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STATE INTERVENTION IN THE ECONOMY

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IN any type of society, regulating the economy is one of the functions of whomever hold the reins of government.

The more complex a society becomes and the wider the ramifications of the economy in production and trade, the more the government's guidance in the economic sphere is bound to grow and spread.

From the days of the earliest civilizations we have seen the two distinct forms in which this function is discharged: the indirect form, when the State – by virtue of its powers – influences the economy by means of legislation and administration, and the direct form, when the State becomes an entrepreneur and, either itself or through its agencies, engages in production and trade.

The forms of State intervention in the economy which interest us are those employed in the western world since the French Revolution and the first Industrial Revolution radically altered the basis and conditions of society.

The evolution of capitalism, up to its destruction in collectivism, is the salient feature of our life in the last few generations and the problem which faces all of us – governments, nations and individuals – in our continual search for freedom, justice and prosperity.

During the long stretch of social, economic and technical

progress in the century which ended in 1914 with the start of the First World War, the State modeled itself on liberal principles which tended to leave the forces of capitalism maximum freedom of choice and action. The task of the State, of which these forces were the pivot, was to create the most suitable framework for their activities by means of taxation, customs duties, public works and foreign policy. The State was not expected to act as a mediator between classes and conflicting interests or to see that the growing wealth was fairly distributed. On the one hand, its indirect intervention in the economic sphere was reduced to a minimum and directed towards promoting the development of capitalism; on the other any direct intervention was taboo except where it was limited – as, for instance, in Italy – to running certain industries, for tax reasons, as a State monopoly.

But the intrinsic evolution of capitalism and the extrinsic forces opposing it with ever-increasing pressure, led to a transformation of the State and its functions. This is a part of history which we all know and have lived through to some extent, but whose essential points must be underlined because they still overshadow our present problems.

The last hundred years of capitalist development have shown that the liberal theory of the private entrepreneur's gain and the automatic play of the market was incapable of achieving adequate production rates and conditions to meet the needs of the masses impelled by an urge for social redress. At the same time Liberal Government failed to satisfy those needs by a fairer distribution of income.

Already in the second half of the nineteenth century socialist and catholic doctrine and even the most advanced liberal thinking began to challenge the moral and practical validity of capitalism. And when its deterioration into imperialism caused a clash between the European nations entailing unheard-of sacrifices by the common people, the ground was prepared for the voicing of new values and new concepts of society and the State.

During the First World War the production and distribution mechanism had to be adapted to meet very different needs from those of peace-time operation. The State took on new jobs and responsibilities and had to make the necessary adjustments to cope

with them. The principle that the good of the community should take precedence over the good of the individual and should be promoted even at the expense of the latter was extolled as a result of the war and has become one of the corner-stones of our political philosophy.

But along with the political and social upheavals, entirely new situations arose as a result of changes within the capitalist system itself and in its methods, giving a new course to the economy and modifying the sociological foundations.

The core of Liberal economic thinking was the entrepreneur's freedom of action. Since he was taking the risks inherent in the undertaking, it was up to him to organize production factors and determine returns. But the rise of the trade unions, increases in the size of the firm due to new techniques, and the nation-wide and world-wide links established between firms, were gradually changing this theory and the economic climate in which it had been conceived and practiced.

Thus we were to witness a widening gap between the ownership and management of companies, the growing dependence of firms on banks and finance houses and increasing competition by the biggest, most efficient and successful firms, which private interests offset by forming cartels.

Conditions were thus gradually becoming ripe for new forms of State intervention in the economy. If in the private sector, the entrepreneur's freedom of action is less and less equated by the assumption of risk, if the owner is increasingly displaced by the manager and if capital is raised from an ever-growing number of shareholders and a nameless host of savers via the capital market, there is no longer and reason to ban public enterprise and management from those economic spheres of major interest to the community. This is still more the case when Liberalism is no longer able to resolve its inner contradictions or control the forces it has set in motion and economic crises are rocking the foundations of society and the State.

II

These changes, already nascent before the First World War,

took shape in the unsettled period between the wars and reached a climax after the Second World War, giving rise in the West to a system under which democracy is trying to solve in freedom the problems of a society which is no longer capitalist but not socialist either.

The modern State, which, with the advent of universal suffrage has become representative of every citizen, is faced with immensely increased responsibilities but at the same time has more varied and better instruments for dealing with them.

As far as economic policy is concerned it is assisted by advances in economics enabling it to measure micro and macroeconomic phenomena with a certain precision and to apply brakes or incentives to mitigate the consequences of cyclical fluctuations. It is armed with technical, legal and administrative means – such as anti-trust laws and price controls – of ensuring that a given type of activity does not damage the interests of the community. It can also count on international solidarity and the support of international bodies which co-ordinate to some extent individual governments' policies and provide a common framework for the various countries' economies.

Balancing economic and social forces in defence of freedom, defending the interests of the many against the actions of the few, and above all promoting and maintaining economic progress – these are the aims which the State pursues both by means of general economic policy and direct intervention.

