

CONFCOMMERCIO

PRESENTATION BY EDWARD C. PRESCOTT

AT THE FORUM:

**"MARKET LEADERS AND SCENARIOS
FOR THE 21ST CENTURY"**

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The International Economic Outlook

Edward C. Prescott

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Market Leaders and Scenarios for the 21st Century

Good Times Ahead for Italy and the EU-15

- Per capita GDP will grow at 2% in the short run
- Per capita GDP will boom over the next 10 years and catch up to the U.S. level
- No danger of U.S. dollar falling a lot
- Interest rates will change little
- Monetary authorities in Euro area and U.S. have inflation under control

Forecast for CE-8

Countries: Estonia, Lithuania, Latvia, Poland, Slovakia, the Czech Republic, and Hungary

- Have been catching up
- Will catch up to EU-15 in 15 years
- A couple already have

WHY?

EU Is a Good System

- Productivity of signers of Treaty of Rome (1957) was 55% of U.S. level for 40 years prior to World War II
- Their productivity caught up to the U.S. level over the next 30 years
- Late EU joiners lost ground relative to original members, but caught up after joining
- EU system will get better as it becomes more internally open – services will be liberalized

Why EU Is a Good System

- All countries have their share of people with talent
- With EU and U.S. systems, these people use their talents to create social surplus
 - rather than using them in unproductive rent-seeking activities
- Italian government makes it hard for Italian entrepreneurs
 - Ease up and they would create greater social surplus
 - The Italian people would be even better off

Some Basic Accounting

- **Low productivity**
- **Low market hours**

Output per person is ***productivity*** times ***market hours per person.***

Examination

Prescott, M.D.



The Statistics for 2006 Percent of U.S.

Economy	GDP per Person	Hours per Person	GDP per Hour
E.U.-15	74	80	92
U.S.	100	100	100
Japan	73	102	72

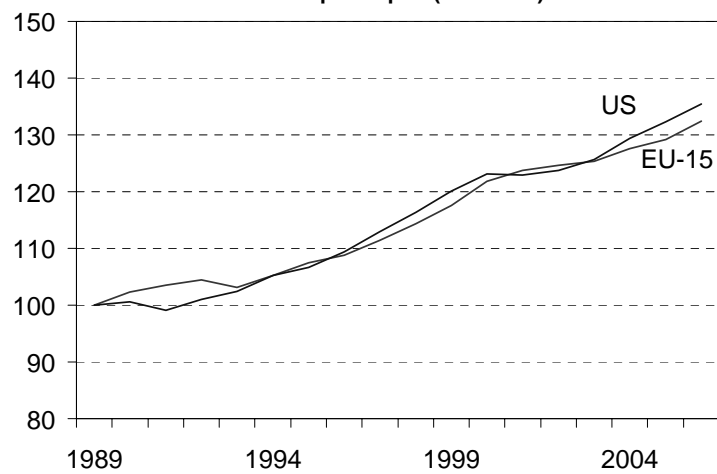
The Diagnosis

- E.U.-15 has a case of low labor supply disease

Is Europe Getting Sicker? NO

GDP Growth in E.U.-15 and U.S. Is Similar

Index of GDP per Capita (1989=100)



Source: GGDC

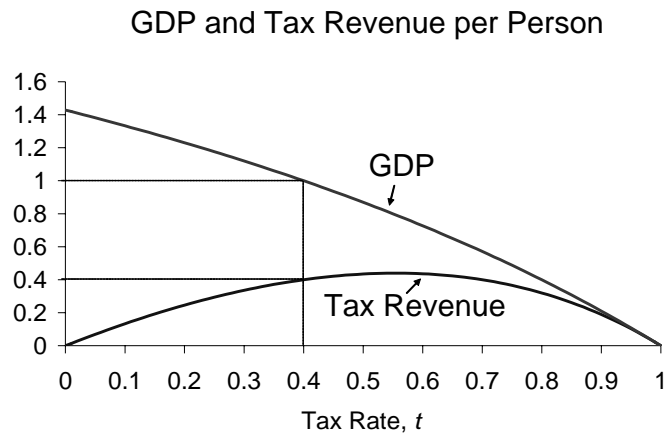
What Is The Cure? Tax Rate Cuts



What about Side Effects of Tax Cut?

