THE ECONOMIC IMPACT OF LEGISLATION. AN HISTORICAL ANALYSIS OF ITALY FROM THE CREATION OF THE KINGDOM OF ITALY TO THE END OF THE SECOND WORLD WAR.

by

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Abstract. This paper aims to evaluate the economic impact of legislation from the creation of the Kingdom of Italy in1861 to the end of World War II. This historical analysis attempts to prove that the process of institutional unification of the states that existed before the creation of the Kingdom of Italy had a positive impact on the growth of the Italian GDP, due to the fact that legislative uniformity helped to simplify economic exchange and development, by establishing certain rules over the entire territory of the Kingdom, instead of the piecemeal legislation existent prior to unification.

JEL classification: N13, K10.

Keywords: Economic History of Italy; Growth, Institutional changes; Legislative complexity; Kingdom of Italy.

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1. INTRODUCTION.

The relationship between legislation and economic activity has been the object of extensive research in economics for its undeniable importance (for a survey of this literature, see Ginsburg 2000). The interdependence between the legislative framework and economic development has been a central concern of modern social theory, providing a focal point for the analyses of Marx, Durkheim, and Weber. More recently, Barro (2013) emphasized the positive impact of the rule of law on economic development.

Up to now, there have been no studies regarding the economic effect of the establishment of the Kingdom of Italy on the GDP of the Italian peninsula, from 1861 to the end of World War II. The Kingdom of Italy constitutes an example of unification of a number of small states: the Kingdom of Sardinia, the Duchy of Parma, the Papal States, the Kingdom of the Two Sicilies, just to name a few. These small states had different legislation, currencies and social customs and this might have represented an obstacle to economic development (due to divergent, and sometimes conflicting, legislation). As a consequence of the unification of Italy, the Constitution of the Kingdom of Sardinia (the *Albertine Statute*, in force since 1848) was extended to the citizens of the unified Kingdom.[1]

The creation of a unified Kingdom in place of the many small pre-unification states might have been expected to promote economic growth: the creation of a single market together with the introduction of a single currency (the lira) throughout the Italian peninsula might be expected to foster economic activity (and trade). Moreover, the creation of a uniform legislation would reduce regulatory uncertainty, simplifying the identification of the rules to be applied.

In this paper we discuss and test empirically the effect of legislation on economic activity by considering the unique historic case represented by the creation of the Kingdom of Italy in 1861. Our expectation is that during the early stages of the new Kingdom, the unified legislation would have

[1]This is known as the *piemontesizzazione* of Italy. With this term we refer to the process of extension of the Albertine Statute to all the pre-unification states. The Kingdom of Sardinia was the only pre-unification Italian state whose citizens enjoyed a constitution and an elected parliament.

favored economic growth. Our dataset covers seventy-seven years, from Unification in 1861 to the end of World War II in 1918.

The paper is organized as follows. Section two contains a brief history of the legislative evolution in the Kingdom of Italy. Section three describes a very simple theoretical model showing the relationship between per-capita GDP and legislation. Section four reports and discusses the econometric analysis. Final remarks conclude the paper.

2. LEGISLATIVE EVOLUTION IN THE KINGDOM OF ITALY: AN HISTORICAL OVERVIEW.

The Kingdom of Italy was established in 1861 as the result of a gradual process of extension of the frontiers of the Kingdom of Sardinia. The hypothesis of a federal solution was excluded, the convocation of a Constituent Assembly likewise: it was therefore decided to extend and centralize the hierarchical *Piedmontese* model. This involved the introduction not only of the Statute of the Kingdom of Sardinia, but also of fundamental parts of its legislative structure.[2] Few new institutions were established, whereas many provisions were made to apply or adjust the Sardinian institutions to the Kingdom of Italy (Cassese, 2014).

An examination of the legislation of the first four-year period of unity allows us to understand the roots of the Italian State. These must not be sought, as in other nations, in military requirements, nor may they be found in the need to elevate a nation to State level. With regard to this latter intention, it is also necessary to underline how few elements were capable of creating a national identity. This was largely due to the fact that the levels of economic and social development in the peninsula were very different. Literacy varied from zone to zone, and particularly from provincial North to provincial South (few inhabitants of the peninsula, not many more than 2%, spoke Italian and only around 10% were able to intend it). The crime rate was also far from uniform.