The varying extent and form of State intervention to be found in different countries are due to political factors, the pattern of society and the degree of development. In the United States and Germany, State intervention is almost entirely indirect, but this does not mean that there are not good grounds for more forceful government measures in other highly developed countries like the United Kingdom or France, or less advanced countries like Italy or in the emerging countries where State control in the main sectors of the economy is vital to the modernizing of a backward society and an embryo economy.

But it is not the situation of this last group of countries that is significant for the State's tendency to take on direct economic responsibilities. It is indeed more significant that this is happening

in industrialized and economically highly developed countries, because it is in these countries that the evolution of economic and social institutions can be gauged, the worth of new formulae tried out and new prospects outlined.

Theory and practice in these countries agree in giving public enterprise four essential aims:

- (a) the performance of public services which are vital to the life of the community, where what matters is that the service in question be carried out properly, regularly and economically;
- (b) the breaking up of monopolies, in defence of consumers' and business's freedom, and of political freedom where the monopoly or cartel creates a vast concentration of economic and political power;
- (c) economic development where there are unbalances between different parts of a country or different sectors, or a lack of vigour on the part of private enterprise;
- (d) control of the output of goods which are a basic factor in other production lines.

The means of achieving these aims and, therefore, the different legal forms and organization of undertakings give public enterprise in each country an individual stamp. And there are, of course, various methods of solving the problems of these undertakings' management, finance and control.

The first aim is fulfilled by the public administration of public utility undertakings – transport, communications, electricity, water gas – which are a special case not only because they operate in a situation of technical monopoly, but also because their public service character affects costs and tariffs and may imply their not being run on strictly business lines and thus receiving government subsidies.

A more interesting case is that of productive undertakings sponsored by the State to promote economic development, revive competition or for both these purposes. It is here that the greatest problems arise in the conduct of affairs.

III

I cannot dwell at length on individual countries' situations and

so I will take the Italian case in particular, for two main reasons apart from the fact that it is my country: because Italy offers a complete range of the various types of public economic intervention and because one of them is typically Italian and represents the most interesting example of State enterprise.

In Italy the State is engaged in economic activities through:

- (a) a number of autonomous undertakings which form part of its administrative organization and, therefore, have no distinct legal entity (State Railways, tobacco and salt monopolies, long-distance telephones, etc.);
- (b) a national electricity undertaking, similar to those set up in England and France.
- (c) A large number of companies: industrial, commercial, transport, banking, insurance, relating to spas and tourism, theatrical, mining, telecommunications and shipping, formed under the Civil Code and grouped under public holding companies with a separate legal entity.

These are the so-called "state holdings" – a group which is of the greatest interest as regards its legal set-up, its relation to the State and its economic function.

The problem which this formula sets out to solve is that of State-owned enterprise engaging in industry in competition with private enterprise, and operating for the public benefit under the rules of a free market economy.

The firms in which the Italian State has an interest are companies limited by shares, except that their capital is held by public holding companies set up by an Act of Parliament. The direction and control of these holding companies are in the hands of the Minister of State Holdings who is in the Cabinet and thus responsible to Parliament.

It goes without saying that where the State is concerned not with its specific political functions but with economic objectives, the undertaking formed to carry out these objectives must have freedom of action and the type of management which puts it on an equal footing with private enterprise. The State-owned corporation must be run for the public benefit on sound lines by a management unhampered by red tape and headed by men with business experience and a business mentality.

This basic concept of State holdings is not valid for all the existing undertakings. For this reason the problems that arise in a practical application of the concept – to which I shall refer later – are not the same in the different firms.

A large number of the State-owned corporations existing today in Italy came under State control not because the government, in pursuance of a given economic policy, deliberately formed or acquired them, but because, due to the vicissitudes of Italian capitalism in the twenties, it was forced during the world crisis to step in to avoid the collapse of the big banks and the many industrial firms they financed and controlled.

The *Istituto per la Ricostruzione Industriale* – I.R.I. (Institute for Industrial Reconstruction) was formed in 1933 to take over both the banks and the firms, put the latter's house in order and then return them to the private sector. But this proved impossible.

As there were objectively good grounds for the form taken by a large part of the State's business interests, the "state holding" became a system.

As regards *Ente Nazionale Idrocarburi* – E.N.I., for which I am responsible, this is briefly, how it came into being.

In 1926 the *Azienda Generale Italiana Petroli* – AGIP had been set up by charter, with the State and two large national insurance institutions holding the capital, but was organized and operated as a private company. AGIP's operations and results and those of other State ventures in petroleum exploration, refining and the marketing of petroleum products led around 1950 to the need to re-organize the whole sector in order to give it a unified policy and strengthen its potential. In 1953 an Act of Parliament set up *Ente Nazionale Idrocarburi* – E.N.I. which took control of the various companies in which the State had an interest and those subsequently formed as a result of the boost given by E.N.I. to operations in the oil, chemical and engineering industries.

I.R.I. and E.N.I. (which of course, means the group of limited companies each of them controls) are today the two outstanding examples of State holding in Italy.