- Won't this reduce revenues that are needed to finance social programs?
Won't it cause suffering?
- The answer is ...

No: Revenues Will Not Fall



If Europe Cuts its Tax Rates to U.S. Level

Consumption per person will increase by

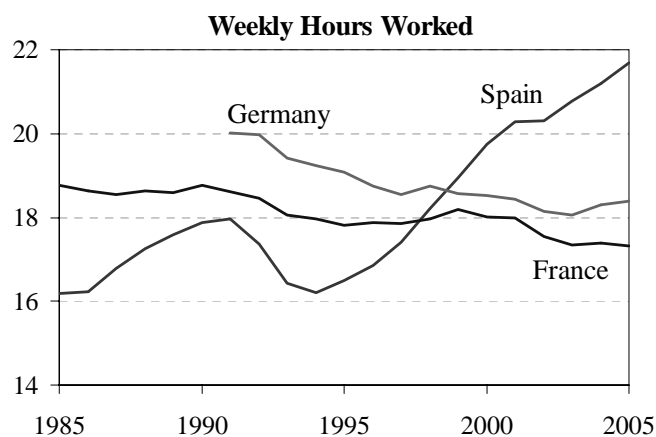
6000 €

and this increase will grow inflation-corrected
by 2% a year

My Prediction

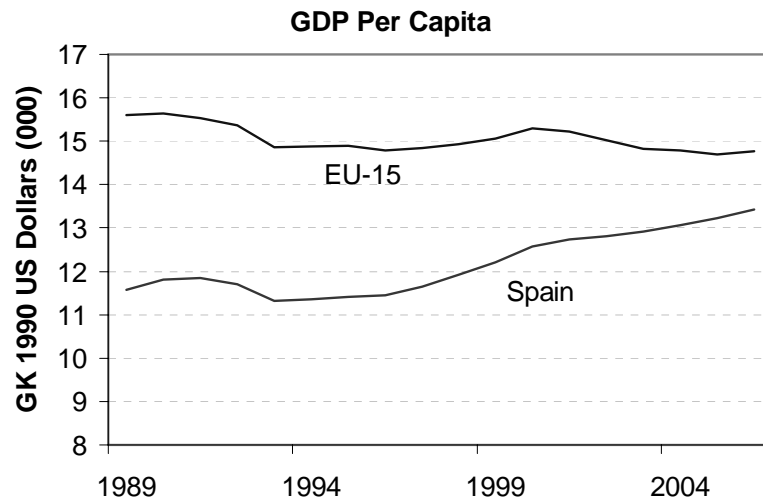
- Europe will reform its tax system – this process has already started
- Labor market policies that depress labor supply will be reformed
- The recent dramatic example of reform is Spain
 - Market hours per working-age person increased from 16 hours in 1994 to 22 hours today

Dramatic Improvement in Hours Worked



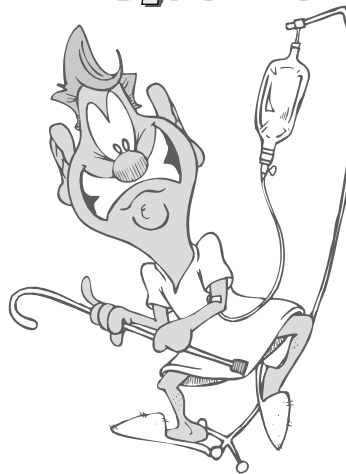
Source: OECD

Spain GDP Per Capita Near E.U.-15



Spain Is Feeling Much Better Now!

España



Summary

- E.U. has a great system that fosters productivity growth
- E.U. has a wasteful tax policy that depresses market hours
- Italy should follow Spain
- What is special about Italy is its entrepreneurs –

They are great