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Ministry of Economy and Finance
Department for Development Policies

2004 Annual Report on Actions in Under-Utilised Areas

Executive Summary

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Submitted to the Italian Parliament by the Hon. Deputy
Minister of Economy
Mr. Gianfranco Miccichè

31 Gennaio 2005

2004 ANNUAL REPORT

on Actions in Under-Utilised Areas

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January 31, 2005

This Report, prepared by the Department for Development and Cohesion Policies (DPS) of the Ministry of Economy and Finance, provides an outline of economic trends and development policies at a territorial level.

All units of DPS were involved in writing the Report: under the responsibility of the Research Service headed by Letizia Ravoni, these include the Service for Territorial Development Policies headed by Paolo Signorini, the EU Structural Funds Policy Service headed by Paola De Cesare, the CIPE (Interdepartmental Committee for Economic Planning) Secretariat, the Service for External Cooperation, the Evaluation Unit co-ordinated by Laura Raimondo, and the Verification Unit coordinated by Aldo Mancurti.

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Special thanks go to all the staff involved in the preparation of this Report for their dedication and care.

PREFACE

By Deputy Minister, the Hon. Gianfranco Micciché

This year's Report of the Department for Development and Cohesion Policies (DPS) provides us with a picture of our Southern regions which once again shows positive and encouraging elements, encouraging us to continue our efforts to identify new strategies and tools for economic growth.

Yet again, EU resources were fully utilised within the end-of-year deadline and, thus, no Region of the South was subject to automatic decommitment of funds. This is no longer a novelty (indeed, since 2002 this has happened every year), but the consolidation of positive results testifies to a definite leap forward in quality achieved by the administrations in programming and in spending funds such that only pessimists could continue to maintain that this is merely due to chance.

Secondly, in terms of additional national resources financing works included in the Framework Programme Agreements, contract award tendering procedures for a majority of the works were finally carried out in 2004. The acceleration of this process was due, in particular, to the new performance-rewarding and penalty mechanisms introduced in 2002 by the Interdepartmental Committee for Economic Planning.

However, the full use of EU reimbursements and national resources is not in itself a positive result, though it is clear evidence that, for a number of years now, Italy has begun to develop the most backward areas of the country. The results are becoming apparent. Indeed, this Report highlights a significant improvement in the water and energy sectors; the conditions for the general improvement of service provision to citizens and for a real reduction in the infrastructure gap in the transport sector have been determined. Furthermore, it is a point of pride for me, personally, to be able to recall that 2004 was also the year in which the Palermo-Messina highway, begun in 1969, was finally completed.

Encouraging signs are also evident in the growth of the number of businesses, in the substantial and constant drop in the unemployment rate, and in the level of exports from the South, which confirms the growing competitive capacity of an area that was traditionally lagging in the foreign trade sector.

These and yet other signs are positive and encouraging but, in all honesty, it must be admitted that there are still many areas that are suffering and lagging in the South of Italy. In my opinion, despite the important steps forward, further work is needed to formulate new national strategies in the tourism sector, to further increase investment in research and innovation, and to continue to improve the still-lagging sectors of health and education.

Today, we are facing a very delicate phase. Right now, Italy - which is one of the principal net contributors to the European Union - is negotiating reform of EU cohesion policy for the years 2007-2013. We are strongly supporting the need for clear rules to guarantee the quality of expenditure, genuine additionality and

greater links between cohesion policies and competition policies. The credibility that we have achieved in the use of EU funds allows us now to take a tough position on these issues.

It is now necessary to carry on, to believe in and stake our chances on development, fully aware of our potential. It is evident that where political renewal has been accompanied by government stability, development strategies and interventions have been more able to unleash their positive effects. Nor can it pass unnoticed that where good and sound policy management has been able to rely on a modern and rigorous public administration, results have been achieved which were inconceivable in the past.

Optimism, formulating planning strategies, renewing the political class, modernising the public administration, rigour and stability of government: this is the message to be drawn from our Southern Regions, in order to face the challenge of growth and competitiveness. With the certainty of success.

EXECUTIVE SUMMARY

There is nothing inevitable in the social and economic backwardness of a territory. But overcoming backwardness depends on the determination with which business and political leaders demand and help deliver greater competition and better services. This is one of the lessons from the new development of the South of Italy (the so-called *Mezzogiorno*) portrayed in this Report.

The document, prepared by the Department for Development and Cohesion Policies (DPS) of the Ministry of Economy and Finance, reports annually to the Parliament on social and economic trends and policies implemented in different regions of the country, namely in its under-utilised areas¹. Particular attention is paid to the South of Italy and to some disadvantaged areas of the Centre-North, which are the subject of two coordinated regional policies: EU policy, implementing the European Treaty, and national policy implementing the Italian Constitution (Article 119, paragraph 5), through the Fund for Under-utilised Areas.

The picture of the *Mezzogiorno* which emerges defies easy stereotypes. This is evident from the successes obtained, namely persistent entrepreneurial and administrative renewal, less external economic dependence (less aid and lower net imports), ongoing progress in infrastructure and services, dissemination of points of excellence (including urban services) and some signs of credit recovery. It is also apparent from the critical points, such as hindered growth (though greater than in the Centre-North), still seriously inadequate quality of many essential services, still excessively high aid expenditure compared to spending on tangible and intangible infrastructure, deficit of competition, including the presence of organised criminal pressures, and the low-level contribution of credit to development.

The familiar *Mezzogiorno* continues to exist, since weakness in both competition and collective services, which holds back the Italian economy and society in general, retains a systemic character and blocks growth in productivity and well being. But we are no longer dealing with the same *Mezzogiorno* of the past.

Today's *Mezzogiorno* is not quite like that of the early 1990s, when subsidies and aid still dominated and both responsibilities and financial resources were lacking at local level. Nor is it the same as that of the mid-90s, with signs of new vitality but lacking the guidance of economic policy. It is not even the *Mezzogiorno* of the late 1990s, when the new policy had only taken its first steps. Today, we are dealing with an area in ferment, with strong processes of change

¹ The term "under-utilised areas" refers to all areas which are deemed worthy of development intervention over and above ordinary intervention, through recourse to EU (and national co-financing) resources – objectives 1 and 2 areas of the 2000-2006 EU Programme – or national resources (cf. the paragraph 5 of Article 119 of the Italian Constitution). For a description of the way in which these areas are identified, including 8 Regions of the South of Italy and the areas of all the Regions of the Centre-North, refer to the Executive Summary and par. III.1.2 of the Third DPS Report.

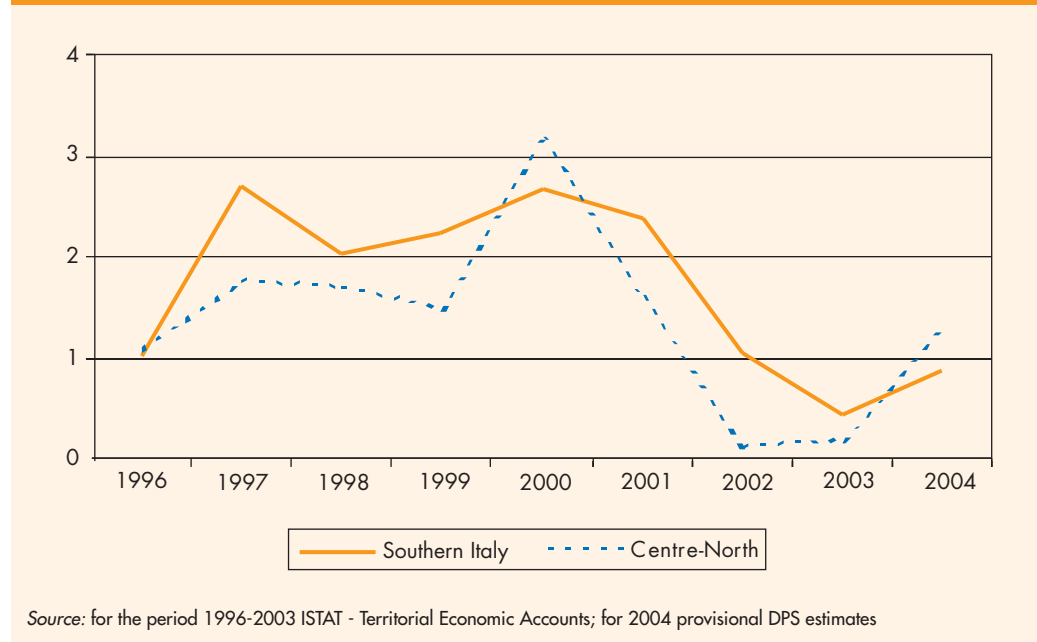
and strong elements of resistance. Regional institutions are at times unrecognisable compared to their state a few years ago, although the decision-making process for priority selection needs to be reinforced; infrastructure and services are improving, although the impact on productivity is taking a long time to be felt; non-agricultural employment is growing, although the labour market remains depressed.