[2] The analysis of the Official Gazette of the Kingdom of Italy (i.e. "Raccolta ufficiale delle leggi e dei decreti del Regno d'Italia") confirms this: it was not, in fact, a constituent phase, but a period of adaptation of the institutions of the Kingdom of Sardinia to the new Kingdom.

The reasons for the creation of an Italian State must be sought, rather, in the ambitions of a dawning Italian capitalism. The ruling political class consisted for the most part of land owners and entrepreneurs. They desired to emulate the rapid industrial development under way in England and France, that they attributed to the creation of a large internal market. This gave them the extraordinary incentive to reach economic unification even before achieving administrative unity. The first governments of united Italy, in other words, were less concerned with the building of a State and the creation of an apparatus a set of administrative organs and rules than with economic unity (Cassese 2014).

Before unification, political particularism had led to a plurality of legislations. Nevertheless, the laws had essentially maintained common characteristics across the different pre-unification Kingdoms during the period leading up to the unification of Italy (the "Risorgimento"), if not in content at least in basic principles. This undoubtedly facilitated the legislative unification of the new State, a unification that could have been realized through three alternative strategies. One option consisted in extending the legislation of the Kingdom of Sardinia to the entire national territory. A possible alternative was to maintain the laws of the single States existing before the unification, thus constituting a decentralized legislative system on the basis of specific territorial needs. The third option was to predispose (*ex novo*) a single valid national codification for the whole territory of the new State.

In the first phase of the unification process, the first option was adopted and the Piedmontese legislation was extended to Lombardy, Emilia, Marche and Umbria. For political reasons, however, this option was subsequently abandoned. On the other hand, the will to realize a real legislative unification was in conflict with the second option, that is the maintenance of the collection of "old" laws and codes. The case of Tuscany, where political necessity had determined the provisional maintenance of the legislation of the "Granducato", or that of southern Italy, which was permitted to maintain the civil and commercial legislation applied up to 1860, could no longer be tolerated without denaturalizing and contradicting the essence of the juridical arrangement of the unitary State. The final solution, therefore, could only be that of editing and publishing new legislative texts to be introduced and applied in the whole State. These were the 1865 codes (Ghisalberti, 1982). Their immediate application, observance and duration over time testify to the correspondence of the unitary legislation to the demands of the new Italian society.

When the “Sinistra storica” came into power, it elaborated a legislative policy of continuity, adding the “Codice della Marina Mercantile” (1877), the “Codice di Commercio” (1882) and the “Codice Penale” (1889); this latter completed and improved the institutional model created in 1865 (Ghisalberti, 1994).

The correspondence of the laws encoded between 1865 and 1889 to the principles of modern liberalism also resulted in the lack of substantial reforms in the fifteen years that marked the apogee of the liberal State. Nevertheless, at the beginning of the XX century, the legislative uniformity typical of the preceding period was abandoned.

During the unification process, Italy appeared as a country characterized by deep and intense disparities, disunited on economic, cultural and even linguistic counts, divided by strong dissimilarities of development. This contributed to produce a characteristic line in Italian institutional history: a derogatory legislation. The purpose was certainly reasonable: to differentiate legislation according to the area of its application and therefore to meet the particular demands of the depressed areas, not only in the south. This was a solution, albeit partial, to the disunited nature of the territory. Nevertheless, the creation of local administrations and procedures that developed parallel to the national ones limited the uniformity of the laws (Cassese, 2014).

The special laws for Naples (1885 and 1904), Calabria (1906) and Basilicata (1908) introduced the principle of legislative differentiation into the Italian legal system. Diversity was realized in various ways: by increasing infrastructural interventions in less developed areas; by introducing special procedures and organs; by providing for tax cuts, credit facilities, contributions for specific areas of the national territory (Cassese, 2014).

The accumulation of extraordinary rules, representing evasions and erosions of the codified laws, always requiring and proposing new adaptations to specific cases, encouraged / gave rise to a sort of "legal disobedience" (Cassese, 2014). It also led to an overabundance of rules: it is evident that the number and complexity of the laws depend on the complicated social relationships and on the quantity of affairs for which the institutions were made responsible (Mattarella, 2011).[3] It is also true, however, that the Italian legislation had become far more abundant and complex than the circumstances required. The complexity of social relationships justified the complexity of the norms but not the contradictory nature of the laws. The derivation of further costs of fulfilment from the excessive number and bad quality of the laws should have been avoided (Mattarella, 2011).

