Recovery Capacity of the Finance System of Italian Municipalities After the Currency Crisis of 1992

Salvatore Villani

University of Naples Federico II, Naples, Italy

This paper is a first pioneering attempt to apply the concept of resilience to the analysis of the public finance systems of local governments, a concept already used and “abused” in various disciplines and fields of science. In particular, it proposes an attempt to estimate the recovery capacity of Italian Municipalities in a crucial period of our country’s financial history, between 1992 and 2000, or between the currency crisis and the introduction of the Euro. However, the analysis also involved the subsequent trends, in order to demonstrate that the current vulnerability of the municipal public finance system, in particular of the Municipalities of Southern Italy, depends not only on the economic cycle but also on the continuous and incessant changes in the financing mechanisms of local governments established by the central government. The analysis showed a lower financial resilience of the Municipalities of the Mezzogiorno (island and continental) compared to those of the Center-North. The determinants of this phenomenon were found, for one part, through the analysis of the financial data of the Italian Municipalities – as presented by the SVIMEZ in its annual reports on the economy of the Mezzogiorno – and, for another part, through the critical synthesis of significant economic events which occurred during the period examined.

Keywords: governmental financial resilience, financial management, vulnerability and recovery capacity of local governments, financial shocks, currency crisis

Introduction

This paper represents a first innovative attempt to apply the concept of resilience to the analysis of local government (LG) finance systems, a notion already used and “abused” in several disciplines and fields of knowledge. Since ancient times, the concept of resilience has always charmed human mind, up to become a metaphor or a sort of *boundary object*, namely an “object” that cannot be precisely defined in only one dimension, rather it is on the borderline connecting and dividing several fields. As such, it is useful in promoting different routes of detailed study and research (Brand & Jax, 2007)¹.

Salvatore Villani, Assistant Professor of Public Economics, Department of Political Sciences, University of Naples Federico II.
Email: salvatore.villani@unina.it.

¹ Among several concepts of resilience developed in several fields of the knowledge, the one considered the most appropriate and suitable to the inquiry carried out in this paper is “the ability for a system to recover suitable operating conditions after an external shock”. In all scientific fields, a shared definition of this notion does not exist. The one herewith applied was proposed in the seventies (Holling, 1973) and used in the study of ecological and socio-ecological systems. This notion is generally defined as “ecologic resilience” and involves ability of absorbing effects produced by a sudden and unfavorable event caused by external forces or factors (external shock), on one hand, and ability of preserving or recovering functions, structure, identity and original mechanisms of self-regulation (*feedback*), on the other hand. For more insights on the main definitions and interpretations of the resilience notion, see also Martin and Sunley (2014), Martin (2012), Duval and Vogel (2008), and Walker, Holling, Carpenter, and Kinzig (2004).

In particular, we aim to estimate the recovery capacity of Italian Municipalities in a critical period of the financial history of the Country, the one between 1992 and 2000, that is, the one included between the currency crisis and the introduction of Euro. However, further trends are also taken into consideration, in order to show how the actual vulnerability of the public municipal finance system, and particularly that of South Municipalities, not only depends on the economic cycle, but also on the continual and constant variations of financing mechanisms of local Bodies established by the central Government.

The examined issue belongs, therefore, to the financial history of Italy and of the European Union (EU), but it also presents some points of considerable interest and modernity which undoubtedly deserve a minimum of detailed study. In fact, as we know, finance of Municipalities is a mechanism through which a certain range of services is provided to the community of citizens. Their level can differ according to the reference community's preferences, with the same set of resources too, or on the basis of a different structure of costs, or pursuant to a different fiscal pressure. The importance of these "differences" and their social acceptance will obviously depend on fiscal choices by the central Government too and by the funds transfer system by means of which the effects of these choices have been equalized.

An evaluation referred to the set of the above mentioned variables (available resources, costs, fiscal pressure) and to their reaction to fluctuations of the economic cycle and to continual modifications of the local territorial Bodies' financing regime is inherently debatable, even if the result is clearly univocal at ordinal level. The current Italian system of local Autonomies contributed, and still contributes, in determining an undeniable deviation in the level of services provided to citizens in all areas of the territory, in job perspectives they have and in their financial treatment. The vulnerability of the whole Italian productive structure and of its system of public finance depends mostly on this phenomenon.

The following section proposes critical comments on the period under consideration and a brief review of economic events that are significant for the study conducted in this paper. The remarks included in this section are supported by the data and the insights contained in the SVIMEZ studies concerning the period examined. Section 3 lists the variables taken into consideration and describes their dynamics in the considered period. Section 4 illustrates and comments findings of the analysis. Finally, Section 5 presents consequent conclusive evaluations.

Resilience Analysis of the Economic Events Occurred During the Period Under Consideration

In this paper, we have tried to apply the concept of resilience to events of the Italian Municipal finance occurred around 1992. Per capita amount of fiscal grants to Municipalities reduced because of a normative provision at that time decided. Reduction, on national level and on cash accounting, is of 48.7% in 1992, compared to the previous year: for South Italy cut was of 53.6%; for North-West Italy it was of 46.0%; for East-North Italy it was of 48.8%; for Centre Italy it was of 34.1%. Compared to current expenditure of Municipalities of Southern Italy, cut counted 32.9%; in North-West Italy, 14.3%; in North-East Italy, 12.6%; in Centre Italy, 10.3% (cf. SVIMEZ, 1995, pp. 11-14). Over these years, SVIMEZ² has stated that Italy entered Europe also as a consequence of these financial measures, but it should be still necessary to establish who paid the "price of the ticket".

