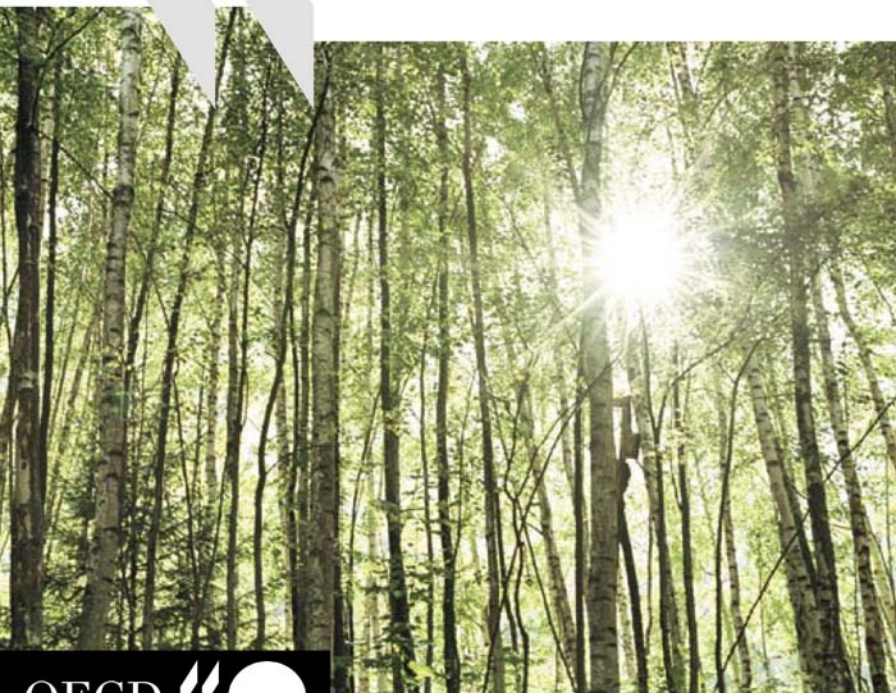




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Economic Surveys**

**Italy**



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# **OECD Economic Surveys**

## **Italy**

**2005**



ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

# ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

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*This Survey is published on the responsibility of the Economic and Development Review Committee of the OECD, which is charged with the examination of the economic situation of member countries.*

*The economic situation and policies of Italy were reviewed by the Committee on 16 December 2004. The draft report was then revised in the light of the discussions and given final approval as the agreed report of the whole Committee on 26 January 2005. Due to exceptional procedural delays in the publication process not all the information is up to date.*

*The Secretariat's draft report was prepared for the Committee by Alexandra Bibbee, Flavio Padrini, Paul O'Brien and Céline Baptista under the supervision of Nicholas Vanston.*

*The previous Survey of Italy was issued in March 2003.*

*This Economic Survey may not include an examination of certain policies that are relevant to the country but fall within the competence of the European Community. While some of these policies may be examined in the Survey of the Euro Area, other policies may not be examined by the EDRC, as the European Commission currently maintains that the Economic Surveys should be limited in their coverage. No limits apply to the policies that can be covered in the Economic Surveys of other OECD countries.*

*The Commission and the member States of the European Union are working actively on ways of reviewing EC and EU wide policies within the context of the EDRC.*

## BASIC STATISTICS OF ITALY

### THE LAND

Area (thousand sq. km.)	301.3	Population of major cities (thousands, 20.10.2001)	
Agricultural area+ (thousand sq. km, 1995)	165.2	Rome	2 547
		Milan	1 256
		Naples	1 005
		Turin	865

### THE PEOPLE

Population , 31.12.02, thousands	57 321	Labour force, 2003, thousands	23 918
Number of inhabitants per sq. km	190	Employment, 2003, thousands	21 822
Net natural increase, 2002, thousands	-19	In agriculture	1 075
Net rate per 1000 inhabitants, 2002	-0.4	In industry	7 019
		In services	13 728