In the period from 1900-1915, that is the period of economic and administrative growth, the quantity but above all the quality of the rules changed radically. From universal and abstract, the laws became particular and concrete (from the *leggi-monumento* to the *leggi-provvedimento*). In the meantime, the administration assumed a new role as the specific place in which the application of the law found its technical mediation, sometimes its mitigation. In short, administrative discretion emerged as a decisive element of government (Melis, 2010).

In the fascist period, a large part of the normative picture remained solidly founded upon the principles of the preceding juridical tradition: not only were the fascist reforms respectful of the inheritance received from the liberal State; they also maintained most of the normative corpus accumulated during the experience of the unitary State. Naturally, the legislative initiative of fascism was nevertheless conspicuous, ambitious and incisive. The regime set its hand to vast sectors of subjects, often giving them new, original orders. It was a season of impressive legislative fertility, (at least on the grounds of quantity), such as united Italy had perhaps never known.

[3] Giovanni Giolitti, after all, noted: "I admit that about the laws the maximum simplicity is the ideal; but it is not always attainable, because the laws must also keep in mind the defects and the deficiencies of a country […] and adapt to them. A tailor that must cut a suit for a hunchback, must also make a hump for the suit" (Giolitti, 1922).

The fascist period was strongly characterized by the powerfully innovative relationship between normative tools and affairs involved in public regulation. Whole sectors were rearranged around a specific law, to which however was connected an incisive production of actions, decrees, ordinances, directives emanated in various forms by the public authority but not necessarily by the State. The legislation of the 1930s therefore produced an impressive activity of secondary regulation, sometimes more meaningful than the legislative measures themselves.

During the Fascist period the role of the national parliament as a place of legislative output has been reduced in favor of the government, to whom since 1926 has been granted a specific power to emanate laws. This task was delegated to the technocratic élites of each sector, that vast world of experts in the single fields, who held a specific and exclusive knowledge of the specific issue to be modified; or,better still, to the interaction among these technocratic circles and the ministerial vertices constituting the direct political-administrative point of contact in each field (Melis, 2014).

The codification produced in the fascist period was almost entirely independent of the juridical ideology of fascism. This was because its formative process developed slowly and with a series of firm controls in order to prevent the ideology of the regime from prevailing over the normative elaborated. The 1942 civil code, for example, was the most important normative text of the fascist period. Fulcrum of the entire juridical system emanated in these years, it was worthily inserted in the tradition of the Italian laws. It succeeded in innovating that tradition by adjusting it to the demands of an economy that was becoming largely, even if not yet primarily, industrial. Since the regime did not outlive such a text, the 1942 civil code had a separate and different life from that for which it had been conceived. Connected to the other codes compiled in the Fascist period, it served to facilitate and simplify the changes in Italian society, accelerating its growth and development. Italy approached the great democracies of the liberal West that were benefited from many of those juridical principles that, despite the dictatorial regime, the code had been able to preserve and to innovate (Ghisalberti, 1994).

In conclusion, none, or hardly any, of the great institutions that had characterized the birth of the bourgeois nations elsewhere were realized in Italy in the years following 1861 (Melis, 2010). Italy did not have a single magistracy, nor a uniform credit framework (six central banks existed at the time of the 1893 banking reform, that reduced them to three). Further, there was not a modern system for the assumption of public employees, nor a unique metric system, nor a national real estate registry, nor a modern and centralized system of fiscal collection.

However, the managing class of unified Italy thought that, if a uniform normative corpus was not adopted, juridical particularisms would be developed, with serious consequences for economic growth. It is necessary to bear in mind that legislative unification represents an essential condition for the creation of a national market. The 1865 codes were an answer to this need. As we have seen, this process continued and, despite the advent of a derogatory legislation, it led to a far more uniform legal system compared to the ones that had been in force in the different States that went to form the Kingdom of Italy.