The economic policy employed in recent years is not extraneous to the positive results. True, the new phase began midway through the last decade due to the healthy reaction of society and the markets, to the sudden reduction of State intervention. But when the State resumed a policy for the South, it did so according to a completely new methodology. It stayed away, as far as possible, from subsidies, and opted instead for a supply policy aimed at better services, competitiveness and institutional renewal.

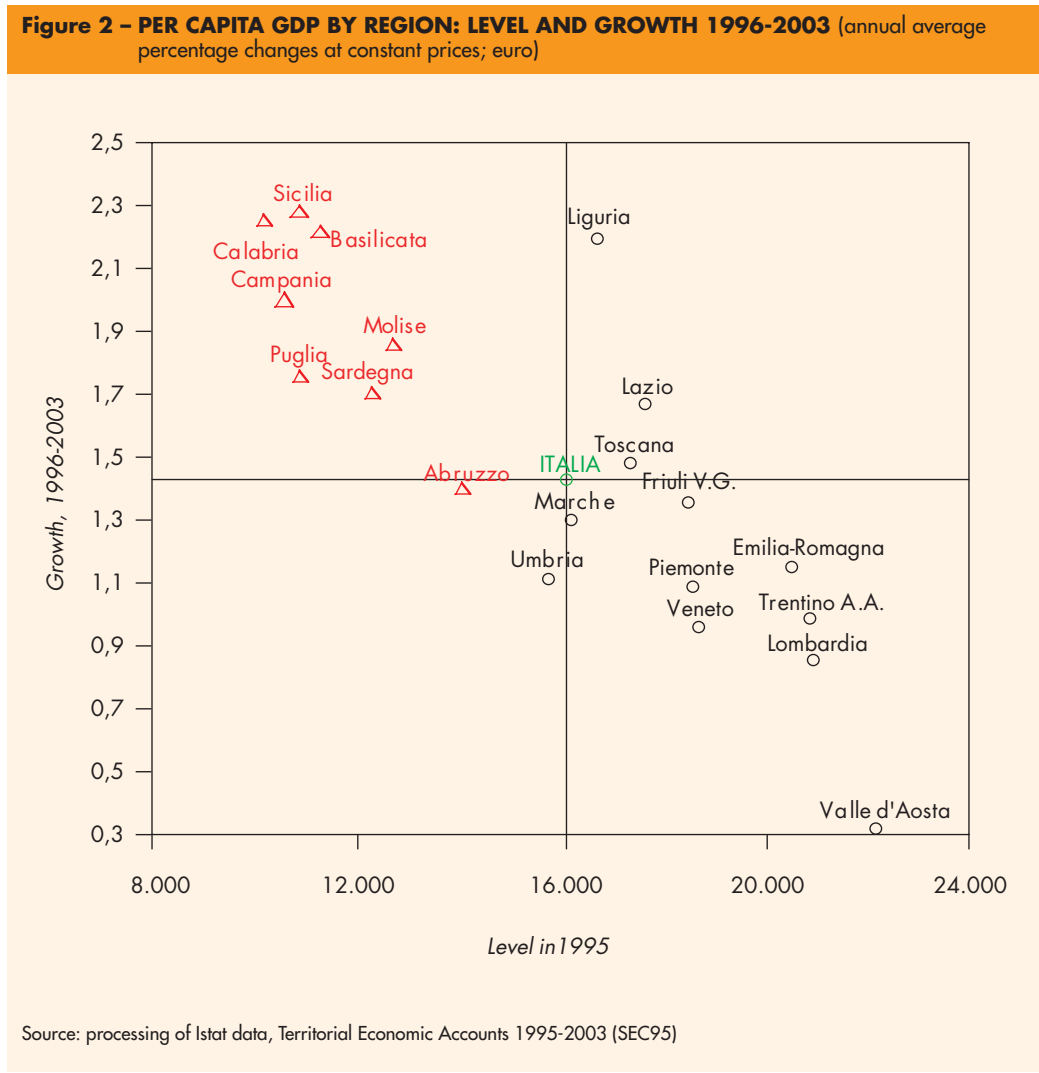
It was, and still is today, a difficult path, which does not deliver immediate results and requires determined persistent business and political leaders ready to break with established rents.

During 2004, a positive cyclical turnaround took place. However, in the South of Italy, as in 2000, this manifested itself later than it did in the Centre-North (fig. 1)

Figure 1 - TERRITORIAL GDP GROWTH 1996-2004 (percentage changes at constant prices)

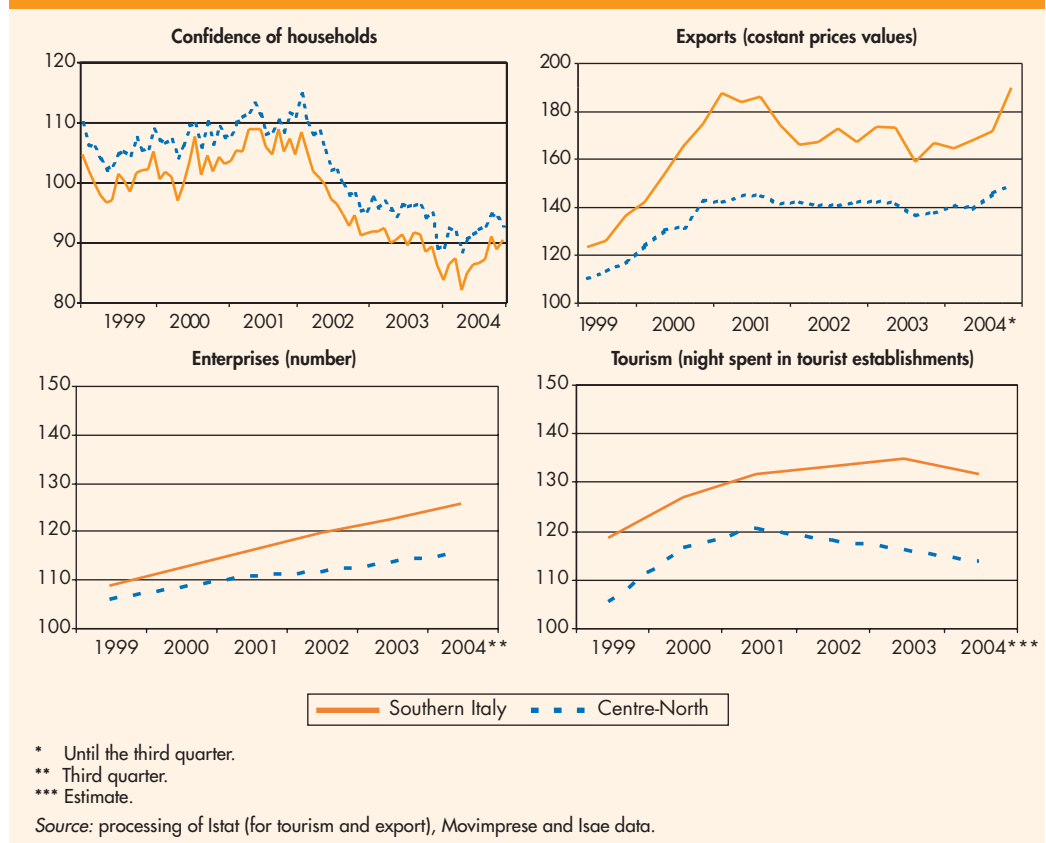


According to this reading, the new phase - which since the mid-1990s has seen the South of Italy grow a half point more than the Centre-North every year, a positive differential never seen in the Republic's history - is still in progress. It is a trend which finally sees a per capita GDP growth in Italy inversely proportionate to the starting value (fig. 2). Changes in productivity, which between 1995 and 2003 grew by 1 per cent per annum in the South of Italy, as against 0.4 per cent in the Centre North, have been determining factors in this trend.



