

CONVERGENCE IN ITALY BETWEEN THE SOUTH AND THE CENTRE-NORTH: AFTER THE EURO
(YEARS 2002-2013)

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ABSTRACT

On the one hand, in favour of the EMU, there were those who, inspired by the neoclassical model, argued that through the European Community's economic and social cohesion policy it would be possible to eliminate not only so-called external diseconomies (lack of infrastructures, presence of crime, lack of human capital etc.), but also all those institutional frictions affecting the flexibility and mobility of factors, thereby allowing market forces to balance the per capita income across regions. On the other hand, against the EMU, we found Keynesian scholars, who, referring to the theory of circular cumulative causation, believed that neoclassical economic policy choices would only have accentuated the dualist system of weak and strong regions. The aim of this essay is precisely that of attempting to make an ex-post assessment of the effects of the single currency on the economy of the South of Italy. The period considered are the years 2002- 2013. The originality of the paper, compared to previous works is that also considers the years of the recent crisis.

1. Introduction

The debate on the costs and benefits of the single currency fuelled the interest of scholars in the nineties. The predictions on the effects of the single currency were based, above all, on two different interpretive approaches: neoclassical and Keynesian. Neoclassical scholars maintained that the establishment of the EMU may not have worked in cases where productive factors were immobile, seeing as the well-known conditions laid down by Mundell (1961) for an *optimum currency area* would not be realised. Also within the neoclassical framework, however, the beneficial effects of monetary union envisaged prior to the implementation of the EMU could be summarized in the following three points: 1) *efficiency*, 2) *stability*, 3) *regional equity*.

In reference to point 1), it was emphasized that with the use of a single currency, the market would be more transparent and subject to greater competition, and this would allow a better allocation of resources, which

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would be transferred from the less efficient subjects (firms producing at high prices) to the more efficient (companies which were most innovative, organized, etc.). The shift of resources would increase the efficiency of the whole system, due to the disappearance of: *a*) transaction costs; *b*) the variability of the exchange rate, thus eliminating the costs of forward currency hedges, and fostering trade flows and foreign direct investment (these were indirect effects of the Single Currency) *c*) the producers' monopoly power, ensuring greater price transparency in the EMU.

In consideration of point 2), it was argued that with the introduction of the Euro countries would achieve greater economic stability resulting from having met the Maastricht criteria and from the greater coordination of economic policies that the Stability and Growth Pact required. Macroeconomic stability is in fact determined by low inflation and lower interest rates, factors that facilitate continued and long lasting growth .

Lastly, in reference to point 3), it was assumed that the single currency not only allowed the elimination of the exchange rate as an economic adjustment mechanism to deal with asymmetric shocks between regions, encouraging factor mobility and the flexibility of the relative prices, but also allowed companies to operate the same way in any region or territory of the Community.

A different view was adopted by theorists influenced by the theory of circular cumulative causation. They stressed, in particular, the inadequacy of the neoclassical model in explaining regional development, since the market by its nature would tend to increase the imbalance between rich and poor regions. Dualism was therefore an endogenous phenomenon, the result of structural change (Carillo et. al. 2008). According to this view, technological innovation in the strong area can initiate the process of structural change which in turn leads to further advancement of technology, while in the weak area, on the contrary, the result is a vicious circle of underdevelopment in which duality becomes an endogenous phenomenon, whose persistence and reinforcement is caused by the initial level of dualism itself. This scenario assumes, in fact, that both capital and labour go in the same direction (contrary to the forecasts of neoclassical theorists). The banking system itself, in this context, often plays a perverse role on the mobility of capital. Rather than injecting capital into the less developed regions, it tends to drain the savings of these regions and distribute them in those where the expectations of returns on capital are higher. Additional cumulative effects to the benefit of the more developed regions, which then tend to increase disparities rather than reduce them, are produced due to the joint effect of the accelerator and multiplier mechanisms. It should also be emphasized, for the sake of completeness, that not all lines of study based on increasing scale efficiencies exclude the possibility of creating a process of convergence between areas with uneven initial development without government intervention. Krugman's model (1993), for example, explains how two regions with different characteristics may have very similar paths of development due to the action of endogenous forces such as advantages in production costs, reductions in transport costs and changing expectations.

This analysis shows that the South of Italy, with the exclusion of Abruzzo, in the years the unification process began, has converged towards the North in terms of wealth per capita up to 2009. After 2009 there is only divergence.

The paper is organised as follows. Section 2 presents a "balance sheet", examining the impact of the single currency on the economy of the South. The section 3 provides an overview of some studies that have investigated the causes of the divergence between North Central and Southern Italy, after the recent economic crisis. The last, Section 4, draws some conclusions.

2. The single currency: a balance sheet for the economy of the South

This section, as previously mentioned, attempts to draw up a balance sheet on the possible effects of economic developments in the South compared to those in the Centre-North, in the years since the introduction of the single currency.

