italian economy's loss of competitiveness. This is reflected, in the new context of European and global economic relations, in a low level of investment and slower growth.

The labour force participation rate is significantly lower in Italy, much lower in the South, than in the other industrial countries.

The proportion of self-employed workers is especially high. The underground economy is abnormally large. These are both indicators and causes not only of a low level of competitiveness but also of widespread social malaise.

VI. At the Bank's annual meeting, in addition to the causes of Italy's loss of competitiveness, I also discussed the possible correctives needed to prevent our economic and social system from losing further ground among the advanced countries and being pushed in some respects to the sidelines of the more highly developed economies.

In the 1990s important measures to curb spending on public employees, social security and health care slowed the surge in these items of expenditure, which was partly due to the aging of the population. Italy did not succeed, however, in bringing the rate of growth in public expenditure below that in GDP.

The consolidation of the public finances was entrusted, as I mentioned earlier, not only to the fall in interest rates but also to an increase in revenue.

A contribution to curbing the deficit came from the reduction in investment in infrastructure. The endowment of public capital is insufficient in the most highly developed regions of the Centre and the North; it is even more inadequate in the South.

The increase in the ratio of taxes and social security contributions to GDP, until it came into line with the European average, occurred in a context of insufficient efficiency and shortcomings in public services. Business investment in the second half of the 1990s grew at a satisfactory pace, reflecting the favourable tax treatment, the lower cost of funds and the reinforcement of the banking system.

Investment is currently depressed primarily by the difficulties affecting financial markets, the uncertain state of the world economy and the lack of a clear growth scenario in Europe and Italy.

The growth prospects of the Italian economy depend on the wisdom and farsightedness of political action and the creation of a macroeconomic environment conducive to growth.

In order to make the desirable reduction in the tax burden credible and lasting, it is necessary to reduce current expenditure excluding interest payments in relation to GDP. It is necessary to boost spending on public works and public investment, implement the Pact for Italy, increase the flexibility of the labour market and raise the productivity of the public administration.

The public sector now accounts, in terms of value added and transfer payments, for more than 40 per cent of GDP. In addition to the immediate positive impact deriving from a reduction of costs in relation to the value of what is produced, an increase in the effectiveness of the activity of the public administration can give a major impulse to the productivity and efficiency of the economy.

We must invest in education and culture, *inter alia* through a new relationship between universities and firms, support the educational role of the family, capitalize on Italy's enormous cultural and environmental wealth, and increase spending on research, which is particularly low by international standards.

The conditions must be created that will reverse the shrinking of the average size of firms and increase the opportunities for them to expand, *inter alia* by pursuing a policy aimed at increasing Italy's diplomatic, cultural and economic presence in foreign markets, as planned by the Executive. Greater use must be made of new technologies in order to enhance productivity and increase the competitiveness of Italian goods in international and domestic markets. The legal framework for the working of the economy needs to be brought up to date.

VII. A fundamental factor in every economic advance is Man, with his ability to foresee, plan, work and realize.

This is the vision of the great classical economists, Adam Smith and David Ricardo, kept alive through to our own times by Keynes, Samuelson, Solow and Modigliani.

Recent research on the structure of the economy of the leading industrial country, the United States, concludes that nearly all the wealth, and therefore productive potential, consists of what is technically known as human capital. The proportion is in excess of 90 per cent. Productive capital in the form of factories, plants, organizational and IT systems, together with roads, bridges, airports and

other public infrastructure, wealth made up of houses and land, and, lastly, gold and net financial assets account for less than 10 per cent of total wealth.

It is an economy in which more than 70 per cent of value added is generated by traditional and advanced services, whose production is based largely on labour. But in comparison with physical capital, human capital also plays an important role in industry, where plant and machinery account for a major share of the total.

This is confirmation, at the end of the twentieth century, of the intuition of Adam Smith, considered the founder of modern economics, who in 1776, in *The Wealth of Nations*, affirmed that this consisted basically in the ability of men to work and produce.

In the great political and economic controversies work has often been identified with payroll employment.

The ability to contribute to the wellbeing of the community exists in jobs of every kind, from those of a spiritual, intellectual or moral nature to those consisting prevalently in a material activity. Every form of work is noble, considering the effort it requires and the contribution it can make to the common good.