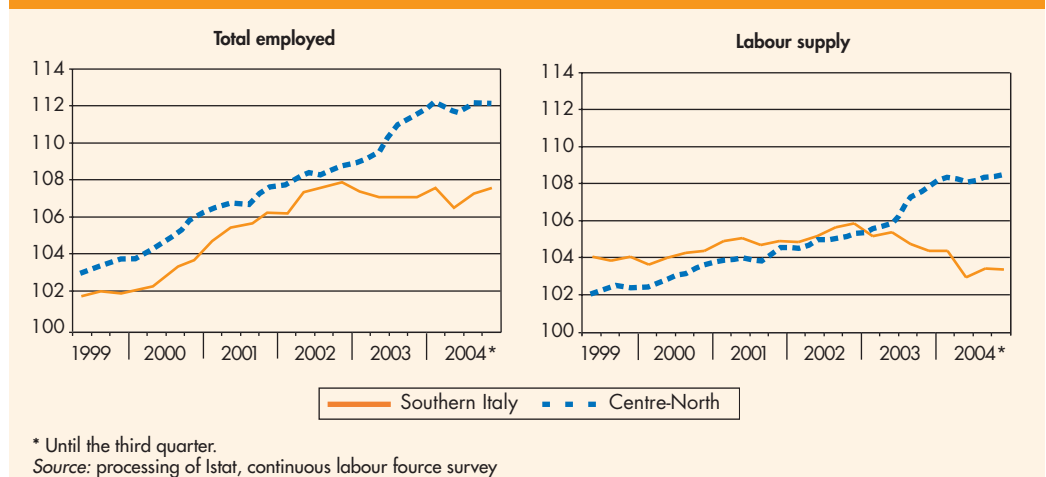
Compared to the previous years, 2004 was marked by the slow pace of tourism flows, while the strong entrepreneurial dynamism and the improvement in exports was confirmed (fig. 3). The reduction in external economic dependence is indeed turning out to be one of the main features of the new development of the South.

Figure 3 – INDICATORS OF THE TERRITORIAL CYCLE (1995=100)



A slight recovery was also evident in the level of employment, once again on the rise in the South of Italy after the downturn that took place starting from the middle of 2002. Labour supply, which for more than a year dropped more rapidly than demand (indicating a drop in people's confidence to look for a job) has stabilised (fig. 4).

Figure 4 – NO. OF EMPLOYED AND LABOUR SUPPLY BY MACRO-AREA 1999-2004
(1995=100; de-seasonalised data)



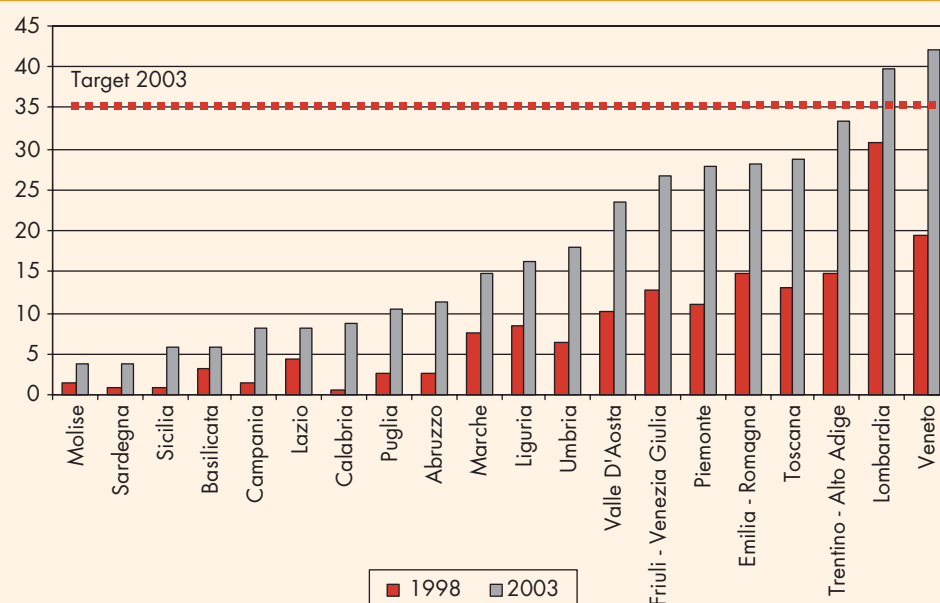
The rate of unemployment has thus undergone a further drop (to 14.7 per cent).

The persistence in the South of Italy of a condition of “hindered development” is mostly due to the quality of collective services. The analysis undertaken in this Report for all European Regions shows that it is not the peripheral nature of Regions *per se* - measured by their distance from the European centre of gravity - which explains differences in productivity, but rather the quality of services such as education and transport infrastructures.

Current policy for the South is aimed at reducing the lag in the supply of collective services. Only the persistence of this policy as planned in national programming documents, and in agreements with the European Union, can reduce the lag which has accumulated over time.

The commitment to improve infrastructures and their management is beginning to address backwardness in the South of Italy for several important public utility services, such as water and waste collection. Only persistence with this commitment, however, together with an increase in the degree of competition in the market for services and a concentration of providers, can enable a positive and timely outcome. For water, efforts made in the South, due in part to the incentives and rules defined by EU programming, have achieved a result greater than expected: the appointment in mid-2004 of relevant Authorities in all the water basins, a pre-condition for any further progress and a better result than that obtained in the Centre-North. The completion of this process now requires overcoming the strong fragmentation of supply and a revision of the current tariff mechanism. The delays, achievements and opportunities in the area of disposal of urban waste are similar (fig. 5).

Figure 5 - SHARE OF DIFFERENTIATED WASTE COLLECTION OVER TOTAL WASTE PRODUCED¹



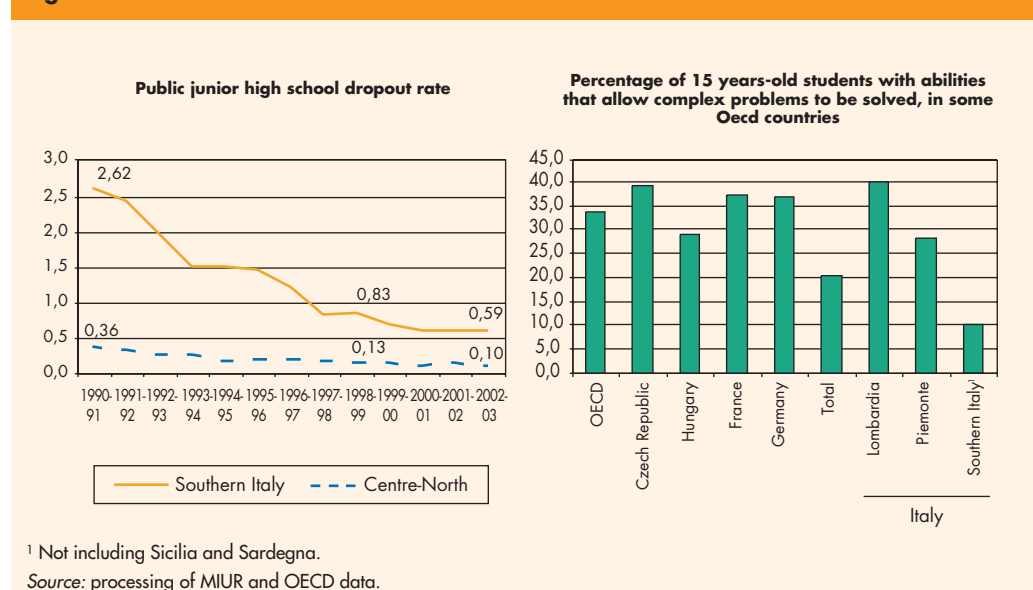
¹ The targets of differentiated urban waste collection (the 15 percent by 1999 and the 35 percent by 2003) are determined by art. 24 of D.Lgs 22/1997 (so called "Decreto Ronchi"). In Italy the 2003 target has been seldom achieved and overcome only by Veneto and Lombardia, while the eight southern regions did not reach in 2003 the 1999 target.

Source: processing of Istat data

For the big networks, especially transport, a reversal of past trends has begun with the coming into force of the so-called “*Legge Obiettivo*” (a law for public works projects), which by the end of the decade should also set a rebalancing process in motion between the two areas of the country. It involves 162 projects throughout Italy, of around 24 billion euro in public expenditure. 8.5 billion were decided on by CIPE (the Interdepartmental Committee for Economic Planning), 49 per cent of which were allocated to the South of Italy. After the intervention on procedures and the acceleration of sub-contracting, it is now necessary, by means of cogent monitoring, to verify and promote a timely implementation of public works.