### THE PRODUCTION

Gross domestic product in 2003, billions of euros	1 302.0	Origin of gross domestic product in 2003 at market prices, per cent of total	
GDP per head (2003, US\$)	25 592	Agriculture	2.2
Gross fixed capital formation		Industry	23.3
Per cent of GDP in 2003	19.1	Construction	4.9
		Other	69.6

### THE PUBLIC SECTOR

Current expenditure in 2003 (percentage of GDP)	48.9	Gross financial liabilities in 2003 (percentage of GDP)	121.5
Current revenue in 2003 (percentage of GDP)	46.4	General government investment in 2003 (percentage of total investment)	16.3

### THE FOREIGN TRADE

Exports of goods and services, as a percentage of GDP, 2003	25.4	Imports of goods and services, as a percentage of GDP, 2003	24.8
Main export categories, as a percentage of total exports, 2003		Main import categories, as a percentage of total imports, 2003	
Manufactured goods	35.3	Foodstuffs	7.1
Fabric and textile goods	14.7	Manufactured goods	25.4
Chemical products	9.5	Metal, ores and scrap	9.1
Transport equipment	10.7	Chemical products	13.6
Mineral fuels	2.1		

### THE CURRENCY

Monetary unit: Euro		Currency units per US\$, average of daily figures:	
		Year 2004	0.8049
		December 2004	0.7454



## Executive summary

**A modest recovery is under way.** A recovery has been under way since early 2004 and is expected to proceed at a moderate pace in 2005 and 2006, with domestic demand continuing to rise faster than GDP. Real growth is projected to remain somewhat slower than the EU average. The gap in consumer price inflation is expected to widen again in 2006. The current-account deficit has increased and export market share losses were substantial until recently. Employment growth has been impressive throughout the slowdown, but the growth of productivity, including that of total factor productivity, has been very weak.

**The public finances present a mixed picture.** Although declining, the debt level still exceeds 100% of GDP. The primary surplus has fallen significantly, and repeated resort to one-off measures has until now substituted for the implementation of deeper-seated reforms. The exceptional revenue measures have prevented the fiscal deficit from exceeding the 3% limit while limiting the negative impact on the economy. The Italian authorities are committed to pursue the phasing out of one-off measures by 2006. The OECD estimates that further structural measures may be needed to reach budget targets in 2005. Although the overall tax burden is not high, the tax system discourages entry in to the formal labour market: a € 6 billion income tax cut is planned for 2005. Devolution is making it more difficult in practice to control public spending. A series of recent pension reforms will contain future spending in that area and encourage workers to remain longer in the labour market. A sustained rise in the primary surplus is required to put public finances on a sound footing.

**Product-market competition needs strengthening.** Large parts of the service sector face competitive pressures that are too weak to encourage managerial or technological innovation, or to resist cost increases, which are then passed through to the traded sector. A stronger commitment to regulatory reform and liberalisation in product markets is required and remaining subsidies to industries should be based on social cost and benefit grounds. Once adequate competition is ensured in the electricity sector, and an adequate regulatory structure put in place, full privatisation should not be delayed. Other candidates for regulatory reform and other liberalisation efforts include the transport sector, road freight, professional services and retail trade. The latter often faces opposition from shopkeeper-captured local authorities and monitoring and benchmarking from central authorities would be crucial.

**Further corporate governance reforms should not be delayed.** Recent scandals have highlighted particular corporate governance problems and the policy reaction was swift, but incomplete. The ability of minority shareholders to play an appropriate role could be improved. The division of competencies among the supervisory authorities is in need of adjustment. It is regrettable that recent proposals to rectify these issues have not yet been implemented. Bankruptcy proceedings for smaller firms are prolonged and too close to criminal proceedings, potentially productive assets are dissipated, and entrepreneurs discouraged from continuing their activities. Speeding up of reforms in this area also is desirable.

**Labour market developments have been positive.** Reforms in the labour market have been far-reaching and have delivered higher employment and falling unemployment. Job security for those on temporary contracts is being improved. Job protection for insiders remains high, however, and there are major differences in labour market outcomes between the regions. Large-scale immigration, much of it clandestine in the past, is a recent phenomenon, and immigrants find work in areas where there are chronic labour shortages. Repeated regularisation exercises show that large numbers are willing to work in the formal sector. More could be done to extend legal immigration and aid immigrants to fit into the Italian society and economy.