² Italian non-profit research institute which studies and promotes public policies for economic development in the Mezzogiorno (Southern Italy).

Currency Crisis of 1992 and Its Effects on the Mezzogiorno's Economy

The EMS (the European Monetary System, which linked currencies participating in a predetermined exchange rate) demonstrated the weakness of its construction with the events of 1992, when the system of fixed but adjustable exchange rates was hit hard by speculation. Speculators' attacks became more frequent and relevant. Moreover, investors took advantage of the progress made in integration to diversify their portfolios internationally. Most central banks - including those in France, Italy and the United Kingdom - had to intervene very often on the markets to prevent the devaluation of national currencies against the Deutsche Mark. Following the intensification of speculative attacks, the Bank of Italy declared the abandonment of the EMS by the lira on September 21, 1992. Lira and pound had to get out of the EMS and the yield of government bonds leaped upward.

In this paper, the 1992 event has to be evaluated with reference to the overall trend of the Italian economy over years, starting from 1991. We will discuss this in the next subparagraphs on the basis of the SVIMEZ reports on the economy of Southern Italy published for several years, for the reason that proposed considerations are still valid today in relation to the current situation.

As we know, the 1992 currency crisis was faced by a strong devaluation of Lira. As a result of this too, reduction of per capita GDP from 1992 to 1993 was limited (see Figure 1): at national level, it accounted for 0.95%; for South Italy, 1.72%; for Centre-North Italy, 0.65%. Effects of 2009 crisis were even more serious: from 2007 to 2009, at national level, in per capita Euros and at steady level, GDP reduced by 7.71% (specifically, for the South, -6.94 % and, for Centre-North, -8.14%).

Figure 1. Per capita GDP in Years of 1991-2014 (absolute values expressed in Euro 2014).

Source: Calculations of the author based on SVIMEZ and ISTAT data.

Table 1

Per Capita GDP in Years of 1991-2014 (Percentage Changes)

Years	Centre-North	Mezzogiorno	Italy	Mezzogiorno in % of the Center-North
1991-2014	7.6	-0.2	6.7	-7.3
1997-2014	-1.8	-3.2	-1.2	-1.4
2001-2014	-9.3	-11.8	-9.1	-2.8
2007-2014	-12.0	-13.7	-12.0	-1.9

Note. Source: Calculations of the author based on SVIMEZ and ISTAT data.

For the overall period to which Table 1 refers, the steady factor is the South's falling back compared to the rest of Italy. From 1991 to 2014, the GDP of Centre-North increased by 7.6%, while the South's one reduced by 0.2%. As a result of this, as Table 1 still shows, the relation between South's GDP and Centre-North's one (which was 60.8% in 1991), arrived up to 56.3% in 2014: the gap so significantly reduced in these years.

Analysis of the economic events proposed in *1995 SVIMEZ Report on the Economy of Southern Italy* is very effective for the considered years.

First of all, in the SVIMEZ Report's Introduction, the authors observe that in 1994 the Italian economy survived a downturn phase. While in 1993, recovery of the foreign demand had been considerable, but in any case not enough to compensate for the internal one, in 1994 the latter too resulted in an albeit soft recovery and added its impulse to the one of exports, by the way becoming more intense. In the Report, it was highlighted how this soft recovery of the internal demand occurred, since devaluation of lira of September 1992 had not luckily produced "besides the immediate advantage of an increase in the international competitiveness of our productions, also an increase of internal prices which would have ended up in cancelling that advantage". However, it was observed how nevertheless in that period (five-year period of 1991-1994) "certainty of perspectives" was missed, albeit this was necessary to ensure "stronger and more long-lasting basis to the recovery than the ones established by Lira's depreciation". As political contrasts between the end of 1994 and first months of 1995 got worse, uncertainty was in fact increased and so did economic operators' mistrust. This phenomenon caused a capital outflow which pushed Lira's international quotation far below the level which should have been justified by the trend of real economy. The increase of raw materials' US dollars' price and of some indirect taxes arranged by the corrective finance action established in February 1995 was added to the effects of devaluation (cf. SVIMEZ, 1995, pp. 11-12)³.

Moreover, in 1995 SVIMEZ Report, it was observed that a "steady development of the Italian economy" represented, and still represents, necessary requirement to obtain a reduction of the internal territorial differences.

In this respect, in 1995 Report's Introduction, it was highlighted how the subsequent economic recovery in the Centre-North areas had been more rapid and stronger, as it had been driven by exports, and this had even fostered a recovery of manpower's emigration from the South. After all, SVIMEZ has always pointed out that emigration and industrialization have always been, for our Country, "not alternative, but complementary solutions for the issue of unemployment in the South" (cf. SVIMEZ, 1995, p. 14).

³ For a more accurate reconstruction of economic events related to the currency crisis and quasi-financial in September 1992, see also Viesti (1996), Visco (1999), and Rossi (2007; 2011).

Mezzogiorno and the Challenges of the European Integration Process

In the following years, the accession process firstly to EMS and second to the common currency was successful, despite the sudden slowdown in the GDP's growth of 1996. According to SVIMEZ, in the scenario so created by monetary unification, acceleration of development had to be pursued as part of an "irreversible" process of international economic integration. In fact, improvement of this process would have allowed companies to cancel risks and (direct and indirect) costs connected to the currency exchange, together with a higher chance to enjoy scale economies in the big unified European market; and consumers to take advantage of lower prices determined by lower costs of production and by higher continental competition. However, ever since then it was pointed out that advantages deriving from membership of the EU would have been higher the more monetary unification was accompanied by political and economic political unification too. In fact, the latter should have to be defined, as SVIMEZ observed, "with everybody's help and not imposed as a matter of fact by the most populous and richest country with the strongest currency, whose right concerns on economic-financial stability have so far clearly prevailed on not less right concerns for development and job creation" (cf. SVIMEZ, 1997, p. 15).