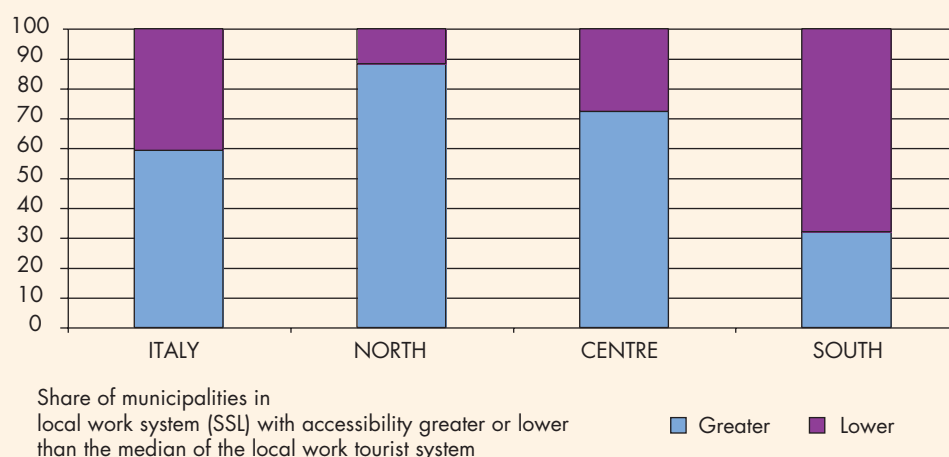
So wide is the gap that has developed in the South in the field of education, that the progress made towards reducing the school dropout rate is not sufficient to bridge it. A recent study carried out by the OECD in 49 countries on the mathematical abilities of 15-years-old students, essential for contributing to competitiveness, especially with the existence of highly-evolved and specialised technologies but also due to the increased complexity of all social and economic contexts, shows a particularly lagging situation in Italy despite the rather positive results of its northern Regions. The percentage of students with abilities that go beyond carrying out clearly described procedures, and which allows complex problems to be solved, is equal to 20.4 per cent in Italy, compared to the OECD average of 33.7 per cent (fig. 6). The Centre-North areas have figures between 28 and 40 per cent, while the South does not exceed 10 per cent, revealing a serious gap within the country. This is a gap which, according to general evaluations that the OECD has itself carried out for all industrialised countries, could to a rather significant extent be due to the school attended.

Figure 6 – THE RELATIVE STATE OF EDUCATION



Social services are also insufficient, both as regards recourse to Local Health Centres and to Casualty Wards (judged to be problematic by 15 per cent of families, as against 9 per cent in the North), as well as in relation to the state of housing. Accessibility remains a strong impeding factor to development in the South. Around 70 per cent of municipalities in protected areas, where the importance of the natural heritage is protected and is a source of particular interest, manifest accessibility conditions lower than the average accessibility of local tourist systems, while this same statistic is around 10 per cent in the North and 30 per cent in the Centre (fig. 7).

Figure 7 – ACCESSIBILITY OF MUNICIPALITIES IN PROTECTED AREAS IN RELATION TO THAT OF LOCAL WORK TOURIST SYSTEMS (percentage shares)



Note: Data refer to municipalities with more of 10 percent of surface included in protected areas, excluding the "metropolitan areas capitals". In the graphs the share of municipalities belonging to the local work system (SSL) with values of accessibility index (defined by ISFORT) greater or lower than the median value of the local work tourist system (Tourist SSL) is represented.

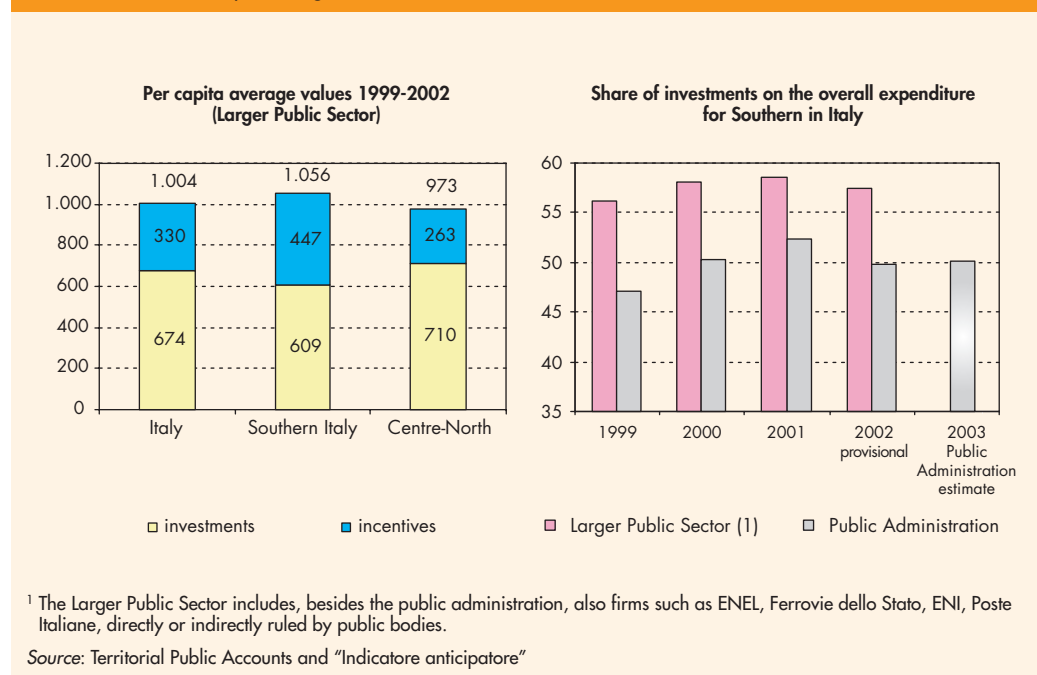
In the field of law and order, the pressure of organised crime remains higher in the South, with 10.8 crimes of this nature committed for every 10,000 inhabitants, as against 8.9 in the Centre-North. However, despite the continued presence of specific and serious situations of emergency, the strong commitment of crime prevention and crime-fighting policy has, in recent years, reduced the gap between the two macro-areas, due also to a significant decrease in the South of some serious crimes (homicides, smuggling, and serious robberies). In 2003, there was on average a substantial re-alignment at the national level of perceived security by families in relation to their area of residence (27.9 per cent of families in the South declared that they lived in an at-risk crime area, compared to the Italian average of 27.4 per cent²).

² Source Istat, Multipurpose survey "Aspetti della vita quotidiana" ("Aspects of daily life")

The Report illustrates policy trends in terms of financial commitments and institutional changes.

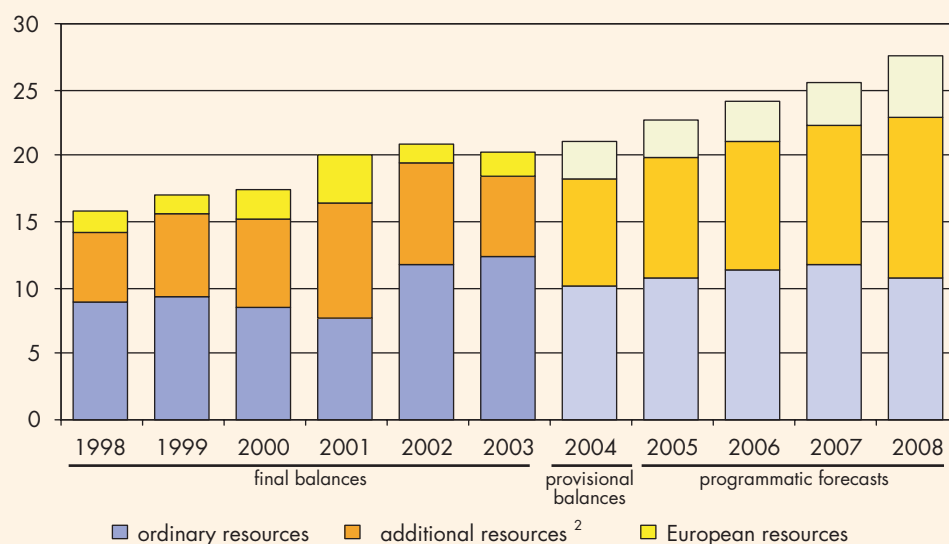
In the South in the period 1999-2002 only 609 euro per citizen was spent annually on tangible and intangible infrastructure, compared with 710 euro in the Centre-North. This serious gap existed, despite a higher capital expenditure commitment in the South than in the Centre-North (1,056 euro per capita as against 973 euro). For this reason, it is important to shift the balance of capital expenditure from incentives to public investment in infrastructure. In the last five years, the share allocated to public investment in tangible and intangible infrastructure, as against total capital expenditure in the larger public sector, has grown by around 4 points (fig. 8), but the progression is not continuous, and remains lower than planned.