## Assessment and recommendations

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*Job creation has been strong, but growth weak, posing budgetary difficulties*

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In recent years, Italy's GDP growth has been below the euro-area average, and total factor productivity growth has been very weak, and even negative. The OECD estimates that the potential growth rate of GDP, possibly only temporarily, has fallen below 1½ per cent. Consumer price inflation has been faster than in the euro-area and relative unit labour costs in both the non-traded and traded sectors have been rising steeply. On the positive side Italy is one of the very few OECD countries to have enjoyed robust employment growth every year since the turn of the century, and its unemployment rate has fallen substantially. Italy managed to respect the 3% Stability and Growth Pact limit on public deficits despite slow growth thanks to sizeable one-off measures. The latest pension reforms will help reduce the growth of public pension spending in future decades by raising the effective retirement age. However, the structural deficit is still significant, gross debt remains well above 100% of GDP, decentralisation is complicating the task of maintaining fiscal discipline, and repeated tax amnesties carry the risk of encouraging tax avoidance and evasion in the expectation of further amnesties. Substantial efforts are needed in coming years, both to assure effective implementation of a fully-funded € 6 billion personal income tax cut that is planned for 2005, and to phase out completely by 2006 the one-off measures that reduced budget deficits in recent years. In sum, although Italy now seems to be recovering from the recessionary influences of the past 2-3 years, medium-term growth prospects seem poor, mainly because productivity growth and competitiveness remain weak. Italy's ageing population will act as a further drag on per capita income growth in later decades, making harder the task of reducing both public-sector deficits and debt while increasing the need to do so.

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*The key challenges are to raise potential growth while maintaining financial discipline*

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The challenges are thus to durably raise real per capita income growth rates and improve the public finances. Two main paths for policy are indicated:

- *Stimulate the supply side.* A series of growth-enhancing measures are needed which should aim to: implement more forcefully policies that will put the non-traded sector under stronger competitive pressure to seek cost-saving innovations; reform bankruptcy legislation that maintains high exit costs for both creditors and firm owners, and corporate governance structures that encourage financial opacity; continue policies that encourage employment creation in the formal sector, while taking stronger measures to raise human capital at all ages.
- *Make determined efforts to reduce public debt and deficits on a permanent basis.* Further savings can be made in public employment, government purchases and subsidies and it is

especially important to ensure that decentralisation is implemented through efficiency-raising measures rather than duplication of posts. Continued forceful action is also required to prevent health spending from exceeding pre-agreed benchmarks. The tax base should be enlarged via simplification of the tax codes and more vigorous efforts to reduce evasion and avoidance. Tax rates should be reduced if and when they can be financed by permanent spending economies.

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### *A gradual recovery is underway*

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The prolonged period of slow growth is ending. Exports are picking up and the erosion of market shares in volume terms has slowed. Private consumption growth is expected to continue to outpace that of GDP, and there are signs that private investment demand is recovering. Employment growth remains positive and private sector wage claims remain moderate, especially in real terms. The short-term outlook is for continued moderate growth, with the output gap narrowing in 2006. There are signs, though, of financial stress in the manufacturing sector, which has yet to emerge convincingly from a 4-year long recession, and worries that Italy's small enterprises in the traditional textile and footwear sectors are losing out to Asian and eastern European rivals, exacerbated by the strength of the euro and a domestic inflation rate that is higher than the euro-area average. And although Italy has a relatively low dependence on imported oil, a prolonged period of high oil prices would have a negative impact because of weaker demand in most trading partners and stronger domestic inflation pressures, and because Italy's exports to oil-producing countries are small relative to GDP.