Following Daniele and Malanima (2007), the index of convergence, I , is thus calculated:

$$(1) \quad I = \frac{GDP_r}{GDP_{C-N}}$$

Where $GDPr$ is *Per capita GDP* of region considered (Southern Italy or Abruzzo or Molise or Campania or Puglia or Basilicata or Calabria or Sicily or Sardinia) and $GDPC-N$ is *Per capita GDP* of Central-Northern Italy.

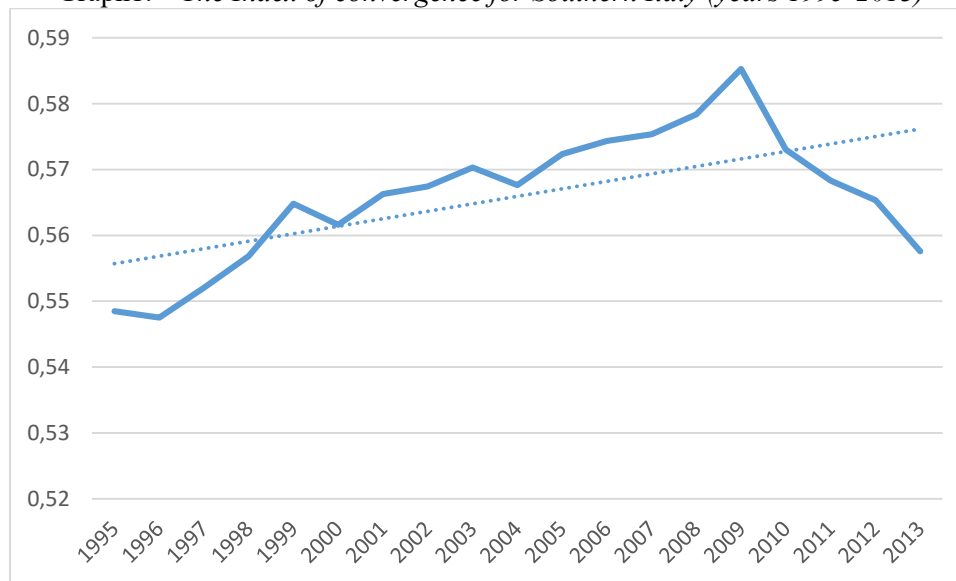
Table 1 *The Index of convergence for the regions of Southern Italy (years 1995-2013)*

Years	Southern Italy	Abruzzo	Molise	Campania	Puglia	Basilicata	Calabria	Sicily	Sardinia
1995	0,5485	0,7149	0,6090	0,5217	0,5487	0,5294	0,4926	0,5375	0,6132
1996	0,5475	0,7169	0,6174	0,5174	0,5463	0,5341	0,4995	0,5369	0,6096
1997	0,5521	0,7195	0,6278	0,5245	0,5469	0,5493	0,5057	0,5365	0,6245
1998	0,5568	0,7090	0,6415	0,5308	0,5573	0,5704	0,5118	0,5364	0,6271
1999	0,5648	0,7175	0,6398	0,5346	0,5758	0,5952	0,5324	0,5362	0,6285
2000	0,5616	0,7242	0,6394	0,5355	0,5723	0,5817	0,5212	0,5311	0,6221
2001	0,5663	0,7257	0,6424	0,5407	0,5697	0,5776	0,5297	0,5426	0,6229
2002	0,5674	0,7185	0,6462	0,5503	0,5662	0,5743	0,5268	0,5439	0,6173
2003	0,5703	0,7108	0,6422	0,5512	0,5662	0,5722	0,5397	0,5467	0,6328
2004	0,5676	0,6891	0,6484	0,5467	0,5673	0,5778	0,5474	0,5411	0,6332
2005	0,5723	0,6990	0,6549	0,5480	0,5666	0,5736	0,5378	0,5592	0,6371
2006	0,5743	0,7032	0,6661	0,5494	0,5706	0,5855	0,5415	0,5583	0,6348
2007	0,5754	0,7077	0,6706	0,5529	0,5687	0,5907	0,5422	0,5568	0,6375
2008	0,5783	0,7181	0,6575	0,5554	0,5724	0,5953	0,5424	0,5566	0,6492
2009	0,5853	0,7137	0,6664	0,5594	0,5776	0,6033	0,5536	0,5680	0,6593
2010	0,5730	0,7107	0,6468	0,5417	0,5695	0,5832	0,5451	0,5566	0,6456
2011	0,5683	0,7207	0,6330	0,5346	0,5671	0,5900	0,5390	0,5474	0,6446
2012	0,5654	0,7185	0,6400	0,5378	0,5658	0,5850	0,5423	0,5356	0,6335
2013	0,5576	0,7184	0,6335	0,5379	0,5460	0,5635	0,5271	0,5332	0,6173

Source: *Our processing of ISTAT*

In *Graph 1* we can see that there is a weak process of convergence between the gross domestic product per capita between the South and the Centre-North for the period 1995-2009. After 2009 (up to 2013), a slow process of divergence leaves again.