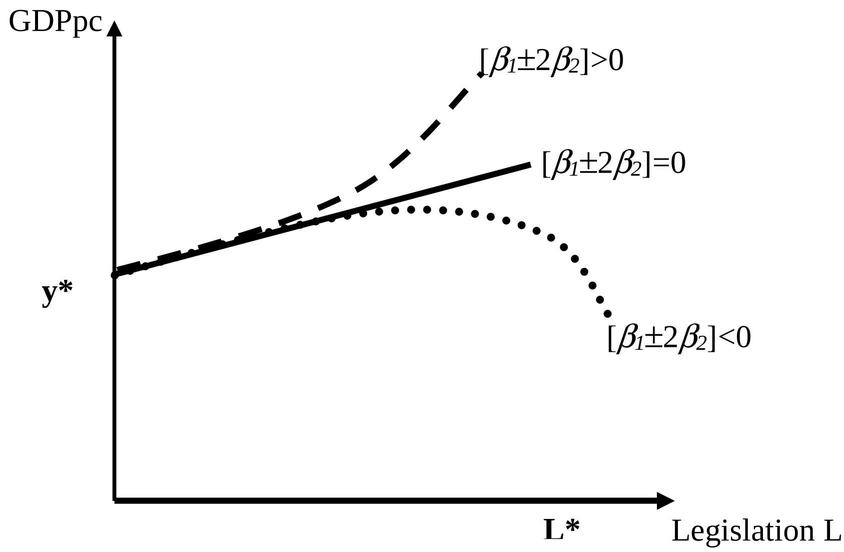
3. **A SIMPLE THEORETICAL FRAMEWORK.**

As mentioned in the introduction, the positive effect of an effective legislation on economic activity is an established result in development economics (Montes and Paschoal, 2016).Nonetheless, legislation may also have a negative effect: an excessive accumulation of laws may lead to an unsustainable level of legislative complexity (Bardhan, 2002, Dawson and Seater, 2013, Di Vita, 2015). Indeed, legislative complexity is considered an obstacle to growth in many countries (OECD, 2014): due to the overlapping and layering of laws, it creates uncertainty about which rule is applicable.

As the number of laws increases, there is also an increase in consequential issues of interpretation and negative externalities of coordination between laws passed at different points in time. This generates legislative complexity with social costs which may outweigh the social benefits, especially in countries with a long history of liberal democracy as their form of government (Di Vita, 2015, Mora-Sanguinetti and Mora. 2015).

Based on the results of the empirical literature (Khan and Hudson, 2014) that suggest the positive effects of an effective rule of law, but also the adverse effects of complex/excessive legislation on growth, the relationship between legislation and the GDP is not likely to be linear. Before proceeding to the empirical analysis, we clarify the theoretical assumptions about the economic impact of legislation L on per capita GDP(y).

FIGURE 1



We may assume, as shown in Picture 1, that the relationship between legislation *L* and the per-capita GDP*y* could be either an increasingly convex curve (dashed line), or linear (continuous line) or a rising concave curve (bullet line). In math notation:

[1] $y = f(\vec{X}),$

where y is per-capita GDP and the vector $\vec{X}$ includes all the relevant explicatives, including legislation *L*. Assuming a log-linear form, eq. 1 can be expressed as follows:

[2] $y = \alpha + \beta_1 L + \beta_2 L^2 + \sum_{i=3}^{n} \beta_i x_i ,$

α is the intercept and β_I is the elasticity of each single variable considered. Given our focus on legislation, we concentrate on β_1 and β_2 representing, respectively, the impact of legislation and its square on per-capita GDP. β_1 is assumed to be positive and (far) lower than one, while β_2 could be either negative or positive. As for now, we set the other explicatives ($x_3,...,x_n$) equal to zero, but we will include them in the subsequent econometric analysis.

Using the first derivative of [2] we obtain

$$[3]\ \frac{dy}{dL} = \beta_1 \pm 2\beta_2 L \begin{cases} > 0 & \Rightarrow \quad \text{the function is increasing,} \\ = 0 & \Rightarrow \quad \text{the function is a horizontal line,} \\ < 0 & \Rightarrow \quad \text{the function is decreasing,} \end{cases}$$

limiting our analysis to the hypothesis of dy/dL> 0, and taking the second derivative we obtain

$$[4]\ \frac{d^2 y}{dL^2} = \pm 2\beta_2 \begin{cases} > 0 & \text{the function is convex,} \\ = 0 & \text{the function is a line,} \\ < 0 & \text{the function is concave,} \end{cases}$$

