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The origins of the public debt of Italy: Geographically dispersed interests?☆

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Abstract

In this paper we reconstruct the macro regional government deficits of Italy and find that the aggregate deficit resulting from our estimates captures quite well the entire dynamics of the Italian national public deficit. This new data set shows that the ultimate cause of the accumulation of public debt of Italy lies in the extraordinary fiscal imbalance of the Southern regions. The new data allow us to test empirically a simple Common Pool model, augmented by a variable measuring the political influence of each macro region in the Government, to verify the existence of a geographically dispersed interests issue for the Italian case. Our measure of political influence turns out to significantly explain the regions' deficits also when controlling for population and income gaps. In addition, using a *J*-test approach, we find that including the predictions of the Common Pool–Pork Barrel regional model into a general model of the Italian national deficit turns out to greatly increase its explanatory power. The results call for deep institutional reforms of the fiscal decentralization so far implemented in Italy.

Keywords: Italian public deficit; Italian public debt; Common Pool; Pork Barrel; Geographically dispersed interests

JEL classification: E62; R50; C22; C12

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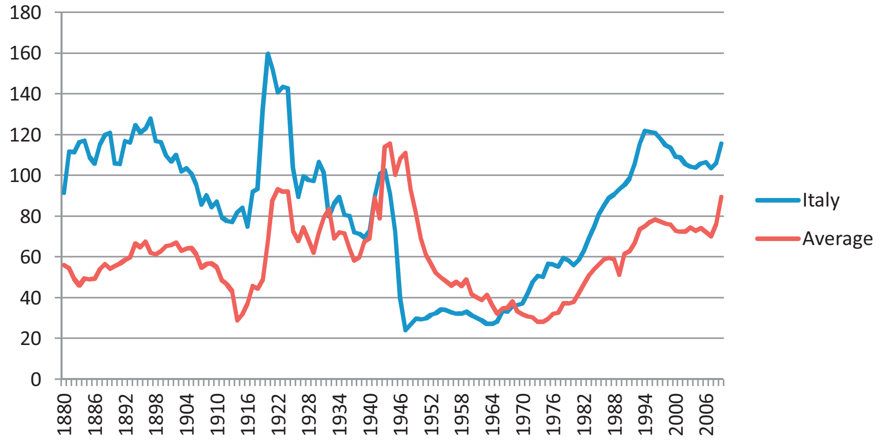

Fig. 1. Public debt Ratio over *GDP* (in color). Average of Belgium, France, Germany, Greece, Ireland, Japan, Spain, Sweden, UK, USA vs. Italy. *Source*: IMF. (For interpretation of the references to color in this figure legend, the reader is referred to the web version of the article.)

> "È la somma che fa il totale"
> "*It is the sum that makes the total*"
> Antonio de Curtis, comedian

1. Introduction and relation to the literature

Italy displays the third largest sovereign debt of the world and the eighth when it is *GDP* weighted. This large stock is not the result of some sudden large banks' bailout but it has been cumulated in a very long period of discrete deficits. This makes the Italian case an important case study when discussing the origins and causes of persistent deficits and the consequent large public debts.

Apparently, Italy's debt shares its dynamics with those of several other developed countries, although the Italian case appears somewhat amplified (see Fig. 1). In what follows we will put some evidence against this alleged similarity.

The positive trend in the accumulation of public debt of many developed countries, typically from the seventies onward, questioned the traditional normative theories of public debt or deficits, either of Keynesian or Neoclassical stream, and opened up the field to the positive theories of public debt. In an important survey, Alesina and Perotti (1994) singled out several theories potentially able to account for this behavior, and discussed their pros and cons.[2]

The last set of theories considered by Alesina and Perotti (1994) are models of geographically dispersed interests. These models have not been empirically adapted and tested to the Italian case yet. In this paper we fill the gap in order to shed light on the ultimate cause of the accumulation of public debt of Italy. In general, models of geographically dispersed interests imply that, as in many Common Pool problems, whenever the decision-making is in the hands of representatives of

[2] The theories Alesina and Perotti (1994) review are: theories of political business cycle, models of intergenerational conflicts, theories of the strategic role of public debt, government fragmentation, theories of budgetary institutions and finally theories of geographically dispersed interests.