Graph1. *The Index of convergence for Southern Italy (years 1995-2013)*



Source: *Our processing of ISTAT data*

In the light of these results, considering recent literature on the issue, we will attempt to identify the reasons that led to this phase of convergence between the Centre-North and South following the advent of the Euro up to 2009. In the next section, we will identify the causes of the divergence between North Central and Southern Italy after 2009. The causes of convergence can be ascribed to the following two reasons: 1) different population dynamics, which were more intense in the Centre-North because of migration (Cannari *et. al.* 2009, 2) the concentration of comparative advantages in sectors characterized by strong economies of scale (Prezioso, 2009).

The first reason is explained (see: Centorrino *et. al.*, 2010) by the effect of the demographic component: the GDP of the South, although not particularly dynamic, is distributed over a population with a lower growth rate than that of the Centre-North, resulting in a relatively high per capita GDP. A cause of this low population growth is the significant amount of people moving from the South to more dynamic central and northern areas (Lombardy, Emilia-Romagna and Lazio). Though this process of population transfer could have well-known negative connotations (see: Draghi, 2009), it is fully accounted for by the neoclassical supporters of the single currency, who maintain that a Mundell-model optimum currency area is created when migration processes involving production factors take place between the regions in the area under consideration.

The second reason, the comparative advantage for firms belonging to sectors with strong economies of scale (see: table 2), even if “exposed to changes in strategy from decision-making centres outside the South” (Prezioso, 2009, p. 115), shows the evolution of Southern industry towards greater integration in international markets. This condition has always been considered necessary to trigger off a significant process of convergence between the regions of the South and Centre-North. As is known, literature concerned with the causes of differences in productivity between the South and the Centre-North (for review, Ofria and Farinella, 2011) has found precisely in the sectors of tradable goods: 1) that companies in the sector are more resistant to external local diseconomies (crime, cost of credit, lack of infrastructures); 2) that this sector is sensitive to a high productivity growth rate, according to the well-known “Kaldor-Verdoorn” model (Ofria, 2009).

It is highlighted that after 2009 sectors with strong economies of scale in Southern Italy have lost weight regarding the Center-North (Tab2), compensated partially by an increasing percentage of the Technology-intensive sectors. Percentage changes are also based on the monetary value of exports. Tab.2 shows how monetary value of the exports in the Sectors with strong economies of scales is reduced, from the 23169009.71 euros of 2008 to the 20050825,15 euros of 2013. Exports also fell in other sectors, with the exception of Technology- intensive sectors, where a significant increase can be observed: from 4033323.691 euros of 2008 to 4656530,947 euros of 2013.

In addition, both the Centre-North and the South (tab.2f) increase exports in Technology-intensive sectors and Traditional sectors (which identify Made in Italy businesses), decrease in Specialist Sectors, while Sectors with strong economies of scale substantially remained unchanged.

Table 2a *Percentage share of exports by macro-branches, Pavitt's model*

Macro-Branches	Southern Italy					
	2008	2009	2010	2011	2012	2013
Traditional sectors	23,9033	28,8905	25,4918	23,7572	22,1884	24,9457
Sectors with strong economies of scale	57,3043	49,0305	54,7837	56,2422	58,1205	54,5081
Specialist Sectors	8,8167	9,5841	8,1860	8,5828	8,2074	7,8875
Technology-intensive sectors	9,9757	12,4949	11,5384	11,4178	11,4838	12,6588
Total Pavitt (manufacturing)	100.00	100.00	100.00	100.00	100.00	100.00

Source: Istat

Table 2b *Percentage share of exports by macro-branches, Pavitt's model*

Macro-Branches	North East Italy					
	2008	2009	2010	2011	2012	2013
Traditional sectors	36,8423	39,4881	37,8162	36,9622	37,9245	38,6189
Sectors with strong economies of scale	27,0281	25,5920	27,2409	27,7911	28,1566	27,4668
Specialist Sectors	33,0746	31,2374	31,3681	31,9553	30,5340	30,5511
Technology-intensive sectors	3,0550	3,6824	3,5748	3,2915	3,3849	3,3633
Total Pavitt (manufacturing)	100.00	100.00	100.00	100.00	100.00	100.00

Source: Istat

Table 2c *Percentage share of exports by macro-branches, Pavitt's model*

Macro-Branches	North West Italy					
	2008	2009	2010	2011	2012	2013
Traditional sectors	25,6421	26,0686	25,8047	25,8567	25,6711	26,2993
Sectors with strong economies of scale	38,6475	35,8014	37,9500	38,3811	38,7289	38,4703
Specialist Sectors	27,3459	28,0262	26,0818	25,9118	25,8896	25,5404
Technology-intensive sectors	8,3645	10,1039	10,1634	9,8503	9,7104	9,6899
Total Pavitt (manufacturing)	100.00	100.00	100.00	100.00	100.00	100.00

Source: Istat

Table 2d *Percentage share of exports by macro-branches, Pavitt's model*

Macro-Branches	Centre Italy					
	2008	2009	2010	2011	2012	2013
Traditional sectors	38,0499	36,0321	35,2131	34,8127	34,2819	36,6322
Sectors with strong economies of scale	28,9045	28,5256	31,5254	33,9147	33,2239	26,5860
Specialist Sectors	19,5015	20,6701	18,4568	16,5724	16,1759	17,1965
Technology-intensive sectors	14,7722	14,8047	14,7002	16,3183	19,5853	14,7722
Total Pavitt (manufacturing)	100.00	100.00	100.00	100.00	100.00	100.00