In a well-organized society, all the different forms of work, of effort, that contribute to a nation's economic and social welfare must cooperate and complement each other harmoniously.

The Italian Constitution makes work the cornerstone of the Republic.

VIII. In every economy, the level of activity, current output, and economic progress depend on firms.

The entrepreneur organizes labour, with the help of the financial resources he possesses or borrows from the market he endows it with physical means of production. He creates value, not in the banal sense of the financial markets, but in

the fundamental sense of growth; he produces goods and services whose market value remunerates the factors of production, his work and the risk he runs.

The market encourages the division of production and specialization by each firm; it rewards those that supply goods of use to the community; it expels those that are unable to direct their efforts towards a useful end; it optimizes the combination of productive factors; and it maximizes the quantity and quality of goods produced.

Using existing techniques and inventions and introducing new methods of production and new products, the entrepreneur gives an impulse to economic growth, to the benefit of the community; he determines the direction of this growth, in terms of goods and services produced and supplied to the market.

The action of the State, the public authorities, the institutions is essential for the profitable performance of economic activity.

The State must provide the economy with public goods and infrastructure that competition and the firm are unable to produce; the collective use to which they are put means they cannot be remunerated in relation to the amount they are used. Public goods and infrastructure do not have to be produced by the State. Private enterprise can provide goods of public utility, but in accordance with the policy and at the initiative of the authorities. The economic operation of such goods requires the possibility of applying charges based on their utilization.

The market must be regulated. For the purposes of competition, there must be complete information and correct conduct. Laissez-faire, especially in the financial domain, can lead to results that are detrimental to the wellbeing of the community.

The State pursues ends that go beyond the economy by means of activities that are essential to social life, the good life of the people, the eudaemonia of the ancient philosophers, the common good.

The State is entrusted with justice, defence, public order and foreign policy.

The economy is part of social life. A good organization of the latter and its orderly functioning constitute the environment in which the economy operates and grows.

Fairness in exchange relationships, commutative justice, is essential to the proper functioning of the market. If the relationships between firms and between firms and the other parts of the economy — consumers and workers — are not correct, the market does not bring progress but involution.

The law punishes deviant conduct, but observance of the rules is ordinarily entrusted to ethics, professional deontology, the honest behaviour of each agent. The violation of ethical norms also has repercussions in the economic field.

The political sphere makes the fundamental choices concerning the community and to some extent indicates the direction for economic activity. The State is not an absolute sovereign, it is a means of pursuing the good of the community, to which it is accountable for its actions.

IX. The essential relationship between the market economy and democracy is immediately apparent.

The absolute sovereign State, whose activities and decisions are not subject to questioning by the people it rules over, was seen in the early modern age in the form of monarchies endowed with a power that claimed to come directly from God.

In reality, these theories sought to justify and legitimate forms of government that almost always derived from military domination and conquest.

A form of absolute dominion, experienced with tragic results in the course of the twentieth century, was that of the dictatorships: Fascism, Nazism, Communism.

The terrible experience of the socialist regimes, in some respects the final outcome of the industrial revolution and of the development of standardized, mass production beginning in the nineteenth century, came to an end only in 1989.

The economy, it has been said, is part of society. It can condition it and in extreme cases subvert it. A severe crisis of the world economy, that of the 1930s, now remembered as the Great Depression, had created imbalances in the relations

between nations and within the most highly industrialized countries. The result was another tragic political experiment, Nazism, in a great nation that was the leading industrial power of central Europe.

After the Second World War, democracy resumed its progress.

Free enterprise, the foundation of economic progress, is part of a broader set of civil and political liberties. These in turn are the expression of Man's spiritual dignity. Democratic institutions and their stability lend strength and support to the great economies.

The advanced and historically stable economies are politically organized as democracies. The economy can prosper for a time in systems where the fundamental freedoms and human rights are restricted, but in the end the conflict explodes to the ruin of all.

Democracy must be complete. The enjoyment of social and political rights must go together with the participation of every individual in economic wellbeing, the fruit of organized social life.

In modern democracies it is a social community, a population bound by ties and historical traditions, by shared language and culture, that by means of a constitutional pact chooses its representatives who preside over the establishment of the laws, the election of the organs of government.

The State guarantees the organization of social life in which economic activity is carried out and the market operates.