Figure 8 - CAPITAL EXPENDITURE: PUBLIC INVESTMENTS AND INCENTIVES
(euro and percentage values)



In absolute terms, capital expenditure of the public administration aimed at the South has grown significantly, from an average value of around 17 billion euro in 1998-2000 to an average value of 20.5 billion euro in 2001-2003, also with a slight increase (from 39 to 39.5 per cent) in the share of total capital expenditure of the country. The achievement of EU spending objectives in the coming years, a clear progress in spending capacity also for national regional funds, the timely allocation and use of resources assigned by the 2005 Budget Law to the Under-utilised Areas Fund (7,8 billion euro, equal to 0.56

Figure 9 - PUBLIC CAPITAL EXPENDITURE IN THE SOUTH OF ITALY: RESULTS AND FORECASTS¹
(billion euro)



¹ Data refer to the Public Administration. For the period 1998-2003 final data; for 2004 provisional data; for the period 2005-2008 programmatic forecasts of the Community Support Framework mid-term review approved by the European Commission in December 2004.

² They include the European Funds cofinancing and the national regional policy resources from the Under-utilised Areas Fund.

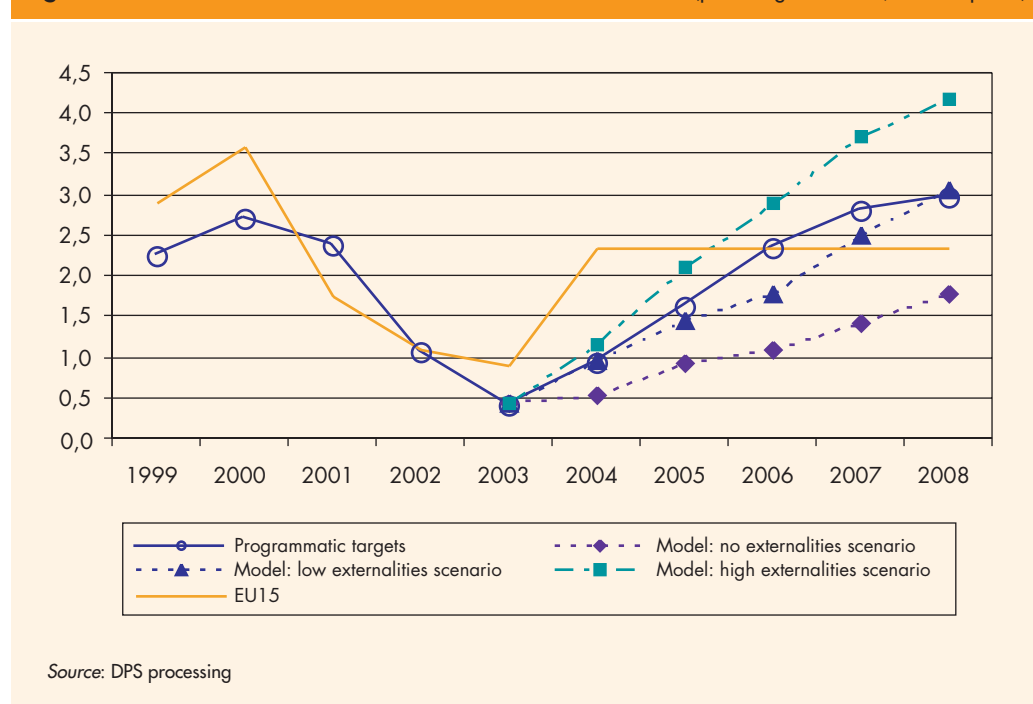
Source: Quadro Finanziario Unico

per cent of the GDP), and the more rigorous pursuit of the objective of channelling to the South 30 per cent of funds allocated for ordinary capital expenditure: all these represent the conditions for a further increase in capital expenditure in the South according to the profile set out in figure 9 and undertaken with the European Union in December 2004. Though these total and additionality targets are lower than those originally fixed, they nonetheless represent rather demanding goals.

Providing these goals were to be achieved and the balance between incentives and public investments were also to take place, together with higher quality of spending, the objectives for GDP growth in the South set in the new programming documents could be achieved. As shown by the simulations carried out using the Department's econometric supply model, results depend not only on the multiplier effect of public expenditure, but especially on the positive externalities that the improvement of services can produce in a local context. Greater caution in setting the forecasts was anyhow suggested by the experience gained in previous years, when effective GDP growth in the South was inferior to that originally planned, not only (for about two thirds) due to the in-

ternational cycle - lower than forecasted - but also (for the remaining third) due to lower capital expenditure and the lack of these supply-side effects originally foreseen. GDP growth in the South is then now expected to exceed the European average only since 2007 and not, in any case, to exceed 3 per cent per annum (cf. fig. 10).

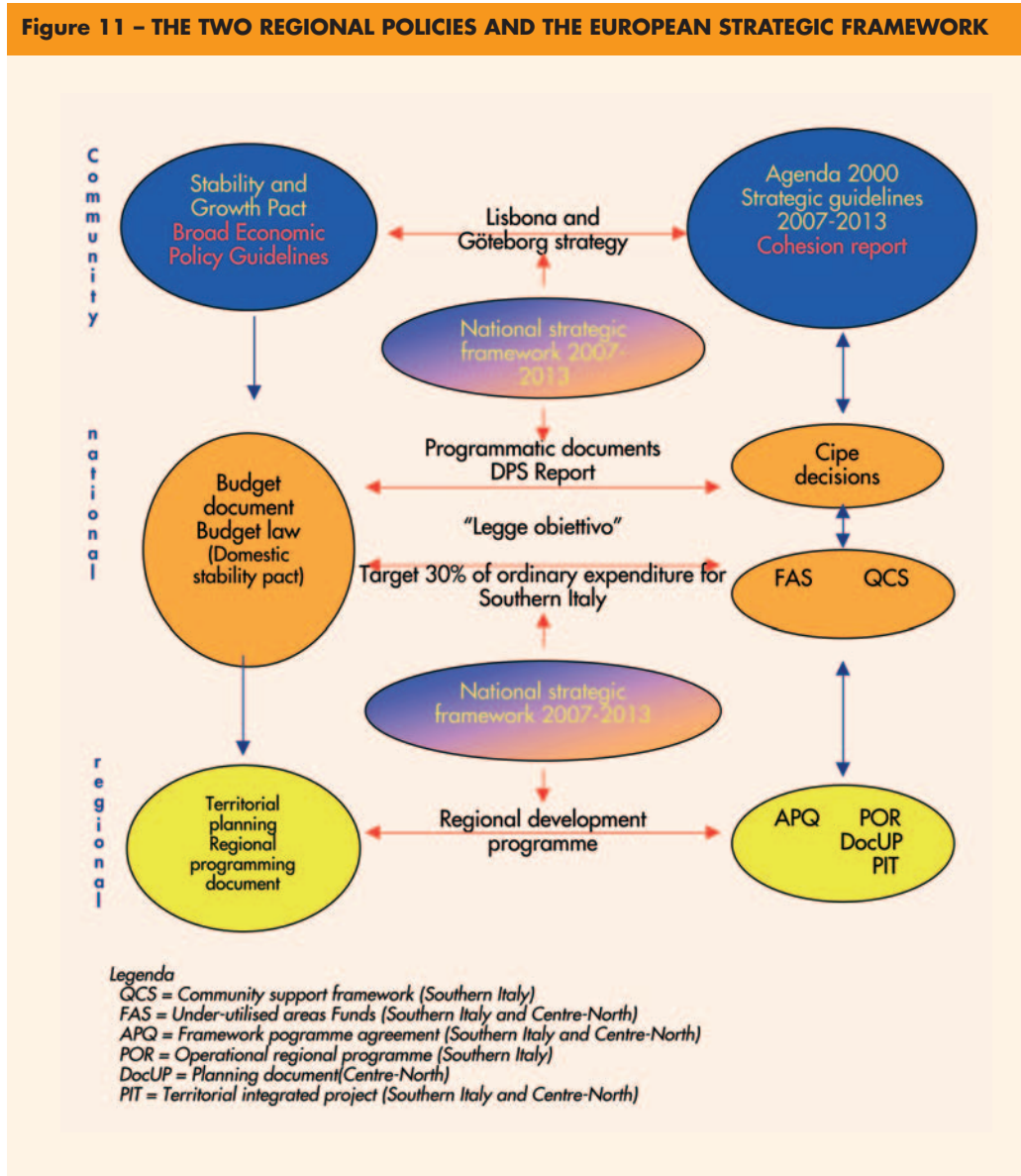
Figure 10 – GDP GROWTH SCENARIOS IN THE SOUTH OF ITALY (percentage variations, constant prices)



The effectiveness and integration of EU and national regional policies, and of these two policies with economic policy as a whole, were reinforced within the context of the intense European debate during 2004 over cohesion policy, on its role and its limits in the achievement of the competitiveness objectives set in Lisbon.