Source: Istat

Table 2e *Exports by macro-branches, Pavitt's model and annual percentage change*

Macro-Branches	Southern Italy					
	2008	2009	2010	2011	2012	2013
Traditional sectors	9664474,553	8104714,449	8995614,403	9153285,057	9079453,582	9176294,365
<i>percentage change</i>		-16,14	10,99	1,75	-0,81	1,07
Sectors with strong economies of scale	23169009,71	13754601,99	19332182,25	21669263,82	23782835,63	20050825,15
<i>percentage change</i>		-40,63	40,55	12,09	9,75	-15,69
Specialist Sectors	3564707,196	2688648,43	2888708,361	3306826,744	3358447,669	2901413,408
<i>percentage change</i>		-24,58	7,44	14,47	1,56	-13,61
Technology-intensive sectors	4033323,691	3505212,09	4071708,829	4399083,729	4699143,914	4656530,947
<i>percentage change</i>		-13,09	16,16	8,04	6,82	-0,91

Our processing of ISTAT data

Table 2f *Exports by macro-branches, Pavitt's model and annual percentage change*

Macro-Branches	Centre-North Italy					
	2008	2009	2010	2011	2012	2013
Traditional sectors	95245919,44	76603591,61	85900939,24	93555363,75	95496439,66	98145489,36
<i>percentage change</i>		-19,57	12,14	8,91	2,07	2,77
Sectors with strong economies of scale	97911883,2	72333334,78	88854506,17	100308046,2	102612215,6	97269801,51
<i>percentage change</i>		-26,12	22,84	12,89	2,30	-5,21
Specialist Sectors	84111611,66	65354936,16	71756087,83	78287077,59	77542461,07	77513356,09
		-22,30	9,79	9,10	-0,95	-0,04
Technology-intensive sectors	21803281,46	20249775,02	23313208,96	21445735,71	26427526,61	27952547,93
<i>percentage change</i>		-7,13	15,13	-8,01	23,23	5,77

Our processing of ISTAT data

3. Causes of the divergence between North Central and Southern Italy after the recent economic crisis

De Grauwe (1996, p. 41) criticized the inflexibility of the convergence criteria of the Maastricht Treaty on 3% budget deficit and 60% public debt, inflation, exchange rates and long-terms interests. For him the Maastricht Treat convergence criteria were imposed by Germany as a warranty and an expression of power, but they weren't really necessary, and create “a great risk of splitting the European Union”: “the Maastricht strategy leads to a divided Europe”. Piacentini and Precious (2007) stressed that in Italy the transition to the regime of Maastricht has caused a reduction in aggregate demand, among other things, because it reduced the value of the Keynesian multiplier following a redistribution of income to the detriment of the categories with a higher propensity to consume (employees). A recent study (Piacentini et.al., 2015, pp 12-13) put in evidence the effects across the North and the South of the Italy of the recent fiscal policies:

Two main results arise from this empirical exercise: 1) "Fiscal tightening does not hit equally regions across Italy. A rise in taxes inflicts more damage in the South than in the North. This is mainly so because of the regressive nature of consumption taxes, which make up about 80% of the overall tax increases (direct plus indirect taxes). Indeed, the South presents values of a consumption propensity higher than the North, and will suffer more from higher taxation on incomes and on essential consumption. 2) Even when considering the country as a whole, a general picture arises, of a country badly suffering government investment cuts. From our evidence, a cut in government investment expenditure is the item which has the most dramatic, negative impact on the economy. This is also because of the static or declining trends of private investment in Italy in the recent period. Advancing, as conclusion, a policy proposal consequent to these findings, the application of the so-called "Golden rule", according to which public investments should be, wholly or partially, excluded from restriction rules on governments deficit, such as the 3% limit, might be an indication for a re-orientation of new fiscal policy rules less penalizing for the economy.

Since 2008 Italian economy has undergone a serious crisis that has been even stronger in the southern areas. There have been discourses about the persistence of dualism, accompanied by a general decline of the economy (Destefanis 2014). This has reignited debate on the lack of convergence between North Center and South of Italy following the recent economic crisis. Cappellin et. al. (2014; 2015) proposes policies of investment in innovative sectors with high knowledge, so to promote economic development in the long run. Marelli (2014; 2015), referring to De Greuwe (1996), shows that one of the main problems of the European Union were the Maastricht criteria, the Stability and Growth Pact and the Fiscal Compact. Little attention has been given to the process of real convergence of economies, to increase the competitiveness of lagging areas. Structural Funds and cohesion policies have proved inadequate in pursuing this goal. Marelli and Signorelli (2014) show that before the crisis there was a certain degree of real convergence only for some macro variables. But after the crisis divergence can be observed. Even before the crisis, the average growth was lower than the European average both in emerging countries and USA. Only new member states of Central and Eastern Europe, who are building the catching-up, showed growth rates higher, in addition some countries like Spain and Ireland, where growth has been "drugged" by speculation. Cappellin (2015) and Marelli (2015) argue that the economic crisis was due to the reduction of the aggregate demand for the rules of the stability pact and the fiscal compact. The monetary policies of the ECB cannot restore growth because they focus on monetary stability, and the policies of "structural reforms" have a deflationary impact on aggregate demand and do not increase labor productivity.

