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Title: *In the shadow of the financial crisis: dismal structural change and productivity trends in Southern Europe over the last four decades*

Abstract: Southern European countries have been facing severe sovereign debt and fiscal deficits problems, which have prompted strong increases in bond spreads. These recent developments stimulated an important stream of research focusing on the performance of financial markets and on the relationship between fiscal policy and growth. The analysis of the specific trajectories of countries facing financial crises and of the interrelatedness of economic and financial crises has received, however, much less attention.

In the present paper we argue that the patterns of growth in Europe can be better understood if a regional, rather than a global European standpoint, is adopted. Accepting that there is a “southern” pattern of growth then explanations and specific policy measures can be envisaged. Common to south-western economies, most notably, Spain, Portugal, and Italy, is their stagnation and increasing difficulties in closing the gap with north Europe over the more recent period. Although Italy, Spain, and Portugal performed differently among themselves, the trends in comparative per capita income for these countries *vis-à-vis* the core EU countries followed a general pattern of rather slow convergence from mid-nineties onwards. At the same time, labour productivity and total factor productivity growth have been relatively disappointing.

In this paper, we give financial crisis an economic frame and shed light on the overall dismal performance of Southern Europe countries by stressing the role of structural change. Resorting to shift-share and growth accounting techniques, we demonstrate that from the mid-nineties onwards the most important contributor to labour productivity growth - goods production industries – suffered a drastic decline. In contrast, low productivity services sectors gained momentum. Such transformations in (economic) structure are shown to be correlated with countries’ international specialization patterns (against high skill and science-based activities) and education performance. Based on southern Europe experience, we conclude that the exclusive focus on policies of fiscal restraint is not sufficient if a long-term growth strategy is required. Any attempt to overcome the present difficulties must necessarily take into account productivity-driven growth measures which require a longer term, spatial and historical view.

Keywords: Long-run growth, structural change, Southern Europe.