From this perspective, participation in the monetary unification had to be considered as a necessity then, and not only as an advantage: the inability in realizing and keeping conditions for economic-financial adjustment programme and for economic-financial stability, which were provided to enter in the unified European market, should have caused mistrust in markets, expectations of the exchange's devaluation, sudden rise of interest rates; recovery of stability conditions and participation to the great advantages the single currency offered in the long term would have been resulted more difficult and painful than it already was in terms of tax burdens, brake on the development and unemployment.

On the contrary, monetary unification offered "the chance of a significant and regular development for the European economy as a whole". According to SVIMEZ, this chance had to be understood, at least to the same extent, by all regional economies, because without a politics able to increase locating interests in weak regions these could have been damaged by the common currency in competing with other regions to draw investments instead of being encouraged. In this case, and for these reasons, the already difficult situation of Southern Italy would have become more and more difficult and critical in the future (SVIMEZ, 1997, pp. 15-16).

The Wasted Chance of Economic and Civil Development

In the following years, the Italian finance system strengthened although within growth differentials which are systematically negative for the overall period of 1995-2000, compared to the average one of the European monetary union (cf. SVIMEZ, 2002, p. 63). In total, (see still Table 1), from 1995 to 2000, the per capita GDP in Euro increased, at constant prices, by 10.2% (respectively, for the Centre-north +9.8% and for the South +11.0%).

During these years, Italy lived a big chance of economic and civil development like the other European countries. Further events showed that this chance was wasted.

In this respect, SVIMEZ had been forward-looking. In fact, in its 1998 Report, it pointed out that Italy, with entry in the monetary union, was obliged to persevere in order to reduce the huge weight of public debt and far from finishing the economic-financial adjustment effort. Therefore, the monetary union had not to be considered as the final goal, as perhaps "it might have looked to Italians when they had supported hard sacrifices for it, but only a middle goal to reach that stability which could be made strong and safe only by reducing the debt" (SVIMEZ, 1998, p. 10).

With the same long term outlook, SVIMEZ clarified that national governments are responsible for economic and social politics, while stability is a duty to be respected for them. However, “to the extent permitted by respect of this duty, objectives of economic and social politics cannot but be the economic development and social equity. Therefore, the axe of financial rigidity, imposed by stability’s duty, must not continue affecting investments; and social and territorial distribution of sacrifices, necessarily involved by politics for stability, must not be influenced by group interests, by categories, by generations, by the strongest territorial areas which are better represented and defended in political and union terms” (SVIMEZ, 1998, pp. 10-11).

Variables Considered in the Resilience Analysis

Current Revenues

According to this research, the events from 1997 to 2000 are of great importance. These events had significant effects on the financial treatment suffered by communities of citizens and, consequently, on the financial resilience of their LGs. This results from two variables: services level and fiscal pressure. Starting from the financial data, as presented by SVIMEZ, in the *Reports on the Economy of Southern Italy* of several years, investigation related to the first variable is indirect. We know the expenditure; knowing the amount of this latter, we can infer the level of efficiency, following the Wildavsky rule, according to which efficiency is itself the effect of investments in services and proceedings. All that means that ascertaining of lower per capita resources which are available to LGs in a territory, compared with those of others, underestimates gaps among levels of services enjoyed in both territories by citizens. This produces a situation which is very dangerous for Southern Italy, where citizens pay more but get less. The principle “to pay more to get less” is regularly applied in this part of the country.

Therefore, the first variable is the one represented by per capita current revenues; by the way, these revenues represent the basis and the significant parameter in relation to investment expenditure, too.

In the period from 1993 to 2000, the trend of current revenues was marked by the financial adjustment programmes aimed at reducing public grants to LGs. In the years from 1993 to 1995, two mechanisms overlap: on the one hand, there is the Delegation Act No. 421/1992 and its implementing rules, given by the Legislative Decree No. 504/1992; on the other hand, there is the mechanism of “cuts” established by the Law Decree No. 155/1993. In this regard, the applied rule is the one of the invariance of financial resources (cf. the Art. 54 c.11 of Law 142/1990), which are made up - as a consequence of 1992 reform - by Local council property tax at 4 per thousand (indicating the “fiscal capacity” of LGs, according to terminology of Art. 119, Par. 3, of the Italian Constitution) and by transfers of State revenue.

On this basis, “cuts” mechanism works. In 1994, for example, these were established by Art. 3, Par. 2, of the Law Decree No. 155/1993 (SVIMEZ, 1995): this norm redetermines the amount of “ordinary financial endowments, which were recognized in 1993 for Provincial Governments and for Municipalities”, to which a reduction of 7% was applied. This cut follows another one referred to 1993 and still gives advance notice of another one for 1995. It is considered, in “relative terms”, as much serious as higher is the amount represented by the amount of State revenue transfers of 1993 on the overall of current revenues. The percentages concerned for the six considered areas are the following: North-West Italy, 44.9%; North-East Italy, 39.3%; Central Italy, 50.7%; Mainland Mezzogiorno, 67.8%; Island Mezzogiorno, 51.1%; total Italy, 49.9%.

In 1997, as we had already observed (compare Section 2), on a well defined situation already explained, occurs the cut of revenue transfers by cash operations. In the next year, system was closed by the introduction, starting from 1999, of the *Internal Agreement of Stability (Patto di Stabilità Interno)*.