The role of technological innovation has been underestimated for aggregate demand and growth. Investments should focus on innovative sectors that could open new market segments and new needs, but also enhance the so-called territorial "capabilities" (Garofalo 2015): resources present in the area, tacit knowledge, skills, networks territorial and competitive local collective goods. Destefanis (2014) considers the enhancement of job skills crucial. Italy, in fact, is characterized by an unbalanced growth of labor skills. Additional tools to increase investment at European level, without changing the commitments with respect to the stability pact and growth are identified by Garofalo (2015, p. 114) in direct funding of projects by the EIB (European Investment Bank) that could be financed by issuing bonds.

Another strand of literature focuses instead on a historical and institutional long-term approach. According to Malanina and Daniele (2007) the gap between North and South has been caused by the effect the policies adopted after the unification of Italy. Even if the South compared to the North, it had low social indicators (literacy, life expectancy, handling of bureaucracy, the distribution of wealth) and infrastructure (Felice, 2013; 2015). The gap increased from the second half of the nineteenth century (1880) until 1951. The development policy for the South made by a State Agency (The "Cassa per il Mezzogiorno") and the economic boom will cause convergence until the 70s. From the early 70s onwards a progressive reduction of the rate of convergence began. From the 90s onwards, with the end of the 'extraordinary intervention' it is preferred that each territory has its own development projects. (Viesti 2011), strengthening the intangible factors and material resources it possesses, so to improve its institutional capacity. (Trigilia 2012; 2011; 2006; Viesti 2003; 2009 In particular, Scarlato (2011); Ciccarelli and Fachin, 2014, Felice (2015); Albanese & De Blasio (2014), attribute the persistence of the Italian dualism to the lack of so-called intangible factors of development: social capital, capacity to create networks, trust, civicness and institutional capital, human capital, tacit knowledge, skills.

4. Conclusions

The paper showed that the weak economic convergence process that affecting the South of Italian from 1999 to 2008 stopped in recent years in a situation of generalised recession of Italian economy. It is considered after the review of the literature that analyzes the causes of the persistence of the gap between the Centre-North and South.

Neo-Keynesians scholars attribute negative role to the austerity policies of the European Union in recent years. These policies have caused only recession and countries with dualist economies like Italy, faced a resumption of the gaps between the Centre-North and the South. They propose structural policies to boost investment in urban areas especially in areas with high knowledge and innovation.

In addition to these strategies, it is necessary to consider the strategic role of the rural areas and the multifunctional agriculture in the innovation. The agri-food chain is one of the few sectors that has been growing despite crisis and demonstrates a big capacity to innovate (Meloni e Farinella 2013); rural areas are now able to offer new complementarities with urban areas, providing public goods and services with high value (blue economy and green economy).

The neo-institutional approach pays a lot of attention on the role of the socio-institutional factors (as social capital, civiness, trust) for the local development, but sometime it becomes excessively culturalist and determinist in the analysis: the "South" risks to remain prisoner of his "cognitive traps."

We need to think new public policies to support the social innovation and green economy. The "Europe 2020" strategy, as it is known, makes "supportive growth" as a priority objective to foster economic, social and territorial cohesion. In that context "social inclusion" plays a strategic role; social inclusion is defined as "the access of all citizens to basic resources, social services, labor market and all necessary rights to fully participate in the economic, social and cultural life and to enjoy a standard of living and well-being considered normal in the society in which they live". On the subject, the 2014 Partnership Agreement (Ministry of Territorial Cohesion, 2014) stresses the need for Italy to promote a significant antipoverty strategy, in line with what has happened in other major European countries. This strategy should take into account the following three pillars of active inclusion: 1) economic support; 2) support for workforce development and job placement; 3) support of social services quality. It is a commitment that Italy took in Europe; so it is important to start developing it and to deploy it at regional level through an experimental and innovative process, which is based on the European "Structural Funds". In this respect, the promotion of social inclusion is of particular relevance, especially in less developed regions, where it is a key component of the effort to establish a full citizenship for the weakest subjects."