as represented in Figure 1. Under the condition that the first and second derivatives of *y* with respect to *L* are both positive (i.e. $dy/dL > 0$ and $d^2y/dL^2 > 0$), legislation always causes a positive externality on the GDP, because its effect on the dependent variable is more than proportional. For $dy/dL = 0$ and $d^2y/dL^2 = 0$ the economic impact of legislation on the GDP is directly proportional to the values of the parameters. Finally, under the conditions $dy/dL > 0$ and $d^2y/dL^2 < 0$ legislation generates a positive externality on the GDP until a threshold level L*is achieved, whereas beyond that point, legislation has a negative effect on *y*.

In principle, all the three alternatives are plausible. The sign and significance of β_i are likely to depend upon the specific case considered (country and time), so it is matter of applied research and we will check this in the next empirical analysis.

4. Econometric Analysis and Results

In this section we study the relationship between legislation and the GDP in the Kingdom of Italy. As matter of fact, the analysis of Italy's GDP per capita in such a period poses many challenges. Indeed, this period goes from Italy's first and main step of unification in 1861, when the Kingdom of Italy was established, to the collapse of the Monarchy and the establishment of the new Republic in 1946.[4]

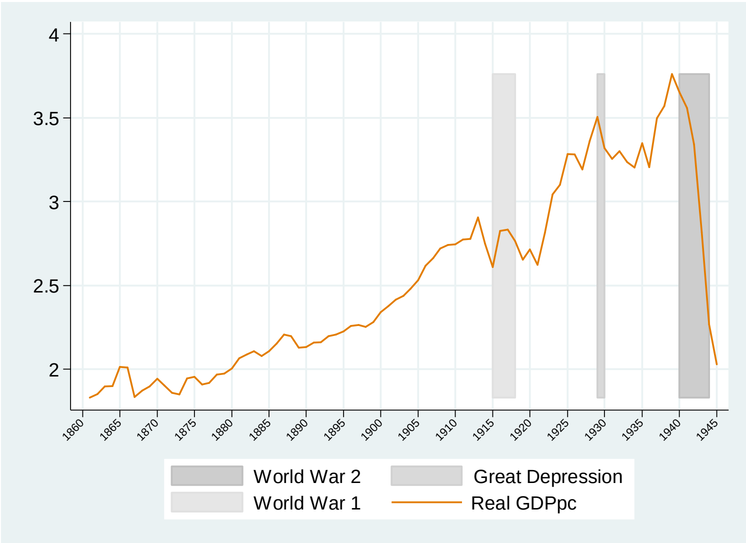
As known, Italy's defeat in World War II entailed the collapse of its previous constitutional order which had existed since 1861. Indeed, that constitutional order had remained formally the same from 1861 to 1943, although Italy turned de-facto into a dictatorship from 1922 onwards as a result of the rise to power of the Fascist party. Nonetheless, a sufficient degree of continuity in terms of legislation (section 2) and economic developments existed from 1861 to 1940.We therefore analyse this period and rule out the years after 1940.

Our variable of interest is the Real GDP per-capita; this is extracted from the database of Banca d'Italia (Baffigi 2011). The data refer to Italy's current boundaries.5 Real GDP per-capita is plotted in Figure 1.

[4] Important events during this period were the annexation of the Veneto region in 1866, the annexation of the Lazio region (which includes Rome) in 1871, World War I in 1915-1918 with the consequential annexation of the Friuli-Venezia Giulia region in 1918, the Great Depression from 1929 and Italy's participation in World War II from 1940.