Table 2, which we here introduce like a first indication referred to the resilience parameters discussed in Section 4, shows percentage variations of current revenues compared to the basic year (1993) over years up to 2000. The Mainland Mezzogiorno is seriously subject to 1997 cut, while it shows a good resistance in 1994. Starting from 1998, recovery is very effective, up to reach in 1999 the assessed entry level on the basic year.

Table 2

Per Capita Current Revenues (a) of Italian Municipalities Belonging to the Regions with Ordinary Statute in Years of 1993-2000 (Absolute Values Expressed in Euro 2001; Index Numbers: 1993 = 100)

Circumscriptions	1993	1994	1995	1996	1997	1998	1999	2000
Central	989	894	925	823	826	840	852	849
1993 = 100	100.0	90.4	93.5	83.2	83.5	84.9	86.1	85.8
Southern	609	618	665	594	422	501	606	603
1993 = 100	100.0	101.5	109.2	97.5	69.3	82.3	99.5	99.0
Island	701	656	785	673	500	694	707	723
1993 = 100	100.0	93.6	112.0	96.0	71.3	99.0	100.9	103.1
North-West	911	833	922	797	729	745	846	928
1993 = 100	100.0	91.4	101.2	87.5	80.0	81.8	92.9	101.9
North-East	907	867	939	854	795	866	906	966
1993 = 100	100.0	95.6	103.5	94.2	87.7	95.5	99.9	106.5
Italy	826	777	846	748	657	720	783	817
1993 = 100	100.0	94.1	102.4	90.6	79.5	87.2	94.8	98.9

Notes. (a) Per capita value calculated on the resident population at the end of the year. Source: Calculations of the author based on SVIMEZ data.

Tax Revenues

In the considered period, introduction of ICI (*Imposta Comunale sugli Immobili*, the Municipal Property Tax) – gradually occurred in the years 1993-1994 – is decisive. As a result of it, at national level, variation of tax revenues between the two years (see Table 3) is 40% on one hand; on the other hand, the occurred variation in the Mezzogiorno reaches 46.2%. In this way, it is confirmed that cuts induce Southern Municipalities in increasing tax to a greater extent, whenever Centre-Northern Municipalities reduce expenditure.

Table 3

Per Capita Tax Revenues (a) of Italian Municipalities Belonging to the Regions with Ordinary Statute in Years of 1993-2000 (Absolute Values Expressed in Euro 2001; Index Numbers: 1993 = 100)

Circumscriptions	1993	1994	1995	1996	1997	1998	1999	2000
Central	250	356	390	360	351	345	362	333
1993 = 100	100.0	142.4	156.0	144.0	140.4	138.0	144.8	133.2
Southern	117	171	214	183	181	173	185	186
1993 = 100	100.0	146.2	182.9	156.4	154.7	147.9	158.1	159.0
Island	102	130	181	168	152	166	157	159
1993 = 100	100.0	127.5	177.5	164.7	149.0	162.7	153.9	155.9
North-West	230	315	384	331	344	344	377	328
1993 = 100	100.0	137.0	167.0	143.9	149.6	149.6	163.9	142.6
North-East	210	300	341	307	325	338	366	323
1993 = 100	100.0	142.9	162.4	146.2	154.8	161.0	174.3	153.8
Italy	188	263	312	277	279	280	299	274
1993 = 100	100.0	139.9	166.0	147.3	148.4	148.9	159.0	145.7

Notes. (a) Per capita value calculated on the resident population at the end of the year. Source: Calculations of the author based on SVIMEZ data.

The evolution of tax burden in the considered years is also worthy to be noted (cf. Table 4). In this case, the detected trends are even more noticeable because of all different GDP's variations resulting for Italy's circumscriptions.

Table 4

Tax Burden of Italian Municipalities Belonging to the Regions with Ordinary Statute in Years of 1993-2000 (Absolute Values Expressed in Euro 2001; Index Numbers: 1995 = 100)

Circumscriptions	1995	1996	1997	1998	1999	2000
Central	1.22	1.16	1.13	1.11	1.16	1.07
1995 = 100	100.0	95.1	92.5	90.8	95.3	87.2
Southern	1.13	1.00	0.98	0.94	0.99	0.99
1995 = 100	100.0	88.3	86.9	83.0	87.6	87.3
Island	0.94	0.90	0.82	0.89	0.86	0.86
1995 = 100	100.0	95.4	86.6	94.8	90.9	91.0
North-West	1.08	0.96	0.99	1.00	1.10	0.95
1995 = 100	100.0	88.3	91.9	92.4	101.9	87.9
North-East	1.00	0.92	0.98	1.02	1.11	0.96
1995 = 100	100.0	91.8	97.5	101.9	110.5	95.5
Italy	1.09	1.00	1.00	1.01	1.08	0.98
1995 = 100	100.0	91.1	91.7	92.2	98.5	89.3

Note. Source: Calculations of the author based on SVIMEZ data.

Current Expenditures

Table 5 clearly shows the situation of gaps among territorial circumscriptions. In 1993, the amount of current expenditure referring to the South of Italy is 66% compared to North-West Italy; in 2000, the corresponding value is 74.5%. Compared to the national average value, the amounts resulting for South municipalities correspond respectively to 71.9% in 1993 and 77.5% in 2000. Therefore, a higher fiscal effort supported by Southern Italy people produces a reduction of expenditure gaps, in a background where the amount of resources generally proves to be completely the same between the two years at national level. Despite the decrease of revenues, in years referred in Section 2 and as a result of the very significant fiscal effort imposed by municipalities' governments to citizens, a comparatively strong increase is observed in the Mezzogiorno (both continental and island) of current expenditures compared to other territorial circumscriptions (see Table 5).

