

THE IT REVOLUTION AND SOUTHERN EUROPE'S TWO LOST DECADES

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Abstract

Since the middle of the 1990s, productivity growth in Southern Europe has been substantially lower than in other developed countries. We argue that this divergence was partly caused by inefficient management practices, which limited Southern Europe's gains from the IT Revolution. To quantify this effect, we build a multi-country general equilibrium model with heterogeneous firms and workers. In our model, the IT Revolution generates divergence for three reasons. First, inefficient management limits Southern firms' productivity gains from IT adoption. Second, IT increases the aggregate importance of management, making its inefficiencies more salient. Third, IT-driven wage increases in other countries stimulate Southern high-skill emigration. We calibrate our model using firm-level evidence, and show that it can account for 35% of Italy's, 47% of Spain's and 81% of Portugal's productivity divergence with respect to Germany between 1995 and 2008. Counterfactual policy experiments show that subsidies to IT adoption or education cannot reduce this gap: only policies which directly tackle inefficient management are effective. (JEL: L23, O33)

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