The legislative branch, made up of members elected by the community, and the executive branch, which presides over the functioning of the State, are ultimately subject, through free elections, to the control of the community and each of its members.

X. Democracies, in a classic definition "government of the people, by the people, for the people", are the most advanced form of political organization,

capable of realizing the moral, intellectual and economic potential of individuals and their free associations.

However, democracies are not immune from pathologies that can undermine their proper functioning, with deleterious effects on social and economic life.

The representatives elected by the people to foster general interests, even if they interpret them in different and sometimes opposite ways, must not direct their action to represent interests conflicting with those of the community.

The line dividing group interests from general interests can sometimes be tenuous.

In federal states, the representatives elected in one of the legislative bodies are explicitly designed to represent the interests of a region. But their action can never go so far as to prefer partisan interests to the point of harming higher general interests; every legislative assembly must ever-more explicitly aim to serve the latter. The analysis, intellectual honesty and moral rectitude of the freely elected representatives must always have as their objective the good of the nation.

Existing within the State, and compatible with it, are associations and organizations that care for particular interests of individuals and organized groups, interests that the State recognizes as elements of society that are worthy of protection. The relationship between social representation and general political representation has become more complex.

These intermediate organizations, bearers of legitimate interests of important segments of the population and the economy may acquire *de facto* an ability to shape decisions and policies that influences the will legitimately expressed, in the interest of the whole community, only by Parliament.

It is not a question of the principle of subsidiarity, whose value, on the contrary, must be resolutely enhanced. Neo-corporatism can certainly play an important role in interpreting and defining interests of significant elements of society. But these forms of political and social organization can develop in a way that risks overstepping the bounds explicitly or implicitly established by the Constitution.

The instability of governments backed by uncertain majorities has at times resulted in important decisions and policies being delegated to these forms of representation, which have contributed on more than one occasion, in recent years, to the orderly and fruitful development of economic life.

The ultimate power over every decision affecting the community as a whole must rest with Parliament, which must not simply ratify agreements reached at lower levels but reconcile them with the general interest.

Decisions can embody the interests of several elements of society, but never to the detriment of the common good of the nation.

XI. In the current phase of history characterized, thanks to the development of communications and especially information technology, by an unprecedented opening up to trade with every other part of the globe, the ability of the entrepreneur to read and analyze situations, to foresee changes, to adjust plans and the organization of factors in a mutable and increasingly competitive environment, is of crucial importance for the firm, for its viability and consequently for the progress of the economy.

The technical and professional culture of the entrepreneur remains fundamental, but it is no longer sufficient.

It is necessary to interpret the times and the changes that are taking place in the context in which the firm operates, a context that used to be local and predictable and has now expanded greatly to include other parts of the world that may be geographically and culturally distant.

One must never, it must be repeated, lose the profound understanding of the context in which one acts. The situation requires, especially of you young entrepreneurs, a cultural openness — not only aesthetic and even less merely superficial, but also of an economic, social and human nature. Along with intuition and creativity, it is necessary systematically, by strengthening your structures and drawing on outside resources, to promote the study of the global economic environment and the profound tensions affecting and shaping it.

The ability of the entrepreneur must be accompanied by a corporate organization and labour relations in keeping with the new times.

It would be a mistake to harm the security of workers and their dedication to the goals of the firm.

Although class struggle and the consequent attitudes in industrial relations have been left behind, not least because they were overwhelmed by history, there certainly remains a dialectical contraposition between employers and employees, between labour and capital.

But in a long-term perspective the two sides must necessarily agree on the objectives.

The viability and growth of the company are of primary interest both to the employees and to the firm and those who finance it.

In an increasingly competitive world, the development of output, its quantity, cannot be taken for granted.

The entrepreneur does not aim only at his personal profit, as a shallow popularization would sometimes have us believe; the entrepreneur seeks, must seek the good of the firm for which he is responsible and of the people who work in it. He must contribute, with the goods and services he supplies, to the growth of the economy and the welfare of the community.

There is a social function of the firm, not decreed by law but innate.

I shall just touch on the theoretical elaboration of the share economy, proposed in fuller form and with utopian aspects by the great British economist James Meade and in a more technical form by Weitzman.