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### *Economic recovery will not by itself resolve the fiscal issues*

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As with many other EU countries, Italy's public finances deteriorated when growth slowed abruptly late in 2001, but the authorities continued to respect the 3% of GDP reference value of the Stability and Growth Pact, resorting to asset sales and one-off measures with limited demand impact, notably tax amnesties. The recovery will bring some fiscal improvement, but not enough by itself for Italy to remain under the 3% limit. In any case, there has been a trend deterioration in the underlying fiscal position since before the 2001-2003 slowdown, with the cyclically-adjusted primary surplus falling from around 6½ per cent, of GDP in 1997 to an estimated 2% by 2004 because of a strong upward dynamic in public spending. The OECD projects further falls in 2005 and 2006 on the basis of announced policy measures, with the public-sector deficit exceeding 3% of GDP in 2005, more so in 2006. This is despite the policy of capping current public spending growth (except on pensions) at 2% for 2005, together with revenue-enhancing measures. Sales of public assets, especially real-estate, are set to continue, and prior securitisations of such sales will continue to help net borrowing in 2005. *Reaching the official budget goal of a 2.7% deficit for 2005 may require additional consolidation measures as well as close monitoring of anti-evasion programmes and adherence to the spending caps.*

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### *More determined action to reduce the deficit will be needed in the medium term*

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Given the high debt-to-GDP ratio, the priority for fiscal policy must be to reduce it substantially over the medium term. Much larger primary surpluses are necessary than those realised in recent years or projected by the OECD, and other debt-reducing measures should be undertaken. Although the latest medium-term fiscal plan (DPEF) postulates an improvement in the primary balance by some ½ per cent of GDP each year until 2008, it does not give precise indications as to how this is to be achieved, whereas Italy's underlying primary spending has been rising faster than the means of financing it for many years now. *A more detailed multi-year budgetary process is therefore desirable. One-off measures should be phased out completely by 2006 as planned, and be replaced by permanent cuts in structural spending programmes, preferably large enough to make room for subsequent growth-enhancing cuts in tax rates. When the output gap has been closed, Italy should further strengthen its consolidation efforts.*

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### *Action should concentrate on spending cuts*

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Some spending cuts can be achieved by improving administrative efficiency: duplications of functions across different levels of government should be avoided while decentralising and the coming retirement of baby boomers should be used as an opportunity to achieve net reductions in staffing levels. Increases in public sector salaries should be limited to moderate rates, in order to be consistent with the new spending growth caps. Priority in spending should be given to improving infrastructure, especially in the south, and human capital. As in virtually all OECD countries, public spending on health is on an upward trend. Insofar as health services are a superior good and households are willing to spend more on them as their incomes rise, this need not be a problem in itself. But this should include a higher level of co-payments, continuing careful scrutiny of regional proposals and outturns, and more benchmarking across regions. Both spending control and efficient delivery are complicated by the fact that health spending is decentralised, yet financed essentially by the State, and wage levels are fixed at the central level. On the pension side, the recent reform is a major one though it is regrettable that it has been delayed to 2008. An updating of benefit coefficients to reflect increased longevity is due in 2005, and it should not be delayed. Further debt reduction measures should include stepped-up privatisations, including in network industries, to attain the € 100 billion target (about 7% of 2004 GDP) of the latest DPEF.

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### *The tax system is being reformed*

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Although Italy's overall tax burden is not above average, including tax on personal incomes, the existence of a large-scale informal sector means that those who pay taxes face high average and marginal rates, which distort work effort and encourage informal working, exacerbated by the fact that the tax codes are complex, making compliance time-consuming. After a pause for most of the 1990s, amnesties were used extensively during the period of slow growth. These practices should be discontinued to avoid the risk of weakening tax compliance. The authorities have instituted a two-part cut in income tax rates, a first stage in 2003 for lower incomes and a second stage for mid to upper incomes,

accompanied by simplifications, in 2005. *On condition that the recent tax cut can be financed through permanent structural measures on the spending side, it is a welcome development. Moreover, it should be carefully designed so as to avoid excessive rises in marginal rates at low to medium income levels via tax allowance withdrawals. Tax amnesties should be definitively phased out and be replaced by more vigorous programmes to fight tax evasion across the economy.*