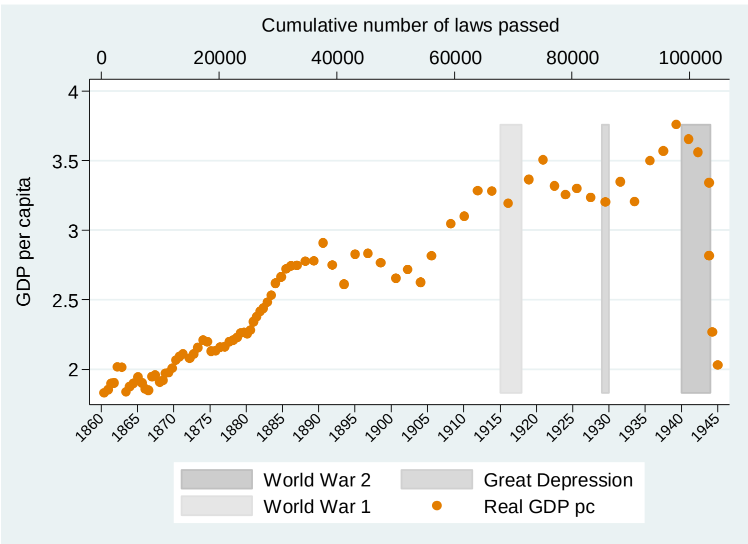
[5] The effect of the abovementioned annexations is uncertain. To wit, the annexation of a populous less-developed area, probably after a conflict which hads directly affected it, may have caused a drop in Italy's GDP per-capita not linked to any particular economic development.

Figure 1 – Real GDP per capita.



As discussed in the first part of the paper, we are interested in checking whether the institutional development of the Kingdom of Italy had a positive impact on the GDP per-capita of the Italian Peninsula. The institutional development is approximated through the number of laws passed by the Kingdom of Italy's Parliament. A simple way to start studying their relationship is to plot it using a scatter-plot. This is illustrated in Figure 2.

Figure 2 – Scatterplot: Cumulative number of laws passed- Real GDP per capita



The positive relationship emerging from Figure 2 is not surprising. As known, per-capita GDP has a positive upwards trend while the number of laws passed each year adds positively to the previous one. Then, both variables have a clear upwards trend. Based on this consideration, a proper econometric analysis is the right tool to check for a causal impact of legislation on GDP.

The GDP series has been the object of econometric analysis for decades. We refer particularly to the literature on the determinants of economic development: Levine (2005) and Arcand et al. (2015) include excellent reviews of this literature. GDP series are known to be not covariance-stationary processes. This is why as a first check we verify the stationarity of the object of our analysis through unit-root tests. The hypotheses tested are: 1) “H0: unit root” using the DF-GLS test (Elliott et al. 1996) and the PPerron test (Phillips & Perron 1988); 2) “H0: no unit root” using the KPSS test (Kwiatkowski et al.1992). Unit-root tests notoriously depend upon the inclusion of the deterministic components and they are sensitive to the number of lags included in the regression.6 A number of different alternatives were run, the results of which are reported in Table 1. On the whole, the tests suggest that the real per-capita GDP series is not covariance-stationary.

Table 1 – Unit Root Tests on Real per-capita GDP

Elliott et al. 1996 H0: Unit Root	DFGLS stat, 1Lag: -1.186 | 5% CV: -2.970 DFGLS stat, 3Lag: -1.016 | 5% CV: -2.959 does not reject H0
Phillips &Perron 1988 H0: Unit Root	T-stat: 0.544 | 5% CV: -2.887 does not reject H0
Kwiatkowski et al.1992 H0: no unit root	T-stat, 4L: 0.644 | 5% CV: 0.146 T-stat, 3L: 0.797 | 5% CV: 0.146 rejects H0

Notes: xL means test executed with x lags.

As a consequence of the non-stationarity found, we study the first-difference of log GDP. As known, first-differencing is likely to make the GDP series stationary. The first-difference of log variables approximates the growth rate. To study the evolution of the GDP through its growth rate is a common practice in current literature. The typical cross-sectional specification for the analysis of the GDP growth rate is:

[6]Under the null of a unit root, inclusion of a constant in Dickey-Fuller kind of equations implies a linear trend, while under the alternative it is just a constant.