The critical points brought to light by the frank debate helped set the foundations to make the current regional policy more binding and strategic, both in the South of Italy and in the Centre-North. The functioning of the Underutilised Areas Fund, the progressive adoption of rules and guidelines for national regional policy partly inspired by those which govern the use of EU funds, and the strong regional commitment to mark a turning point in the multilevel governance tool (the Framework Programme Agreements) through which Regions and the central State coordinate their interventions, have already produced tangible effects. Others will come about through the work

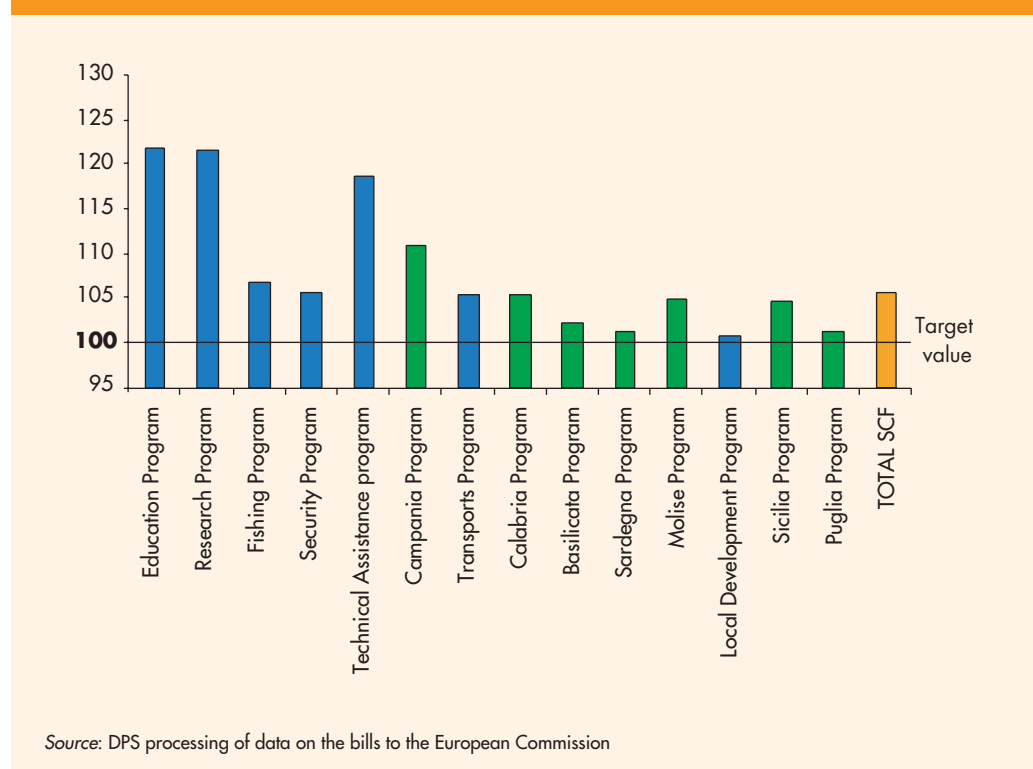
which has already been started, together with local authorities and social and economic actors, on elaborating the National Strategic Framework for the 2007-2013 period (cf. fig. 11).



This framework explains, together with financial considerations, Italy's strong backing of the Commission proposal for the 2007-2013 Financial Perspectives and the strong stance in the negotiation. Both in the South of Italy and in the Centre-North, cohesion policy is a tool generating service quality and institutional renewal and consolidation of a national regional policy depends on cohesion policy being retained. Together with rural development policy, cohesion policy represents the only line of intervention contributing to the net financial balance with the European Union.

The positive results obtained in the management of EU funds contributed to strengthening Italy's negotiating position. The end of 2004 saw not only a new success, namely the avoidance of automatic decommitment of resources (cf. fig. 12), but also a significant increase in the efficiency of the responsible administrations, which, spurred by performance-rewarding mechanisms, reduced the seasonal nature of their expenditure. Thanks to the advance timing with which payment requests were received, 4.6 billion euro in reimbursements were obtained by 31 December from the EU budget, which contributed to reduce the net indebtedness of public administrations. These results were obtained in the context of the results of the mid-term review of EU programmes, both in the South of Italy and in the Centre-North, which re-confirmed the strategic priorities, while introducing some adjustments in the implementation process.

Figure 12 – COMMUNITY SUPPORT FRAMEWORK PROGRAMMES OBJECTIVE 1 2000-2006: LEVEL OF ACHIEVEMENT OF "TARGET VALUE" OF PAYMENT REQUESTS AS AT 31 DECEMBER 2004 (percentages)



As regards the use of EU funds, tangible and intangible infrastructure projects are turning out to be more concentrated than in the past. The ten most significant projects absorb over 1 billion euro of resources, while the first one hundred exceed 4 billion euro. These first one hundred projects show a concentration in some public utilities (water, waste and energy at about 900 million euro), train and metropolitan transports (at about 1.3 billion euro), roads and motorways (at about 1 billion euro) (cf. fig. 13).

Framework Programme Agreements (FPA), whose programming strongly accelerated in 2002 and 2003, in 2004 witnessed a positive turnaround in the awarding of contracts. The binding obligations and incentives introduced by the CIPE in 2002-2003 and Regions' learning process contributed to this result. For FPA financed in 2002, 40 percent of all funds were contracted by June 2004; in the following months there was a further acceleration, driven by the deadline (31 December 2004) set by CIPE for the commitment of resources. The final outcome will be made public in March 2005.

Figure 13 – PRINCIPAL 100 INFRASTRUCTURE PROJECTS LAUNCHED BY THE COMMUNITY SUPPORT FRAMEWORK 2000-2006 OBJECTIVE 1¹ (units, million euro)

| Typologies | Number | Expected cost |
|---|--------|---------------|
| Water and sewer plants | 29 | 537 |
| Waste disposal plants | 5 | 325 |
| Energy network | 3 | 65 |
| Infrastructure and services for enterprises | 5 | 102 |
| Cultural and recreational structures | 6 | 120 |
| Railways | 21 | 914 |
| Subways | 3 | 361 |
| Airports | 3 | 111 |
| Ports | 3 | 54 |
| Highways | 2 | 411 |
| National and regional roads | 16 | 564 |
| Monitoring systems for crime prevention | 4 | 181 |

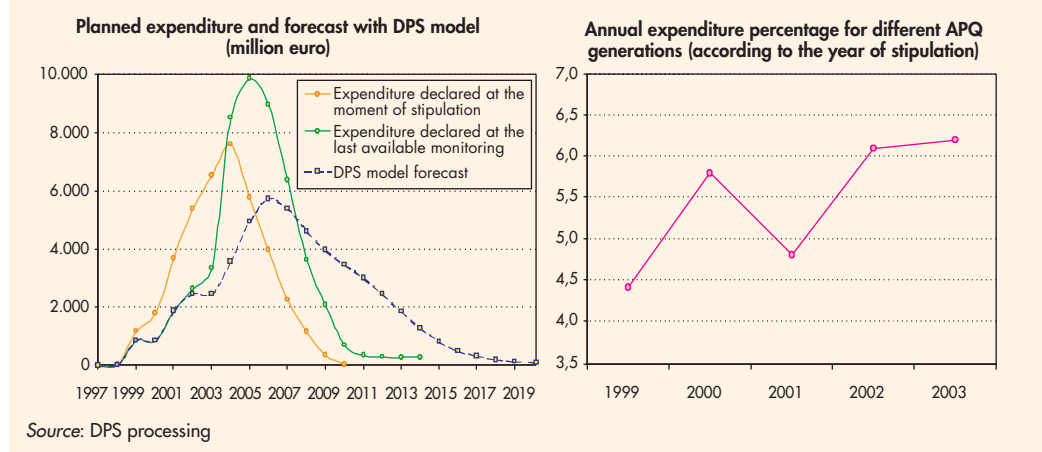
¹ Infrastructure projects already financed by the Support Community Framework (SCF), and for which at least the 5 percent of their cost has been paid.