On the practical plane that theory suggests forms of variation in the wage bill during the life of the firm and the economic cycle, by means of which to provide a reward for the possibly greater-than-expected success of the firm's activity. It is also

necessary to create a wage structure that will ensure the viability of the firm in downturns as well, preventing these from affecting employment.

By allowing the wage bill to fluctuate, within well-defined limits, variations in employment and, ultimately, a lower level of employment are avoided.

Initial timid applications of these historical visions have been productivity-linked pay, variable working hours and, finally, fixed-term hiring.

This approach, whose ultimate aim is to ensure the viability and development of the firm and the stability and growth of employment and output, can and must be translated into more advanced forms of industrial relations, into a new diversification of income from salaried employment.

It is up to the representatives of the social partners to define the scope and structure of these new relations. The consequences are to be drawn in terms of bargaining levels, the aim being for negotiations to be close to the life and activity of the firm.

The social doctrine of the Church, as expressed in *Pacem in terris*, itself considers a wage to be composed of a part that allows him and his family a standard of living consistent with human dignity and another part which remunerates the employee's ability and effort and his contribution to production. The second component can vary with the quantity and quality of production, but also with the business cycle and the circumstances in which the firm has to operate.

Flexible forms of employment have had the great merit of increasing employment substantially after the crisis of the 1990s.

A system of industrial relations established at the end of the 1970s, basically geared to a productive structure consisting typically of large enterprises producing standardized, mass goods and operating in an economy implicitly assumed to be in continuous expansion, was replaced, with the reforms of the 1990s, by a more flexible system of labour relations, one more consonant with the new economic environment.

However, on the one hand flexibility becomes precariousness in the absence of growth; on the other, in the case of unskilled jobs, it can impair productivity and the employee's identification with his company's goals.

Training remains essential.

The approaches to work and industrial relations need to be further developed, starting out from the ideas developed by Ezio Tarantelli and Massimo D'Antona. It is necessary to move along the lines of the so-called Labour Charter to which Marco Biagi devoted so much of his social and intellectual commitment. These approaches are largely incorporated into the Pact for Italy.

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On several occasions I have recalled that Italy does not fully utilize its endowment of labour, savings and hence capital, entrepreneurship and cultural and environmental resources.

In the first part of my speech I described the origin, incongruences, imbalances and structural problems of our economy.

Understanding them indicates the paths for solving them. Structural reforms are necessary in order to remove the incrustations of a period going back to the difficulties that began in the 1970s.

The appearance of new difficulties in the course of time has often prevented us from grappling with the problem at the roots. Reforms are the way to prepare a better future and we cannot shirk them.

In the field of the public finances, it is necessary to aim at a configuration that raises the quality and quantity of services, while simultaneously reducing costs and increasing the efficiency of the sector and the effectiveness of interventions.

The redesigning of the welfare state, acknowledging what is unsustainable, must aim at preserving and strengthening this great conquest of all the advanced countries in the last century.

The evolution of the world around us and globalization pose new problems but also open up new horizons for the growth of production.

The “novelties” must be confronted by business, by the social partners, by the public authorities, abandoning old approaches and operating according to criteria adequate to the times, with decisiveness and clear thinking.

On momentous objectives, points of convergence can be found in the common interest. The South must constitute a resource able to contribute significantly to the growth of our economy; it is necessary to close the gap that still exists between the two Italies. The efforts of government must be flanked by those of business in these regions. This is necessary in view of the still severe imbalances between the South and the rest of the country, the high level of unemployment, the sometimes difficult social conditions. The modernization of the public administration is a task for government. It is also up to government, with the cooperation of private enterprise, to endow our economy with a modern system of infrastructure.

It is firms that identify the lines along which production is developing; they follow them by organizing and activating the factors of production.

An environment conducive to such growth must be created on the one hand by public services and the tax system, on the other by a concordance of strategic objectives and industrial relations and by an income structure consistent with the goals agreed between the social partners.

Research and education must provide the foundation for technological advance and for innovation in production.

The engine of growth is the development of human capital, consisting of professional ability and culture.

It is the desire to work well, to improve, that drives growth and leads to development. You young people must venture, innovate, risk. A new page of economic democracy must be written.

The ultimate factor of all progress is Man, with his cultural openness, his ability, his social and moral spirit.