$$\Delta lGDP_i \;= \alpha + \beta \cdot lGDP_{i/t-1} + \vec{\Gamma} \cdot \vec{X}_i + \varepsilon_i \, \Delta lGDP_i = \alpha + \beta_i \cdot lGDP_{i/t-1} + \vec{\Gamma} \cdot \vec{X}_i + \varepsilon_i$$

where the dependent variable is the first-difference of log GDP, α is the constant, the initial level of the GDP is included to test conditional beta-convergence (Young et al 2008) and$\vec{X}_i$ is a set of explicative variables; for applications of this specification, see Arcand et al. (2015) or Barro (1996). We adapt this cross-sectional specification to our time series data. The main concern in this regard would be serial-correlation, but the series of the real GDP growth rate does not exhibit serial correlation at all, as shown by the autocorrelation and partial autocorrelation functions in Table 2. We therefore estimate the following specification:

$$\Delta lGDP_t \;= \alpha + \beta \cdot lGDP_{t-1} + \vec{\Gamma} \cdot \vec{X}_t + \varepsilon_t \, \Delta lGDP_t = \alpha + \beta \; \cdot lGDP_{t-1} + \vec{\Gamma} \cdot \vec{X}_i + \varepsilon_i$$

Table 2 - Auto and Partial Correlations

LAG	AC	PAC	Q	Prob>Q
1	-0.079	-0.081	0.5192	0.471
2	-0.184	-0.197	3.333	0.188
3	0.009	-0.022	3.340	0.342
4	0.036	-0.011	3.452	0.485
5	-0.050	-0.049	3.669	0.598

In accordance with the literature on the determinants of GDP growth (Sala-i-Martin et al. 2006), we include the following explicative variables($\vec{X}_i$): the years of school education (SCH, from ISTAT), the Inflation Rate (INF, from Banca d'Italia), the degree of trade openness (OPE, from Banca d'Italia), the amount of public expenditure (PEX, from Banca d'Italia), the amount of total investment in fixed capital (TFI, from Banca d'Italia), a dummy to control for World War I (D_W). The number of laws passed (LEX) is our variable of interest. Table 3 reports summary statistics for the variables used in the estimation. The estimation output is recorded in Table 4; Newey-West standard errors are computed and used to check statistical significance.

Table 3 - Variables

Variable		Obs	Mean	Std. Dev.	Min	Max	Source

Per-capita GDP Constant Prices (r.y. 2005) Thousands of Euros	GDPpc	80	2.51	0.54	1.82	3.76	BdI
Inflation Rate % (via GDP deflator)	SCH	79	3	10.33	-14.73	42.67	BdI
Literacy Rate (age 15-19)	INF	81	62.37	22.88	26.5	88.2	Istat
Degree of Openness	OPE	80	0.23	0.04	0.1	0.36	BdI (our calculations)
Public Expenditure (constantprices)	PEX	79	7.36E+10	3.39E+10	2.25E+10	2.25E+11	BdI
Total Fixed Investments (constant prices)	TFI	80	10547.83	6283.92	2583.68	23030.53	BdI
Number of Laws passed	LEX	80	1247.55	816.03	416	3458	Istat

Table 4 - Estimation Output

ΔGDPpc_t	1	2
	-	-
GDPpc_t-1	0.292**	0.279**
SCH_t	0.019	0.013
INF_t	0.047	0.05
OPE_t	-0.091	-0.065
PEX_t	-0.017	-0.009
TFI_t	0.062**	0.063**
D_W	0.011	0.005
		-
LEX	0.030**	0.358**
LEX^2		0.027**
_cons	-0.143	1.038**
N	79	79

All variables are in log terms.
** marks significance at 5%
* marks significance at 10%

The estimation output shows a negative and significant effect of the initial per-capita GDP level coherently with the beta-convergence notion. Among the explicatives included, Total Investment in fixed capital turns out to be statistically significant and signed as expected. The other explicatives turn out not statistically significant. As for the contribution of the institutional environment, as approximated by the number of laws passed (LEX in Table 4), the effect emerging from the estimation in column 1 is positive. However, when its squared value is added, the sign turns negative; both are statistically significant.

5. Final Remarks.

The results of the econometric analysis seem to confirm the positive impact on the GDP of the newly created Kingdom of Italy that introduced a single currency and created a uniform legislation within the borders of Italy, thus promoting economic activity and trade and encouraging social and economic mobility.

The process of unification of legislation took place with the extension of the Albertine Statute to all the Kingdom of Italy, together with the subsequent production of legislation by a parliament elected by universal male suffrage. The results of the econometric analysis show that a low level of legislation accumulation and stratification makes the social revenue of legislation greater than the social cost due to negative coordination externality. This is because a threshold level of legislation stock is achieved and the social revenue of new legislation is lower than the social costs.

These are our preliminary conclusions, that need deeper analysis to reach more robust results.

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