We have carried out two detailed analyses. Since our analysis of resilience has as its object variations cyclical, we have considered it appropriate to exclude expenditure components whose variability is smaller, that is expenditures about staff and for interests. In Table 6, the difference between current expenditures and staff expenditures is directly shown.

Staff expenditures represent a variable whose congiuntural variations are limited on Municipalities' finance, also as a result of recurrent prohibitions of hirings and block of accessory benefits. On the contrary, other current expenditures change, and in accentuated manner (cf. Table 6). In 1993, at the beginning of the story, these expenditures were 75.7% in the Mezzogiorno, compared to the national data; at the end, the percentage was 83.5%. It's like somebody has chased a physiological level of expenditure (for public services) during these years, but it is paid by citizens with very significant increases of fiscal pressure (see Table 4).

Table 5

Per Capita Current Expenditures of Italian Municipalities Belonging to the Regions with Ordinary Statute in Years of 1993-2000 (Absolute Values Expressed in Euro 2001; Index Numbers: 1993 = 100)

Circumscriptions	1993	1994	1995	1996	1997	1998	1999	2000
Central	910	807	858	860	803	771	861	852
1993 = 100	100.0	88.7	94.3	94.5	88.2	84.7	94.6	93.6
Southern	517	546	562	529	555	538	568	558
1993 = 100	100.0	105.6	108.7	102.3	107.4	104.1	109.9	107.9
Island	611	620	667	645	644	726	651	678
1993 = 100	100.0	101.5	109.2	105.6	105.4	118.8	106.5	111.0
North-West	783	775	812	729	750	724	755	749
1993 = 100	100.0	99.0	103.7	93.1	95.8	92.5	96.4	95.7
North-East	768	773	828	765	802	786	783	782
1993 = 100	100.0	100.7	107.8	99.6	104.4	102.3	102.0	101.8
Italy	719	706	745	701	709	698	722	720
1993 = 100	100.0	98.2	103.6	97.5	98.6	97.1	100.4	100.1

Note. Source: Calculations of the author based on SVIMEZ data.

Table 6

Per Capita Current Expenditures, Net of Personnel Expenditures, of Italian Municipalities Belonging to the Regions with Ordinary Statute in Years of 1993-2000 (Absolute Values Expressed in Euro 2001; Index Numbers: 1993 = 100)

Circumscriptions	1993	1994	1995	1996	1997	1998	1999	2000
Central	586	541	582	604	556	536	605	632
1993 = 100	100.0	92.3	99.3	103.1	94.9	91.5	103.2	107.8
Southern	345	359	389	380	386	426	369	419
1993 = 100	100.0	104.1	112.8	110.1	111.9	123.5	107.0	121.4
Island	701	656	785	673	500	694	707	723
1993 = 100	100.0	93.6	112.0	96.0	71.3	99.0	100.9	103.1
North-West	544	545	575	511	516	496	525	532
1993 = 100	100.0	100.2	105.7	93.9	94.9	91.2	96.5	97.8
North-East	516	531	571	529	556	554	542	563
1993 = 100	100.0	102.9	110.7	102.5	107.8	107.4	105.0	109.1
Italy	456	459	490	466	469	466	482	502
1993 = 100	100.0	100.7	107.5	102.2	102.9	102.2	105.7	110.1

Note. Source: Calculations of the author based on SVIMEZ data.

Second detailed study regards the so-called “programmability index of balance sheets” (cf. Table 7).

Here too we use the criterion of isolating the “not programmable” expenditure part, in the short term at least, namely salaries where interests on loans and cash advances are added. In this way, we can identify part of the expenditure which directly finances services and whose variation more directly depends on the offer of them, albeit in a completely rough way and by difference.

From data represented in Table 7, two extremely significant phenomena, characterizing balance sheet management in Southern Italy, but above in all the Municipalities of the Italian Islands, are observed: we are talking about a lower programmability level and, at the same time, its sudden change in direction from its original development path in conjunction with Italy’s entry in the European currency Union and with the issuance of the first Bassanini Act (Law No. 59/1997). With this law, Parliament authorized Government in realizing the maximum possible decentralisation inside the allowed borders of the applicable Constitution.

Thus, we can believe that the before said phenomena clearly depend on choices of the international economic politics and of decentralisation implemented during those years (Pica & Villani, 2010). In fact, in this respect, we remember that in the same year there was the reorganisation of normative on local taxes (Legislative Decree 446/1997), as well as of the system of State grants to LGs (Legislative Decree 446/1997). Both phenomena equally contributed to making 1997 a unique year or, as SVIMEZ defined it, “a new break in the history of local finance” (SVIMEZ, 2001, p. 344).

Table 7

Index of Programmability of the Budgets (a) of Italian Municipalities Belonging to the Regions with Ordinary Statute in Years of 1993-2000 (Index Numbers: 1993 = 100)

Circumscriptions	1993	1994	1995	1996	1997	1998	1999	2000
Central	42.8	48.6	45.9	41.9	36.9	41.3	43.6	42.8
1993 = 100	100.0	113.6	107.2	97.9	86.2	96.5	101.9	100.0
Southern	43.3	44.5	49.1	48.0	18.6	39.5	49.8	53.0
1993 = 100	100.0	102.8	113.4	110.9	43.0	91.2	115.0	122.4
Island	33.3	33.7	38.6	36.5	-6.9	25.8	33.8	32.8
1993 = 100	100.0	101.2	115.9	109.6	-20.7	77.5	101.5	98.5
North-West	46.6	47.4	52.2	48.2	34.0	43.5	49.1	57.6
1993 = 100	100.0	101.7	112.0	103.4	73.0	93.3	105.4	123.6
North-East	42.6	41.8	44.0	41.9	30.2	38.4	43.0	50.3
1993 = 100	100.0	98.1	103.3	98.4	70.9	90.1	100.9	118.1
Italy	43.1	44.8	47.4	44.5	27.9	39.3	45.4	50.2
1993 = 100	100.0	103.9	110.0	103.2	64.7	91.2	105.3	116.5

Notes. (a) Calculated as a complement to 100% of the sum of personnel expenditures and interest on the amount of state grants and tax revenues. Source: Calculations of the author based on SVIMEZ data.

