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We are told that History is always written twice; this was certainly the case of the creation of the Eurozone. Not many years ago, Italy's entry into the monetary Union was exalted as a success, finally allowing our Country to enjoy financial stability. Many held the view that the Italian manufacturing industry might not be able to compete in the global market, once deprived of the weapon of competitive devaluations. But their concern was met by the counter-argument that the *external constraint* generated by the single currency would force Italy's political class to adopt those structural reforms Italy had long waited for: by mitigating the fiscal and bureaucratic burden, enhancing flexibility in labour market rules and removing bottlenecks in the domestic market, the Government would allow exporting enterprises to increase their size and compete successfully at the technology frontier. It is somewhat frustrating and at the same time extremely helpful to read from Prof. Moretti's interview that 15 years later, the Agenda is still there, and still to be implemented. In the meantime, those pessimistic prophecies came true. Italy turned out to be a loser in the large-scale process of concentration of capitals, and today it appears to be a marginalised and impoverished country, unable to attract productive investments as well as to give a future to its most talented youth. There is no wonder then, that the view that the monetary Union was among the main reasons for the Italian decline had such a vast success, and that the Euro itself is now seen by many as Germany's Trojan Horse to flood the single market with its products. Prof. Moretti promptly rejects this subtly self-indulgent narrative: Italy's decline is Italy's fault. The forces of globalisation and technological change are structural, long-term factors operating globally, and describing them as the outcome of deliberate economic policy choices is simply misleading. But this does not mean that declining wealth and increasing inequality is the fate of industrialised countries. The success of decline of an area depend on how well it attracts investments in innovative sectors. Creating high value added jobs means not only to pay high salaries to high-skilled workers, but also to create the conditions for even more new jobs and higher salaries for professionals, as well as for low-skilled workers employed in local services. In the end, it is not individual categories who benefit or suffer from economic change, but entire communities. Italy had the potential to take up this challenge: its current status as a peripheral Eurozone Country stems from no conspiracy, but from the short-sightedness of our entrepreneurs, who were unable to innovate the traditional structure of their family-run businesses, in order to cope with the costs of innovation, as well as from the failure of our political class to shape an appropriate institutional framework for economic change. We have failed to respond to this challenge so far: but we cannot blame anyone but ourselves.

Mariella Palazzolo

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MORETTI

HUMAN CAPITAL IS A COMPASS:
LOOK FOR INNOVATION AND YOU WILL FIND WEALTH

> *"Economic growth in innovation hubs benefitted all workers, including low-skilled ones, with high employment rates and high salaries."*

Telos: The polarisation of incomes and wealth is a topical issue. In your book, "*The new geography of jobs*", you described the increasing divergence among geographical areas taken as a whole, beyond that among workers with different skill levels. Could you please outline the outcome of your research?

Enrico Moretti: When we take into account the most significant changes in the U.S. labour market over the last 30 years, 2 long-period trends emerge. The first one is a relative increase in the demand for high-skilled workers, compared to that for low-skilled workers. This trend stems both from technological progress and from the globalisation of the markets of goods and services. The second trend reproduces the first one at a regional and local level: areas with more high-skilled workers have enjoyed higher growth rates, and have attracted more innovative enterprises, producing goods and services that are not reproducible at lower costs in China or Poland. But there's more: once an area attracts innovative enterprises and high-skilled workers, more innovative enterprises can be expected to cluster in that area in the future as well. This means that the diverging economic trends of those areas that attract investments in innovative sectors and of those that do not are self-reinforcing. My book describes how this process has unfolded in the U.S. over the last 30 years. The U.S. are generally thought of as a single labour market, but it actually includes at least 300 different labour markets, one per each metropolitan area. Over the last decades, some traditionally developed areas such as San Francisco, Boston, Washington D.C., New York have successfully specialised as innovation hubs, and new areas emerged such as Seattle, Austin, Raleigh-Durham. The impact of technological change and globalisation on these areas was a positive one, resulting in a highly innovative industrial environment, high *per capita* patent rates, high salaries, continuous improvement in life quality indicators. By contrast, areas once wealthy such as Cleveland, Detroit, Philadelphia, remained stuck to traditional manufacturing productions, thus being badly damaged by the very same economic forces that benefitted the best-performing areas: the result was a combination of relatively low-skilled jobs, declining salaries, declining population. But here is the most interesting part of the story. The vast majority of American (and European) workers will never work in Google, Apple or a biotech corporation. Even in the Sylicon Valley, most of the labour force is employed in services: salespersons, waiters, taxi drivers, lawyers, architects, doctors. All these workers do not compete in the global market: they produce services that are sold in the local market. Since the demand for these services is a function of the local wealth, the areas that were successful as innovation hubs generate enough wealth to pay high salaries in the services as well. It must be stressed that each new job in highly innovative sectors stimulates the creation of 5 new jobs in local services. Hence, the conclusion can be drawn that economic growth in innovation hubs