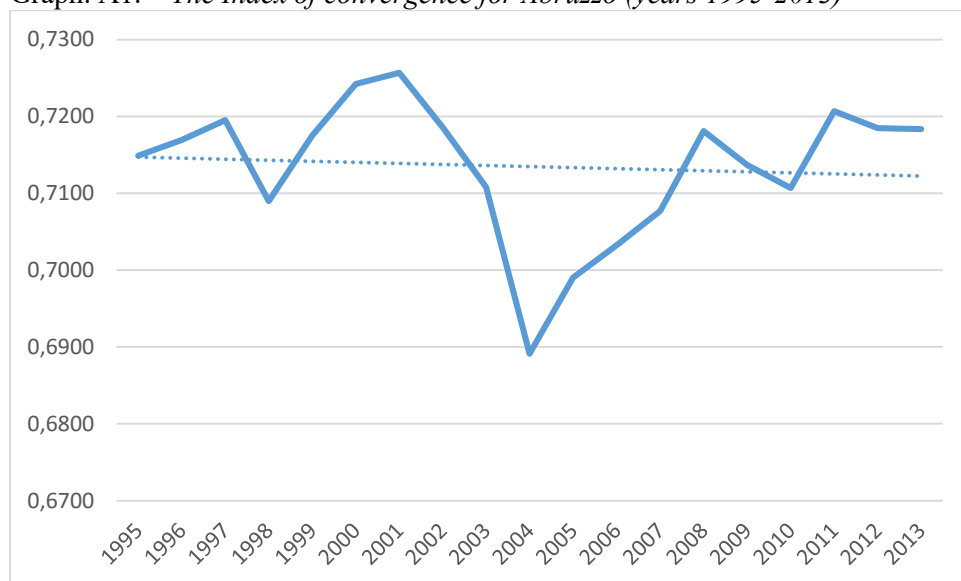
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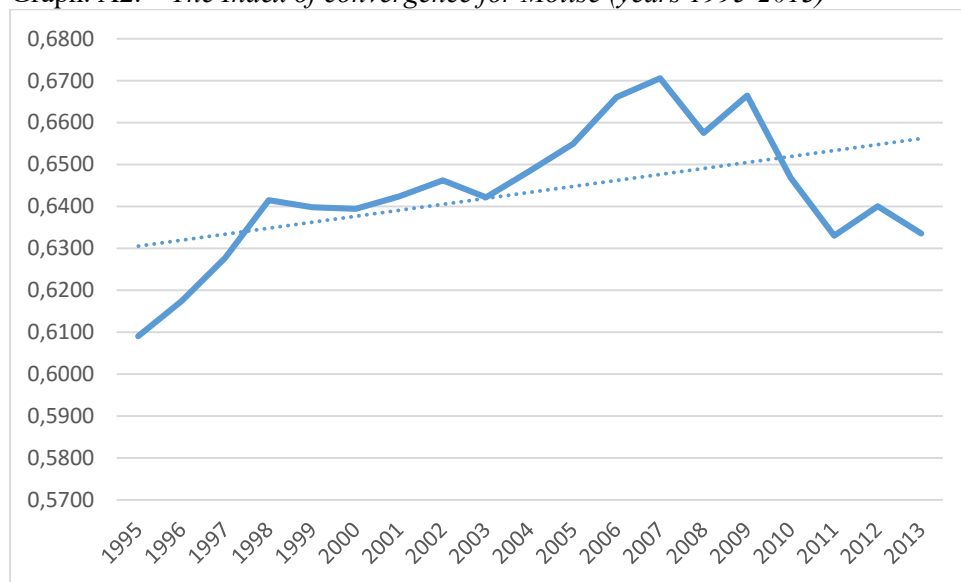
APPENDIX