### Italy's supply-side performance has weakened

Italy's per capita income is about average for the EU and a little higher than the OECD average. Its relative ranking has slipped somewhat, essentially because its growth performance has weakened not only relative to its own past performance but also relative to that of almost all other OECD countries. More worrying, recorded total factor productivity growth seems to have been negative lately. One consequence has been that although wages have grown very little in real terms as perceived by employees, (i.e. relative to the consumer price index), unit labour costs have risen quite significantly for their employers. For several years now, Italy has thus been losing price competitiveness within the euro-area, and recently even more sharply against non-euro-area countries as the euro has strengthened. Export volumes have fallen, and market shares in real terms have been eroded. Italian producers face heightened competition from eastern European and Asian countries on both the export and domestic markets. This process appears to be continuing: inflation in Italy is higher than the euro-area average, the output gap is closing, and although productivity performance is projected to pick up with the cyclical recovery, there are no early signs that it is going to do so rapidly. It is therefore important to understand the reasons for this poor productivity performance, and to find policies that will improve it.

### Poor productivity and competitiveness reflect structural problems

An alternative (but less than fully convincing) interpretation of recent employment, output, and trade statistics is that there are measurement problems. For example, employment growth may be overstated as informal labour “emerges” into the formal sector. However, a reason why this interpretation is less than fully convincing is that national accounts data already include estimates of the informal economy, which therefore cannot represent a significant source of bias in the productivity statistics. Employment costs may be overstated as tax credits for contract conversion are registered as higher profits rather than lower labour costs and growing use of flexible labour contracts reduce non-wage rather than wage labour costs, while output may be understated because of quality improvements. Cyclical labour hoarding may have also played a role in the deceleration of productivity. However, persisting relatively high core inflation and relatively large current account deterioration suggest that there is a structural – rather than just a measurement or a cyclical – problem with productivity and competitiveness in Italy. *It would therefore be wise to base policy decisions in such an important area on the awareness that those structural problems are at the origin of the slowdown in economic performance. This is even more the case when the appropriate policy actions are ones that are desirable in themselves.*



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### *Productivity in the non-tradeables sector needs to be boosted*

---

OECD measures of competition and performance in product markets show that although Italy has made undeniable progress in reducing administrative burdens and strengthening competition, its recorded progress is not better on average than in other countries, and it therefore remains a relatively poor performer. *The service sector in particular lacks competitive pressure to resist cost increases and to innovate, in part because of remaining direct public-sector involvement in some sub-sectors, especially transport and energy. Pervasive price controls in freight transport are hard to justify, and political influence on road infrastructure is damaging and inefficient. Professional services mostly fall outside antitrust jurisdiction, and opening up of retail trade to supermarket chains is resisted by local authorities, often captured by local business interests. The retail sector issue needs to be discussed and resolved at the national level.* A consequence of protected high cost services is that input costs for the traded sector are higher than they need to be, and rise faster than in major trading partners. Although benefiting from a boost of recent reforms, there is a specific problem with the electricity sector, which remains dominated by the incumbent, while new generating capacity additions are hampered by local opposition and administrative barriers, as are interconnections with foreign producers. This and other structural factors result in electricity prices that are significantly higher than in surrounding EU countries, and overall generating capacity constraints could prove a bottleneck to growth in the near future. *Recently decided separation of the generation and transmission network as well as ways of augmenting generation capacity in response to market signals should not be delayed. This is an issue that, like retail trade, requires concerted action on a national scale. Consideration should also be given to fully privatising the electricity and gas transmission networks, subject to safeguards for third party access.*

---

### *Corporate governance needs further improvement*

---

As noted in previous Surveys, the Italian corporate sector is characterised by a large number of small firms, often family-controlled, and a small number of very large firms, also often family-controlled even when publicly quoted. A recent series of bond defaults, including those of the Argentinian government, Cirio and Parmalat highlights the need for improvement in the system of corporate governance and oversight provided by the market. These episodes might have contributed to falling consumer confidence in the past few years, and underline the need to strengthen protection of minority shareholders as stressed by the OECD Principles of Corporate Governance, to establish more effective supervision of the market, and to update a bankruptcy legislation which does not ensure to either protect creditors or allow companies' owners to start a new business. Re-establishing confidence in the financial system will enhance the development of a private funded pension pillar with the diversion of worker severance fund flows into privately managed plans. This in turn would have further beneficial effects on domestic capital market development. A poorly performing financial sector represents a brake to an efficient allocation of capital with negative consequences on the growth of profitable firms, on R&D and innovation, and finally, on aggregate performance.