Source: DPS processing.

Progress is extending to national regional policy which had long been affected by strong inefficiency in the implementation process. A difficulty on the part of administrations in making accurate forecasts for spending time still exists. The DPS has dealt with this issue - a correct assessment of cashflow needs is indispensable for improving the trade-off between budget rigour and spending objectives – by making its own forecasts. The ability to spend of administrations is anyhow improving: from an implementation cost equal to 4.4 per cent per annum for agreements signed in 1999, the share has risen to more than

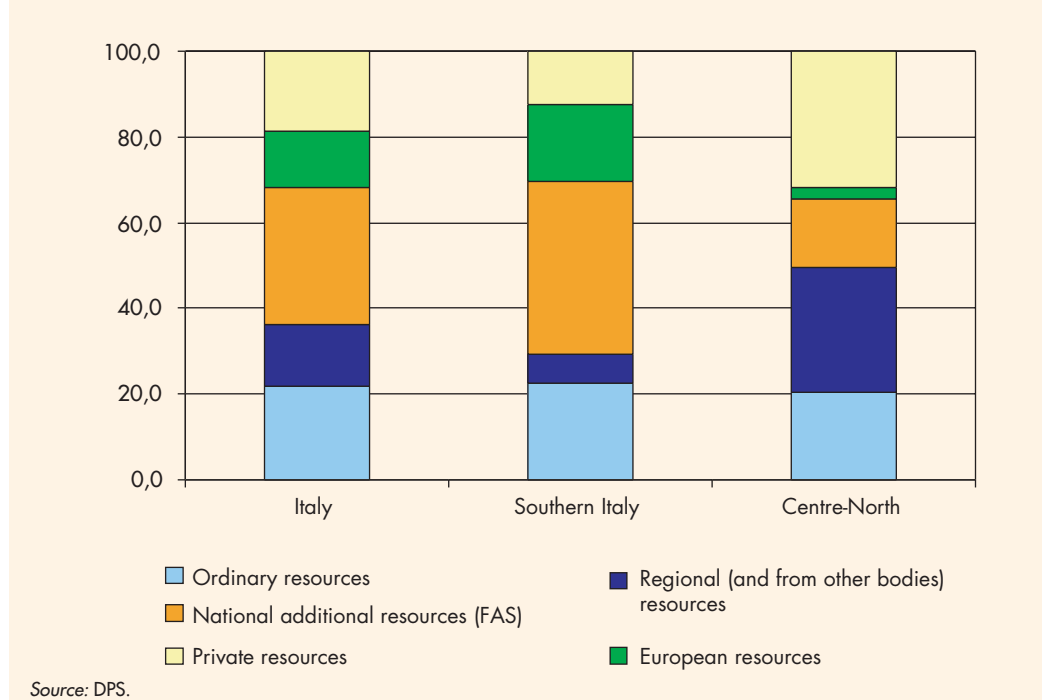
6 per cent for agreements signed in 2003, and a further increase seems to have taken place in 2004 (cf. fig. 14).

Figure 14 – FRAMEWORK PROGRAMME AGREEMENTS: SPENDING FORECASTS AND INCREASE IN IMPLEMENTATION CAPACITY



FPA are also relevant in the Centre-North, where they are worth 8.8 billion euro. The contribution of regional (29 per cent) and private (32 per cent) resources is particularly high and greater than in the South, while the contribution of additional resources deriving from national and EU regional policies and allocated for territorial rebalancing, is clearly lower, though significant (cf. fig. 15).

Figure 15 – THE ROLE OF THE VARIOUS SOURCES OF FINANCING IN THE FRAMEWORK PROGRAMME AGREEMENTS OF THE CENTRE-NORTH AND THE SOUTH OF ITALY (percentage values)



In September 2004, the allocation of more than 10 billion euro by CIPE brought about a further shift from incentives to infrastructure spending. Around 60 per cent was allocated to public investment in infrastructure, and of this more than a third was assigned to research and large national strategic projects, selected through the Evaluation and Verification Units of DPS. In particular, 1.1 billion euro was allocated to 11 large transport and water interventions under the so-called “*Legge Obiettivo*”, selected through a ranking based on expected implementation timing. A penalty mechanism for delays was introduced (cf. fig. 16).

Figure 16 – GENERAL ALLOCATION OF THE UNDER-UTILISED AREAS FUND OF SEPTEMBER 2004¹

| | million euro | allocation % |
|--|-----------------|-----------------|
| Tangible and intangible infrastructures | 6.447 | 63,7 |
| <i>National strategic infrastructure interventions:</i> | 2.424 | 23,9 |
| • acceleration of "Legge obiettivo" big infrastructures | 1.130 | 11,2 |
| • research, information society and education | 540 | 5,3 |
| • security; water, land and energy; cities; others | 754 | 7,4 |
| <i>Infrastructure interventions selected by the regions:</i> | 4.023 | 39,7 |
| • in the Southern Italy | 2.823 | 27,9 |
| • in the Centre-North ² | 880 | 8,7 |
| • management efficiency | 320 | 3,1 |
| Incentives | 3.676 | 36,3 |
| • Tax relief grants ³ | 3.376 | 33,4 |
| • Self-entrepreneurship and self-employment | 300 | 3,0 |
| Total | 10.123 | 100,0 |
| ¹ excluding appropriated funds for 2.168 million euro | | |
| ² for the research and information society, 109 million euro | | |
| ³ for investments 2.476 million euro, for employment 850 million euro, for advertising campaigns 50 million euro. | | |
| Source: DPS. | | |

Behind these results and further results to come is a decisive factor both in the South and in the rest of the country: the institutional renewal of administrations and markets. Of particular significance in 2004 were:

- the consolidation and dissemination of institutional changes achieved in the preceding period thanks to the EU performance reserve of 6 per cent, now monitored and made available to the public to enhance a “name and shame” pressure (fig. 17);

Figure 17 – STATE OF PROGRESS OF THE INSTITUTIONAL OBJECTIVES OF THE “6 PER CENT” PERFORMANCE RESERVE¹ – AS AT 31 JULY 2004

| Objectives | Basilicata | Calabria | Campania | Puglia | Sardegna | Sicilia | Fishing | Research | Education | Security | Local Development | Transports |
|--|------------|----------|----------|--------|----------|---------|---------|----------|-----------|----------|-------------------|------------|
| Regional and national programs | | | | | | | | | | | | |
| A.1 appointment of executives | X | O | X | X | | X | | | X | X | X | |
| A.2 Implementation of management inner control unit | x | | • | x | • | x | O | | x | x | x | x |
| A.3 Creation and functioning of the evaluation units | x | x | x | x | x | x | | x | x | x | x | |
| A.4 Information society in public administration | x | • | | x | | x | | | x | • | x | |
| Regional programs | | | | | | | | | | | | |
| A.5 "single office" for enterprises (by the 30.09.2002) ² | x | x | x | x | | x | | | | | | |
| A.6 Services for employment (by the 30.09.2002) ² | x | x | x | x | | x | | | | | | |
| A.7 Implementation of territorial and landscape planning | x | | x | x | | x | | | | | | |
| A.8 Integrated service | x | • | | x | | O | | | | | | |
| A.9 Implementation of urban waste disposal in "ATO" | x | • | • | O | | • | | | | | | |
| A.10 creation and effectiveness of the "ARPA" | x | • | x | • | | x | | | | | | |

| Targets achieved | |
|------------------|-------------------|
| X | by the 30.09.2002 |
| • | by the 30.09.2003 |
| O | by the 07.2004 |
| | not achieved |

¹ The table refers to the progress with respect to requirements and indicators of 6 percent performance reserve (as voluntarily updated by the regions) and does not include possible progress achieved regarding further information. A selection of them is in table V.2 of the Report.

² The survey of the information for these two indicators is conducted by the Public Administration Ministry – Formez and by the Ministry of Labour – Isfol. The updated information will be available by February 2005

Source: DPS processing.