Capital Expenditure

The research hypothesis expressed in this paper is that the decisive variable measuring the ability of the system of Italian Municipalities (and above all the Mezzogiorno's ones) to resist to financial shocks, is represented by capital expenditure or, to better say, in that part of it which is directly consisting of investments.

Table 8

Per Capita Capital Expenditures of Italian Municipalities Belonging to the Regions with Ordinary Statute in Years of 1993-2000 (Absolute Values Expressed in Euro 2001; Index Numbers: 1993 = 100)

Circumscriptions	1993	1994	1995	1996	1997	1998	1999	2000
Central	258	204	223	218	230	240	284	281
1993 = 100	100.0	79.1	86.4	84.5	89.1	93.0	110.1	108.9
Southern	197	169	172	171	190	202	220	231
1993 = 100	100.0	85.8	87.3	86.8	96.4	102.5	111.7	117.3
Island	158	136	169	197	194	212	183	223
1993 = 100	100.0	86.1	107.0	124.7	122.8	134.2	115.8	141.1
North-West	308	277	434	482	445	451	461	561
1993 = 100	100.0	89.9	140.9	156.5	144.5	146.4	149.7	182.1
North-East	234	216	262	279	326	327	334	332
1993 = 100	100.0	92.3	112.0	119.2	139.3	139.7	142.7	141.9
Italy	240	208	266	284	290	299	312	345
1993 = 100	100.0	86.7	110.8	118.3	120.8	124.6	130.0	143.8

Note. Source: Calculations of the author based on SVIMEZ data.

Table 8 above shows capital expenditures' trend in the five territorial circumscriptions of Italy. In 1993, per capita value of expenditure in the Mezzogiorno was 82.1%, compared to national average level: in 2010, the corresponding value was 66.7%.

Trend of percentage variables shows a capacity of reaction to 1994 *shock* which was much smaller than the one experienced by other circumscriptions. There is, however, the exception represented by the case of Central Italy where, for this variable and for other ones, the lowest reaction to the financial *shock* seems a pre-ordered choice accompanying or even advancing choices of the National government.

For capital expenditure's case too, it is useful to separate one of their components which has specific and unique importance, that of direct investments (see Table 9). In 1993, they represented 87.3% compared to the national average value, the same value which was confirmed in 2000.

Table 9

Per Capita Direct Investments of Italian Municipalities Belonging to the Regions with Ordinary Statute in Years of 1993-2000 (Absolute Values Expressed in Euro 2001; Index Numbers: 1993 = 100)

Circumscriptions	1993	1994	1995	1996	1997	1998	1999	2000
Central	145	137	153	144	172	187	209	217
1993 = 100	100.0	94.5	105.5	99.3	118.6	129.0	144.1	149.7
Southern	138	138	141	131	164	172	193	192
1993 = 100	100.0	100.0	102.2	94.9	118.8	124.6	139.9	139.1
Island	133	120	146	161	175	192	166	195
1993 = 100	100.0	90.2	109.8	121.1	131.6	144.4	124.8	146.6
North-West	172	160	186	188	206	217	233	219
1993 = 100	100.0	93.0	108.1	109.3	119.8	126.2	135.5	127.3
North-East	193	181	221	223	246	267	287	280
1993 = 100	100.0	93.8	114.5	115.5	127.5	138.3	148.7	145.1
Italy	158	149	170	169	193	206	221	220
1993 = 100	100.0	94.3	107.6	107.0	122.2	130.4	139.9	139.2

Note. Source: Calculations of the author based on SVIMEZ data.

Table 10

Per Capita Capital Expenditures, Net of Expenditures for Direct Investments, of Italian Municipalities belonging to the Regions with ordinary statute in Years 1993-2000 (absolute values expressed in Euro 2001; Index Numbers: 1993 = 100)

Circumscriptions	1993	1994	1995	1996	1997	1998	1999	2000
Central	112	67	70	73	58	53	75	64
1993 = 100	100.0	59.8	62.5	65.2	51.8	47.3	67.0	57.1
Southern	59	31	31	40	26	30	27	40
1993 = 100	100.0	52.5	52.5	67.8	44.1	50.8	45.8	67.8
Island	25	16	23	36	19	20	16	28
1993 = 100	100.0	64.0	92.0	144.0	76.0	80.0	64.0	112.0
North-West	136	117	248	295	238	234	228	342
1993 = 100	100.0	86.0	182.4	216.9	175.0	172.1	167.6	251.5
North-East	41	35	41	56	80	60	48	53
1993 = 100	100.0	85.4	100.0	136.6	195.1	146.3	117.1	129.3
Italy	82	59	96	115	97	92	91	125
1993 = 100	100.0	72.0	117.1	140.2	118.3	112.2	111.0	152.4

Note. Source: Calculations of the author based on SVIMEZ data.

In this respect, weak point is the one regarding financial part of investments. In fact, a significant quota of them is financed in the Mezzogiorno not with ordinary resources but with State interventions.