Graph. A1. *The Index of convergence for Abruzzo (years 1995-2013)*



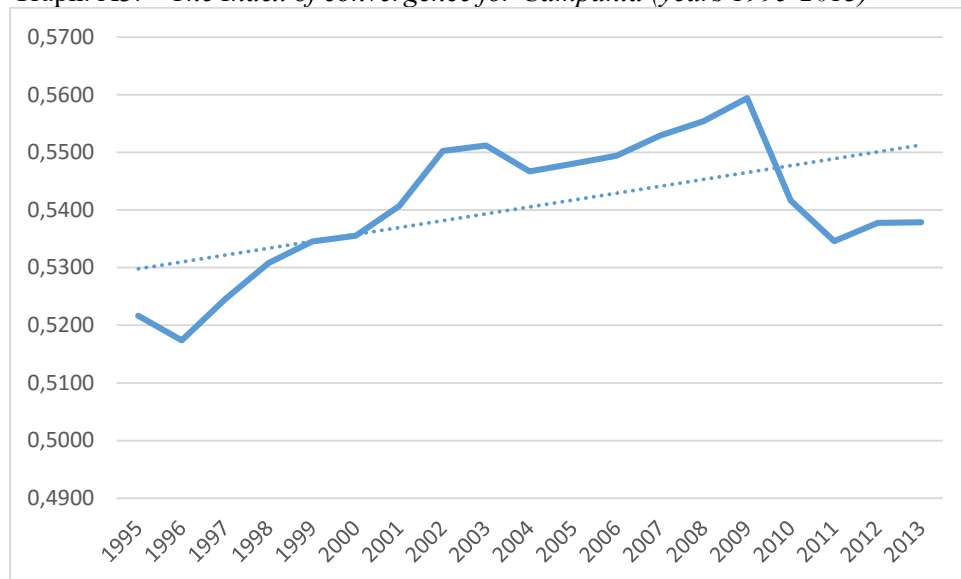
Source: *Our processing of ISTAT data*

Graph. A2. *The Index of convergence for Molise (years 1995-2013)*



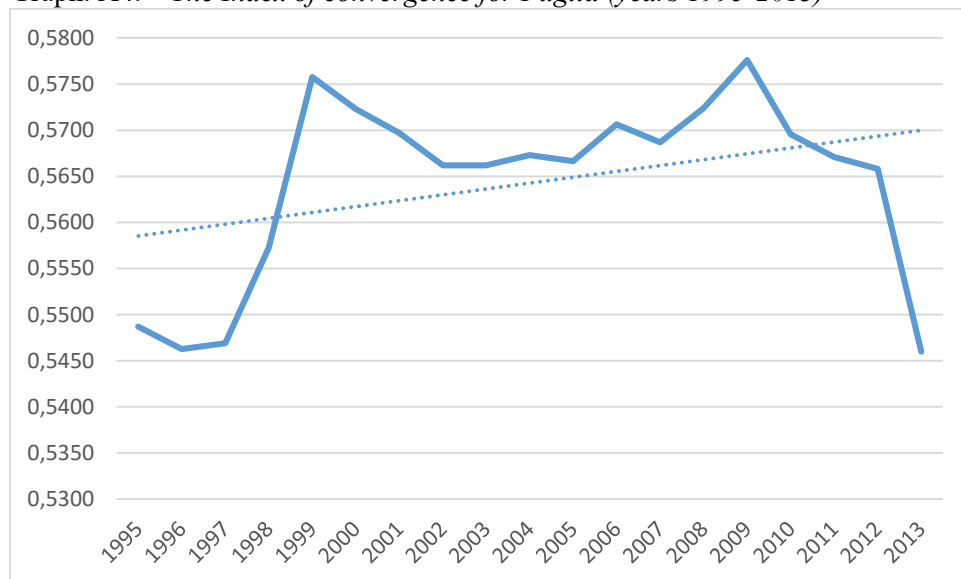
Source: *Our processing of ISTAT data*

Graph. A3. *The Index of convergence for Campania (years 1995-2013)*



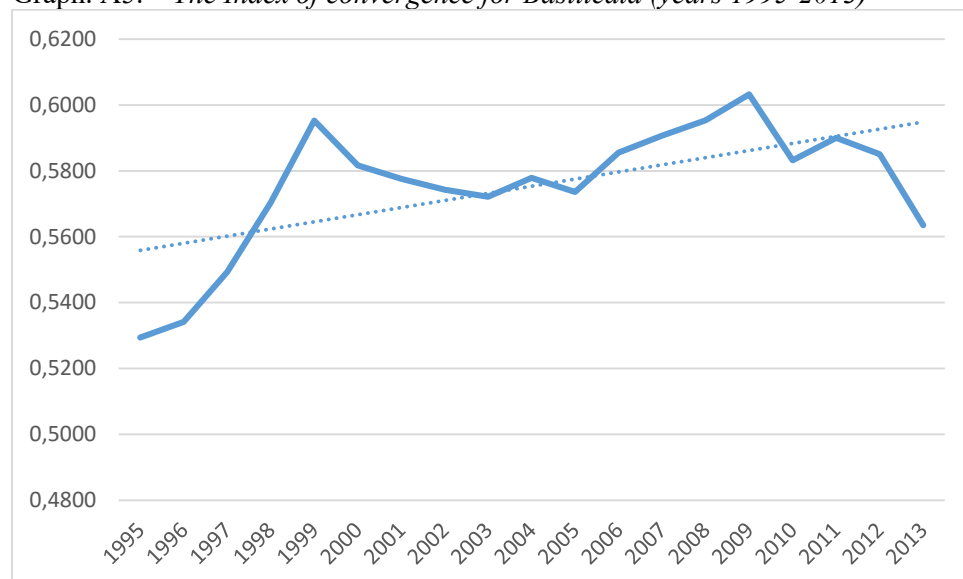
Source: *Our processing of ISTAT data*

Graph. A4. *The Index of convergence for Puglia (years 1995-2013)*



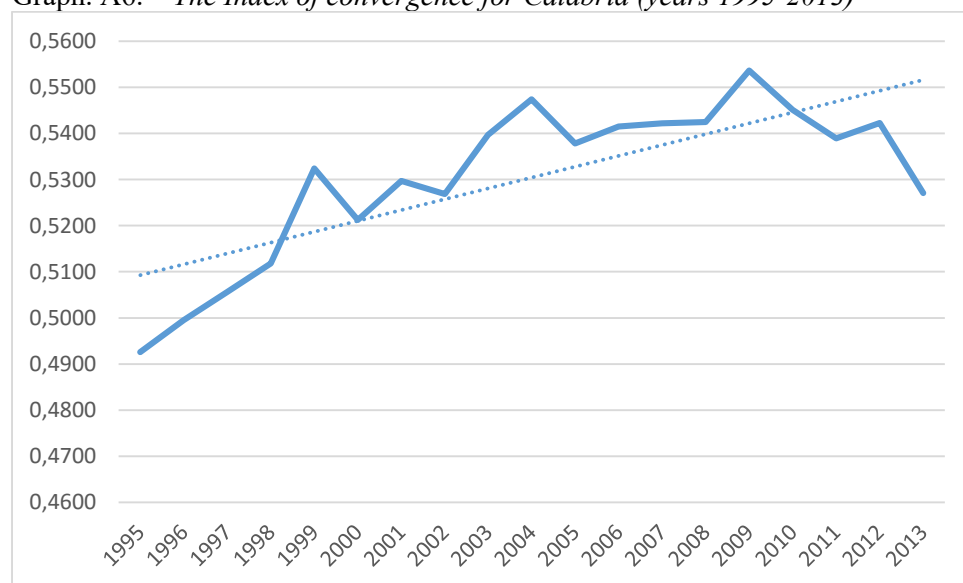