---

### *The first policy response has been prompt*

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The first policy response to serious corporate mismanagement was prompt, with a justifiable trade-off between the need to act swiftly to restore confidence and conserve assets, and the goal of creating optimal policies to deal with such situations, but a number of desirable measures have yet to be implemented. Originally, a bipartisan bill was submitted to the parliament in May 2004, concerning corporate governance and financial supervision. Some of the proposed measures progressively lost support and the bill was not approved. A new version of the bill under discussion in parliament still aims to strengthen minority shareholders' rights and improve the financial supervisory structure. *Approval of these measures should remain a priority in order to enhance confidence in the Italian financial market.* Bankruptcy law should also ideally encourage the maintenance of still-productive assets in order to help pay off creditors, and the reallocation or dissolution of unproductive assets. The new emergency bankruptcy procedures for large companies protect corporate assets more effectively than before, by speeding up the process. Under these procedures, a commission, appointed by the Ministry, supervises the restructuring exercise, while complying with normal judicial and market regulations. *Nevertheless, comprehensive bankruptcy reform remains an urgent matter.*

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### *Employment creation has been remarkable*

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Statistically, the reason why per capita incomes have continued to rise a little in the past few years, despite apparently falling total factor productivity, is that employment creation has been vigorous. Indeed, more jobs were created in the recession years 2001-2004 than in the preceding 4 years of brisker GDP growth. The unemployment rate fell in each year of the recession, and is now below the estimated NAIRU. The labour market reforms of earlier years and more recently led to the increase in employment, although employment data may have been somewhat boosted by flows of previously under-recorded informal labour, especially newly regularised immigrant labour, into the formal force. The reforms have made it easier and cheaper to adjust enterprise labour forces *via* temporary contracts, and tax incentives have facilitated their conversion to permanent contracts. Thus employers have been more willing to take on low-skilled or inexperienced employees on flexible contracts, which have allowed them to gain work experience and build up skills, without them necessarily remaining indefinitely in a state of precariousness. The large increase in employment, particularly of the low-skilled, goes some way to explaining the weak growth of productivity. But the example of other countries, for example the United States before 2001, and especially Ireland, shows that it is possible to have strong growth in both employment and in total factor productivity for a prolonged period. *Competitive product markets seem to be needed as well as flexible labour markets.*

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### *Nevertheless, the labour market remains segmented along regional lines while absorbing many immigrants*

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Unemployment rates in the more prosperous Northern and Central regions are under 5%. The southern regions continue to register rates at least three times higher, and the gap has diminished only marginally since 1998. The chronic problem of low mobility of

unemployed southern Italians towards the other regions perhaps influenced by the growing importance of equalisation transfers, is in contrast to the comparative success of immigrants in integrating themselves into the economy. Typically, immigrants, and especially illegal immigrants, arrive in the south of the country and head north to where the jobs are. Successive regularisation programmes have resulted in very large numbers of illegal immigrants joining the formal sector, thus widening the tax base and enhancing social security revenue.

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*Immigration policies should be more realistic and consistent*

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However, Italy's immigration policy is not well adapted to large scale inflows, perhaps a legacy from its past history of being an essentially emigration country. Official quotas for non-seasonal workers are relatively low and in practice linked to backward-looking labour-market assessments. *Given that Italy's immigrants appear to come looking for work, and finding it, a larger official quota for immigrants not tied to specific job offers might be appropriate. This will entail efforts in training and integration within the Italian labour market.* Illegal immigrants could then be dealt with more firmly.