- the adoption of performance-rewarding mechanisms by individual Regions for their own local authorities, as proof of the dissemination of a methodology which was, until recently, unknown in Italy’s administrative system;

- the launch by the DPS of a “Programme for knowledge transfer”, which, as in the case of EU cohesion policy, assists Regions and Central administrations in the implementation of national regional policy, with monitoring, production of statistics, analysis, training, evaluation, verification of critical points, and implementation of pilot local development and bilateral cooperation projects.

Coming to State aid, in 2004, the reform process continued, addressing three distinct objectives: to compensate for the higher unit costs of disadvantaged areas of the country; to correct capital market failures, particularly strong in disadvantaged areas and for investments in research and innovation; to support the attraction of investment and the development of local business incentives to be negotiated, case by case, between the State and private firms

(cf. fig. 18). In particular, the transformation of capital grants into interest-relief grants (increasing banks' responsibility) is being extended to all incentives. This process should be sustained by the creation -under the 2005 Budget Law- of a rolling fund.

Figure 18 – REFORM OF THE SYSTEM OF INCENTIVES FINANCED BY THE UNDER-UTILISED AREAS FUND¹

| Category | Incentive | State of the reform implementation | Available resources at the end of 2004 ² | |
|---|--|---------------------------------------|---|--------------|
| | | | million euro | share % |
| Automatic, to compensate for costs | - investment tax relief grants | | 4.889 | 23,1 |
| | - employment tax relief grants | reformed | 2.470 | 11,7 |
| | - advertising campaigns | | 130 | 0,6 |
| By announcement, to correct capital failures ³ | - entrepreneurship and self-employment | reformed | 1.765 | 8,4 |
| | - 488/92 Law | being reformed | 6.243 | 29,5 |
| | - territorial pacts | reformed being /reformed ⁴ | 2.945 | 13,9 |
| By negotiation, to integrate | - area agreements | being reformed | 578 | 2,7 |
| | - program agreements | | 1.911 | 9,0 |
| infrastructure action | - agroindustrial agreements | pilot projects being | 100 | 0,5 |
| | - location agreements | reformed ⁴ | 100 | 0,5 |
| Total incentives | | | 21.131 | 100,0 |

¹ Further resources will be come available at disposal through the rolling fund introduced by the Budget Law 2005, which completes the incentives reform.

² They do not include funds already paid by the end of 2003.

³ Interventions for research financed by the 208/98 Law has to be added.

⁴ By the 488/92 Law.

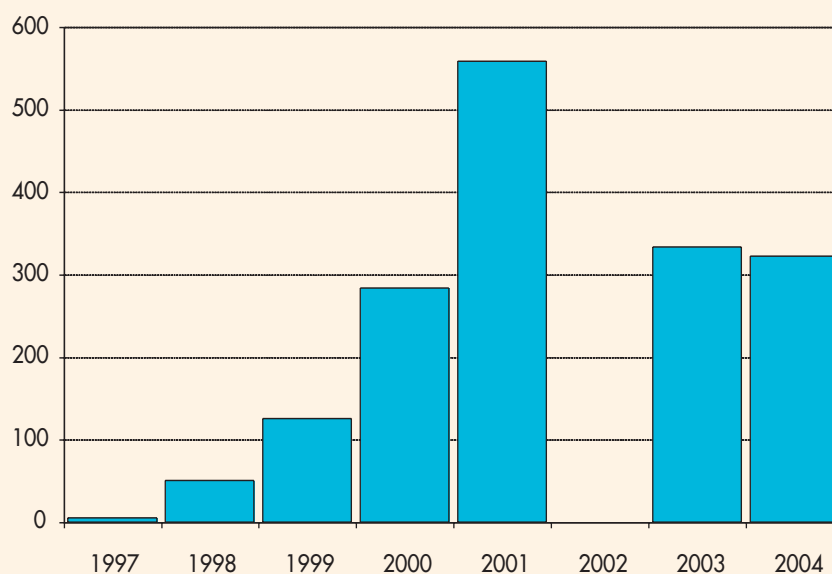
Source: DPS.

A strategy to attract foreign investment was finally developed in 2004 by Sviluppo Italia and a new tool, called “localisation contract”, was experimented with the settlement of some initial contracts. In order to ensure that 2005 constitutes the “take-off” year for this initiative, a new simplified incentive tool was approved in the 2005 Budget Law.

Incentives to promote self-employment as well as micro-enterprises and franchising were continued. The strong role played by the loans makes it a more suitable tool than others to promote, not substitute, credit relationships between banks and business initiatives. Effectiveness in supplying financial means to parties who already have work experience, makes it a tool capable of encouraging the

emergence of irregular labour into regular labour. After its suspension in 2002, this tool was re-launched with new criteria (figure 19).

Figure 19 – FUNDS GRANTED FOR THE PROMOTION OF SELF-EMPLOYMENT¹
(million euro)



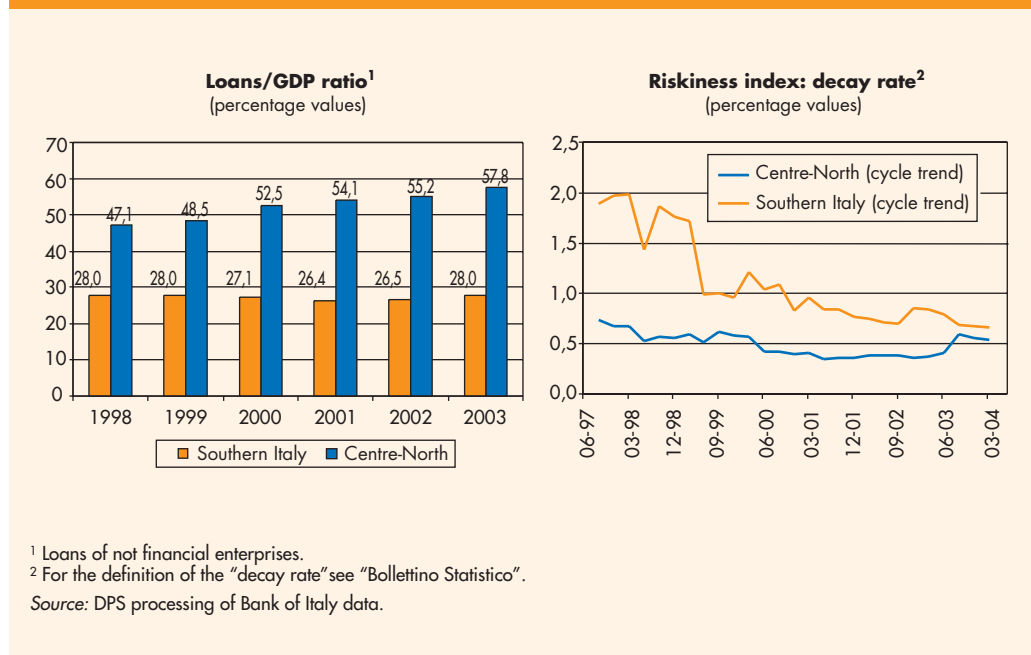
Source: DPS processing of Sviluppo Italia data.

The completion of the incentives reform is also called-for by some positive initial signs which come from the banking-business relationship.

In the second half of the 1990s and at the beginning of the current decade, the available indicators showed that the credit system, despite a deep reform (which reduced, especially in the South, the number of banks, and increased the number of counters as well as profitability) was not contributing to the new phase of development in the South. The ratio of loans to GDP actually fell (from 28 per cent in 1998 to around 26.5 per cent in 2001 and 2002), becoming less than half of that of the Centre-North; the interest rate differential remained high, even when adjusted for the different sectoral composition of the two macro-areas (about 1 point per cent). But in the most recent period, quantitative and qualitative signs seem to indicate that the reform of the credit system could finally bear fruit even in the South. A more active credit policy seems to characterise both the branches of institutions incorporated by large banks of the Centre-North, as well as smaller-sized credit agencies. Moreover, the loans/GDP ratio rose in 2003, returning to the level of 1998; and at the beginning of 2004, the risk factor of credit users fell in the South to reach the

levels of the Centre-North (cf. fig. 20), even if this has not yet been reflected in the interest rate gap.

Figure 20 – CREDIT AND THE SOUTH OF ITALY



The conditions could be ripe for a new banking-business relationship in the South of Italy. Whether this opportunity is taken depends on a number of factors: the capacity of the public sector to complete the reform of current incentives, the commitment of businesses to soliciting the banking system and individual banks, the commitment of banks to investing in new sources of profit in the South. These factors might all have a rather relevant role in allowing the growth rate of the South to actually overcome the European growth rate.