Source: *Our processing of ISTAT data*

Graph. A5. *The Index of convergence for Basilicata (years 1995-2013)*



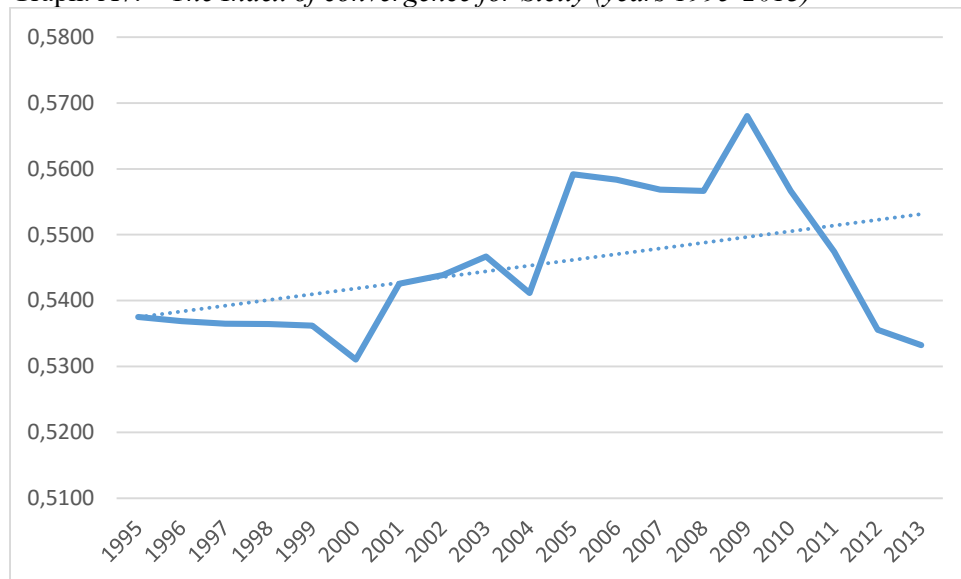
Source: *Our processing of ISTAT data*

Graph. A6. *The Index of convergence for Calabria (years 1995-2013)*



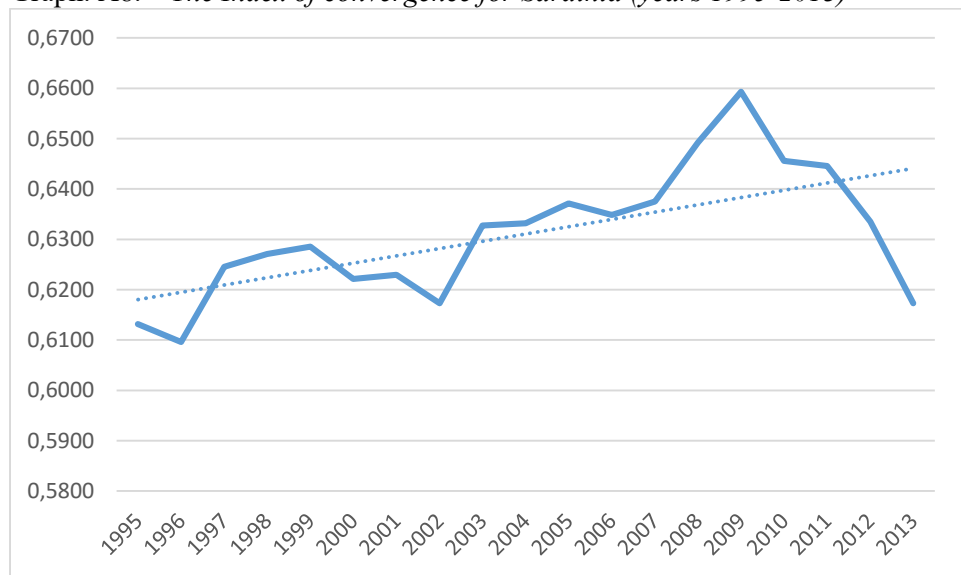
Source: *Our processing of ISTAT data*

Graph. A7. *The Index of convergence for Sicily (years 1995-2013)*



Source: *Our processing of ISTAT data*

Graph. A8. *The Index of convergence for Sardinia (years 1995-2013)*



Source: *Our processing of ISTAT data*