This last data is confirmed in what is highlighted in Table 10 above. Value referred to capital expenditure different from direct investments corresponds to 72% in 1993, compared to national average level, and in 2000 at 32%. Compared to other districts, performance in terms of expenditure capacity after the 1994 *shock* is completely modest. Observe that other capital expenditures in 2000 count toward 36% of the overall capital expenditure at national level (61% for the North-West Italy).

Results of the Analysis

In order to evaluate the influence of 1992 currency crisis on the Municipal finance for all territorial circumscriptions, the measuring method of regional economic resilience suggested by Martin (2012, p. 16 ff.) has been used.

The resistance index r_{RES} is a sensitivity index; it measures the ability of a region or circumscription to “resist” an economic *shock* in comparison with the average of registered value in the overall regions or circumscriptions.

Algorithm used for calculation is the following:

$$r_{RES} = \frac{\frac{\Delta G_R}{G_R} - \frac{\Delta G_N}{G_N}}{\left| \frac{\Delta G_N}{G_N} \right|} \quad (1)$$

where $(\Delta G_R/G_R)$ and $(\Delta G_N/G_N)$ respectively represent variation of the economic factor considered at regional and national levels. A r_{RES} value higher than 0 provides a (relatively) higher “resistance” (less sensitiveness) of region or circumscription to the economic shock, compared to the rest of nation. On the other hand, a r_{RES} value lower than 0 stands for a (relatively) lower ability of region or of circumscription to resist (high sensitiveness) to the *shock*, compared to the national average.

On the contrary, recovery rate r_{REC} is referred to a later phase compared to the one where the unfavourable event occurred; it measures the ability of a region or a circumscription to recover after economic shocks.

In this case, algorithm used for calculation is the following:

$$r_{REC} = \frac{\frac{\Delta G_R}{G_R}}{\frac{\Delta G_N}{G_N}} \quad (2)$$

A r_{REC} value higher than 1 represents the ability of a region or of circumscription to develop quicker than the national average after the economic *shock* occurred. On the other hand, a r_{REC} value less than 1 means that a region or circumscription, after the economic *shock*, develops slower than the National average.

Table 11 shows the indices of resistance and recovery related to the identified phases of economic downturn and growth. The considered period goes from 1991 to 2014, a long time frame which includes the last downturn period too which affected our Country starting from 2007-2008.

Table 11

Indices of Resistance (a) and Recovery (b) Referring to the Trend of Direct Investments of Italian Municipalities Belonging to the Regions with Ordinary Statute in Years of 1992-2012

Period	Centre-North		Mezzogiorno	
	r_{RES}	r_{REC}	r_{RES}	r_{REC}
1992-1994	0.16	-	-0.37	-
1994-1998	-	1.12	-	0.68
2009-2012	0.17	-	-0.44	-

Notes. (a) Algorithm used for the calculation of the resistance index: $r_{RES} = [(\Delta ID_R/ID_R) - (\Delta ID_N/ID_N)]/|\Delta ID_N/ID_N|$, where $(\Delta ID_R/ID_R)$ and $(\Delta ID_N/ID_N)$ are, respectively, the variation of direct investments at regional and national levels. (b) Algorithm used for the calculation of the recovery index: $r_{REC} = (\Delta ID_R/ID_R)/(\Delta ID_N/ID_N)$. Source: Calculations of the author based on SVIMEZ data.

Municipalities of Centre-Northern show, for the whole considered period, a high financial resilience compared to the ones belonging to regions of Mezzogiorno (Island and Mainland), in terms of both resistance and recovery to economic shocks, like the one represented by 1993 currency crisis and by the following financial “adjustments” on the State grants which marked the trend of current revenues of Municipalities from 1993 to 2001. However, it is not difficult to identify the determinants of the municipal finance system’s less resilience of Southern Italy. As we have revealed from the analysis made in the Section 3, it is clear that explanatory variables of the phenomenon are basically two: the ratio between staff expenditure and current expenditure or, even better, the programmability index of balance sheets, and the ratio between tax revenue and income of the considered communities. Data given in Table 7 show, in fact, lower programmability values of balance sheets of the Southern Italy Municipalities and, above all, of the Islands ones. This phenomenon was caused, as explained by SVIMEZ in its annual “*Report on the Economy of Southern Italy*”, by lower revenue of taxes assigned to municipal administrations and, therefore, ultimately by choices of tax decentralisation implemented by the Italian legislator during those years. In fact, higher revenue “is the result of the tax base distribution on the territory, which is that characteristic of strongly progressive taxes, such as the ICI and the IRPEF” (SVIMEZ, 2001, p. 341 ff.).

The main instrument of municipal tax autonomy, introduced starting from the ‘90s, and the mechanism of IRPEF⁴ revenue sharing, as they are strongly progressive compared to the income, conflicts with the basic equality concept of citizens, according to the meaning given by Buchanan (1950) since 1950. However, unfortunately, it seems that the Italian legislator apparently ignores, or pretends to ignore that:

Starting from 1994, system of State grants to Municipalities has to offset the strongly progressive distribution of ICI compared to the income, and so that each provision reducing (even proportionally) revenue transfers by the State or making situation of territorial governments worse, whose level of transfers is higher (like in the case of the internal stability “pact” and the system of sole treasury), unjustifiably undermines the financial situation of weakest Municipalities and ultimately life conditions of each citizen belonging to them. (Pica, 2003)

Furthermore, it is necessary to consider, as we have predicted (see Section 3.4: Capital Expenditure), that a significant part of direct investments of Municipalities is financed in the Mezzogiorno not with ordinary resources, but with State interventions. This phenomenon further increases vulnerability of municipal finance system, which is exposed not only to risks deriving to an unfavorable trend of the economic cycle, but also to variations of the financing regime (grants and expenditure constraints) established by the central government.