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*Participation rates remain low*

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Although employment has risen substantially since the late 1990s, and unemployment rates have fallen, overall employment rates in Italy remain low, as do participation rates. The overall participation rate for those of working age is 63%, compared with an EU average of close to 70% (and a US figure of 75%). As in most countries, participation rates for prime-age males are well above 90%, but the figure drops to barely over 30% in Italy for males over 60 years old. Female participation rates are low by international comparison at all ages. Less than 50% of women are in the labour force compared with an EU average of 60%. And as in other southern European countries, part-time employment of women accounts for a relatively low proportion of their total employment. Participation rates of women and older males are lower than the EU average even in the prosperous Italian regions that experience chronic labour shortages. There is therefore considerable room for expanding output for some time to come by raising participation and employment rates of women and older males, including in the northern and central regions, towards international levels.

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*Policy efforts should focus on older workers and women of all ages*

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The pension reforms should help raise participation among the older workers in future years, though it is important that higher participation is accompanied by higher employment. *Adequate training for workers before they reach the vulnerable age will be important, and the public employment service should strengthen efforts to find jobs for the unemployed in this age group. The actual impact of the reforms on participation of older workers should be monitored.* As in other Mediterranean countries, there is a traditional culture of women staying at home to look after their children, and to care for their ageing parents. *Concerns about the low rates of female participation can be addressed by greater public investment in child-care facilities and care support for the elderly in order to help women stay in paid work. The high tax wedge on*

*labour should be reduced, while the tax allowances for dependent spouses should be reformed in order to strengthen the financial incentives to work for second earners, especially those with low skills. Many immigrants are working as domestic help, potentially liberating their higher-skilled employers to join the labour force. Liberalisation of immigrant flows could help facilitate this process. Recent labour market reforms have increased the supply of part-time jobs, which may be particularly attractive to women. Liberalisation of opening hours in the retail sector, and encouraging the spread of large retail outlets, as well as reforms in other product market areas, would further expand job opportunities for women along similar lines.*

### Educational outcomes are unsatisfactory

Compared with other OECD countries, an above-average proportion of the Italian population has only lower-secondary education. This is especially true for older age-groups, but it is also true for younger ones. Forty per cent of 25-34 year-olds are in this category compared with an EU and OECD average close to 25%, and the results of the OECD Programme for International Student Assessment (PISA) show that Italian 15-year olds have attainments well below the average in particular in mathematical and problem-solving skills. There is a high proportion of youth which is in neither education nor the labour force, suggesting a difficult school-to-work transition. The risk of unemployment later in life is also considerably higher for those with only lower secondary education. The policy reaction to these features has been to raise the number of years of compulsory schooling from 10 to 12, and to reform the structure of primary and secondary education in major ways, including improving the school-to-work transition in the form of a vocational track, as detailed in the previous OECD Survey. *These reforms go very much in the right direction, and should be monitored to ensure that they are achieving their goals. Job-related training should be the next priority.*

### Quality of the tertiary sector needs improvement

Furthermore, a smaller proportion than the OECD average has completed tertiary education, even though a relatively high proportion embarks on it. Years spent in obtaining an undergraduate degree are greater than the average, raising the opportunity cost of tertiary education and discouraging the formation of high level skills. The demand for high-skill workers may be hampered by the specialisation of Italian industries in low tech sectors and the small size of Italian firms, which reduce their R&D spending capability. At the tertiary level, a problem is an insufficient number of younger professors, for whom there are barriers to entry. Academic appointments lack transparency, promotion is not always linked to productivity, and Italy spends far less than the OECD or EU average on research and development, and significantly less on tertiary education. As a consequence Italy suffers from a pronounced net brain-drain. At the same time, administrative barriers to the recognition of foreign degrees and other professional qualifications mean that Italy misses out on the diffusion of high-level technical skills, experience and knowledge from abroad. *These shortcomings should be addressed with urgency. Policies here should concentrate on increasing the size of the teaching body, and making it easier for qualified persons, including foreigners, to occupy posts on merit and, eventually, with greater security of employment than is currently the case.*