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benefitted all workers, including low-skilled ones, with high employment rates and high salaries. New jobs for low-skilled workers can therefore be created by attracting high-skilled workers, and benefitting from the multiplier effect.

Are peripheral Eurozone Member States, including Italy, on an irreversible path leading to industrial desertification and impoverishment? Do they resemble the worst-performing U.S. areas you described in your book?

Unfortunately, they do. Of course every country has its historical, institutional and cultural peculiarities, but the economic forces that are reshaping the job market in the U.S. are the same that are operating in Europe, the only difference being that Europe is approx. 20 years behind in the unfolding of this process. The main problem with the structure of the industrial environment in Italy is the poor development of highly innovative sectors: for this reason, economic change is damaging Italy, like it is damaging Detroit and Cleveland. Italy's industrial environment is traditionally made up of family-run small enterprises, with very little potential to innovate, precisely because they are too small to afford such a fixed cost as that of investing in innovation. Let us take the example of pharmaceutical industry, which I talk about in the Italian version of my book. In the Seventies and Eighties, Italy had a dynamic pharmaceutical sector, that was successful in creating patents and competing in the global market, employing thousands of workers both directly and through the multiplier effect. The concentration process that took place in the Nineties led many Italian companies to be acquired by multinational corporations, and many laboratories to be closed down and delocalised. Today, Italy does not attract investments in pharmaceutical innovation any longer, jobs have declined and, since this is a self-reinforcing trend, it is fair to predict that they won't come back.

Well-respected scholars such as Paul Krugman advanced the hypothesis that the polarisation of incomes over the last decades reflects the consequences of a shift in economic policy choices rather than the impact of skill-biased technological change. To what extend was this process determined by purely political factors in your view?

Krugman was one of the most influent economists in the '80s and '90s; he certainly deserved the Nobel Prize for his academic work. However, more recently his contributions have based more on ideological assumptions than on the available historic evidence. There is very little evidence that the increase in inequality is linked to deliberate economic policy choices. Inequality in the U.S. increased both in Blue States such as New York and California and in Red States such as Texas. It increased in sectors with a highly unionised workforce and in others with a lowly unionised workforce. It increased in Sweden as well as in the U.S. Above all, increased inequality can be observed in pre-tax wages. I wish inequality could be explained with explicit political choices: should that be the case, the problem could be solved simply by electing a different Administration. But those we are observing are long-period trends, reflecting a structural change in the way we produce goods and services, as well as in the geographical areas production tends to cluster.

In Italy, we have been long debating on how to promote an increase in productivity of labour. Localising settlements and granting tax incentives to productivity gains is the solution envisaged by the Government in the last years. Is this a credible solution in your view?

It is a first step, praiseworthy but not decisive: it is much more than a palliative treatment, but much less than a structural change able to generate a virtuous process *per se*. No reform can change the *status quo* in the short run: since we are dealing with long-term trends, any reform can only produce an improvement in the labour market in a timeframe of at least 5-10 years. The objective of any reform should be that of stimulating the creation of jobs, producing goods and services that are not reproducible at lower costs: to achieve this aim, it is necessary to foster investment in high value added sectors. Reforms in Italy should focus on 3 fields. One: removing the fiscal and bureaucratic hurdles, discouraging small and medium enterprises from increasing their size. Two: addressing the dualistic structure of the labour market, allowing companies to hire workers whenever they need to, without being concerned that they may not be in the capacity to dismiss them in the future. Three: promote competition in domestic markets of goods and services, by tackling rent-seeking resistance from professional categories. This would greatly benefit both consumers and those enterprises that compete in the global market.

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