Summary for non-specialists
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Growth Effects of Structural Reforms in Southern Europe: The case of Greece, Italy, Spain and Portugal

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This paper uses a semi-endogenous growth model for analysing the intertemporal effects of structural reforms in Southern European countries (Italy, Spain, Portugal and Greece). Since many reforms are likely to have effects on TFP such an approach appears warranted. We use a comprehensive set of structural indicators in order to calibrate the model to important macroeconomic ratios and levels of productivity and employment. A model based analysis has the advantage that we can look simultaneously at different structural rigidities. Assessing reform needs in a comprehensive fashion also allows us to assess the plausibility of the individual reform multipliers generated by the model.

Our results show that structural reforms yield significant economic gains in the medium and long run. However, the short run gains are unlikely to be large. The results point to the importance of product market reforms and labour market related education and tax reforms as the most promising areas of structural policy interventions.

In particular the analysed structural reform scenarios show that the GDP-per-capita gap between the selected Mediterranean countries and the average of the best three euro area performers can be closed in the long run by about 78 % in Greece, by 87% in Italy, 99% in Spain, and by 67 % in Portugal. Reforming the product market yields the highest GDP gains in Greece. All four countries would largely benefit in the long run from skill-upgrading of their labour force. Short term gains can mostly be expected from tax shifts towards higher VAT (and lower labour taxes). In terms of employment gains, tax reforms and skill-upgrading in the form of increasing the share of medium and high-skilled labour supply can help the most to increase the employment rate in the long-run. Closing the reform gap relative to a benchmark country (or aggregate) should roughly close the corresponding income gap. This is the case for Spain, and to a lesser extent for Italy. In case of Greece and Portugal the aggregate effects of the reform scenarios cannot close the full income gap, suggesting that there are remaining structural rigidities which we have not quantified here.

This paper also argues for placing more emphasis on education policy which is key in upgrading the labour force, especially in these countries where the share of low skilled labour is among the highest in the euro area. Increasing the share of medium and high-skilled human capital promises significant long-run economic gains in these countries.