⁴ IRPEF (*Imposta sul Reddito delle Persone Fisiche*) is the personal income tax applied in Italy by the central level of government.

Conclusions

This paper is a first pioneering attempt to apply the concept of resilience to the analysis of the public finance systems of local governments, a concept already used and “abused” in various disciplines and fields of knowledge. In particular, it proposes an attempt to estimate the degree of resilience of Italian Municipalities in a crucial period of our country’s financial history, between 1992 and 2000, or between the currency crisis and the introduction of the Euro. In this period, in fact, the EMS, although formally operating, entered in deep crisis. The lira and the pound sterling, subjected to the strong pressure of financial speculation, which thwarted every effort of central banks to keep parity with the ECU (the European Currency Unit), had to abandon the system and gradually, after a transitional period of economic convergence of the member countries of the European Community, the Euro was introduced (1999). The analysis in the paper, however, does not only take into consideration this period of deep crisis of Italy and EMS. It also involved the subsequent trends, in order to demonstrate that the current vulnerability of the municipal public finance system, in particular of the Municipalities of Southern Italy, depends not only on the economic cycle but also on the continuous and incessant changes in the financing mechanisms of local governments established by the central government.

The analysis showed, for the whole considered period, a lower financial resilience of the Municipalities of the Mezzogiorno (island and continental) compared to those of the Center-North, in terms of both resistance and recovery to economic shocks represented by 1993 currency crisis and by the following financial “adjustments” on the State grants which marked the trend of current revenues of Municipalities from 1993 to 2001. The determinants of this phenomenon were found, for one part, through the analysis of the financial data of the Italian Municipalities – as presented by the SVIMEZ in its annual reports on the economy of the Mezzogiorno – and, for another part, through the critical synthesis of significant economic events which occurred during the examined period. The determinants of this phenomenon are basically two. The first is represented by the wrong choices in the decentralisation of tax autonomy made by the Italian legislator in those years: The main instruments of municipal tax autonomy, introduced starting from the ‘90s, and the mechanism of IRPEF revenue sharing, as they are strongly progressive compared to the income, are incompatible with the basic equality concept of citizens and unjustifiably undermine the financial situation of weakest Municipalities. The second depends on the financing system of direct investments of Municipalities, which is funded in the Mezzogiorno not with ordinary resources, but with State grants: this system increases vulnerability of municipal finance system, which is exposed not only to risks deriving to an unfavorable trend of the economic cycle, but also to variations of the financing regime (grants and expenditure constraints) established by the central government.

In conclusion, the financial resilience analysis contained in the paper will undoubtedly provide useful insights to study more in dept a difficult period of the financial history of the Italian State, but it can also give an important lesson for the future. The main lesson is that wrong financial choices of central government can lead to a worsening of the vulnerabilities of the financing system of local governments and, in this way, weaken their ability to react to unexpected economic shocks.

References

- Brand, F. S., & Jax, K. (2007). Focusing the meaning(s) of resilience: Resilience as a descriptive concept and a boundary object. *Ecology and Society*, 12(1), 23.
- Buchanan, J. M. (1950). Federalism and fiscal equity. *American Economic Review*, 40(4), 583-599.
- Duval, R., & Vogel, L. (2008). Economic resilience to shocks. *OECD Economic Studies*, 1, 1-38.
- Holling, C. S. (1973). Resilience and stability of ecological systems. *Annual Review of Ecology and Systematics*, 4(1), 1-23.
- Martin, R. (2012). Regional economic resilience, hysteresis and recessionary shocks. *Journal of Economic Geography*, 12(1), 1-32.
- Martin, R., & Sunley, P. (2014). On the notion of regional economic resilience: Conceptualization and explanation. *Journal of Economic Geography*, 15(1), 1-42.
- Pica, F. (2003). La questione dell'autonomia degli Enti territoriali nella riforma del Titolo V della Costituzione in alcuni recenti studi. *Rivista economica del Mezzogiorno*, 17(1/2), 19-46.
- Pica, F., & Villani, S. (2010). Le scelte tributarie del federalismo fiscale. Implicazioni per le Regioni del Mezzogiorno. *Rivista economica del Mezzogiorno*, 24(4), 839-862.
- Rossi, S. (2007). *La politica economica italiana 1968-2007*. Roma-Bari, Laterza.
- Rossi, S. (2011). *Aspetti della politica economica italiana dalla crisi del 1992-93 a quella del 2008-09*. In M. Ciaschini, & G. C. Romagnoli (Eds.), *L'economia italiana: modelli, misurazione e nodi strutturali – Giornata di studio in onore di Guido M. Rey*. Milan: Franco Angeli.
- SVIMEZ (various years from 1995 to 2001). *Rapporto sull'economia del Mezzogiorno*. Bologna, Il Mulino.
- Viesti, G. (1996). Che succede nell'economia del Mezzogiorno? Le trasformazioni 1990-199. *Meridiana*, 26/27, 91-130.
- Visco, I. (1999). *Politica monetaria e inflazione in Italia, 1994-96*. In N. Acocella, G. M. Rey, & M. Tiberi (Eds.), *Saggi di politica economica in onore di Federico Caffè*. Milan: Franco Angeli.
- Walker, B., Holling, C. S., Carpenter, S. R., & Kinzig, A. (2004). Resilience, adaptability and transformability in social-ecological systems. *Ecology and Society*, 9(2), 5.