They are known as multi-sectoral integrated groups or differentiated groups and their size, flexibility and vitality enable them to create the necessary conditions for carrying out the State's

aims, which the holding company must guarantee by its powers of control and the companies must put into effect.

The public character of E.N.I. is unmistakable because it stems from a clear-cut government decision in pursuance of an economic policy justified by the situation in its main sector of operation.

The importance of energy for economic development, inadequate home production of primary energy sources and the international character of the oil industry in fact forced Italy to seek the greatest possible independence from outside sources of supply and to obtain imports on the most advantageous terms. The E.N.I. Group was formed to achieve these aims and it is one of the many examples of State intervention in the oil industry.

IV

The problems of State holdings, which are partly common to other forms of State intervention, are varied and complex. They concern the definition of aims, the ways of achieving them and relations between the State and the undertakings. They are political, legal and economic problems, giving rise, of course, to lively and never-ending political and technical discussion which goes to show the importance of this type of intervention in the economy for the structure of society and the State.

I can only make some brief references.

It is not always easy to define the aims of a public undertaking or group of undertakings, and still less to decide how they are to be achieved, especially where such undertakings are operating in competition with private enterprise.

For this very reason the companies in which the State has an interest must be run on sound business lines. The opponents of State intervention in fact insist that they should behave like private firms, especially when the capital is partly public and partly private, as often happens. There is no doubt that to be run on sound lines means at least that a public enterprise should adopt all the practices and techniques of a well-run private firm. But the bone of contention is what should a public enterprise do in regard to the profit motive, which is the essence of private and which entails the use of certain criteria of management.

In view of the aims of public enterprise which I mentioned earlier, it is obvious that the profit motive cannot and should not be the main aim of a State-owned company. But this does not mean that it must be eliminated altogether or that it may not be a means to an end. For one thing the profit motive is a gauge of efficiency which cannot be overlooked if public enterprise is to be run on sound lines.

The crux of the matter is what price policy should a public enterprise adopt?

If it has been given the aim of restoring or stimulating competition in a given sector, it is felt that its prices must be fixed at a level which allows maximum use of production capacity and enough profit margin to give a return on capital, without providing additional income. But since private firms tend to adopt a price policy which enables them not only to obtain the funds they need for plant replacement and capital remuneration but also to set aside appropriations for future developments, public enterprise cannot forgo higher profits than will provide for mere capital remuneration unless it can be sure of finding the financing it needs on the market at reasonable rates or unless it can count on State backing. In some cases this may mean, as is happening in Italy, that the government is obliged to increase taxes to finance public enterprise.

If the aim of a public enterprise is to promote economic development in a particular region or sector, and it has to operate in uneconomic conditions such as private enterprise would reject, the State must provide a cushion of subsidies or else reduce costs. Unless it does this it is endangering the soundness of the enterprise as well as the aims it is pursuing. If it does so, it must be able to exercise the necessary controls to ensure that the enterprise does not sit back and cease to be efficient.

The problem I have just outlined is one of the most delicate. It is true to say that neither the various interpretations of the behaviour of private firms nor economic models are enough to give public enterprise practical guidance.

The attitude of public enterprise to the profit motive and the fixing of prices, as indeed to many other management problems, must be determined by a sober appraisal of all the facts and forecasts – national, international and of the particular sector, group and firm

– in relation to the aims to be achieved. To this end both the government's political and administrative bodies and the heads of the enterprise, with their business experience, must work together, each within their own sphere and responsibilities but in close harmony.

V

Here I should like to call attention to the immense importance of planning in this connection.

In those countries where it is found advisable to use public intervention to change the market mechanism with a view to adapting it to development aims, planning appears to be an essential instrument in rationalizing the choices of the public and private sectors in terms of the proposed aim. And when the public sector is already widespread and powerful, and the State can exert through it a profound influence on the whole economy, the plan becomes an instrument for making this sector to give the lead in pursuing the overall aims of the economy.

It is a matter of distinguishing between the public and private sectors, of laying down what each of them can and should do, but at the same time of co-ordinating their functions, and the administrative activities of the State as well, into a concerted and coherent whole.

Control of the public enterprises is one of the biggest problems in a mixed economy because it must be effective without being a bottleneck and because the usual political and bureaucratic bodies for controlling the State administration are not suited to controlling industrial firms. In Italy the problem has been solved by giving the Minister of State Holdings and Parliament overall political control and the group holding company the day-to-day control over the firms' activities. This avoids bureaucratic interference in the firm's affairs whilst ensuring their public character and aims and guaranteeing that they are run on sound lines.

The changes in the capitalist system which have given rise to the State's new functions are by no means over. Factors which have existed for some time have not yet produced all their possible effects and their full significance has not yet been grasped.

The gradual, continuous dwindling of money values, the falling off of individual saving and its replacement by public and business saving, the propensity to spend egged on by increasingly aggressive sales campaigns which mean that supply rather than demand determines production tendencies, are all a clear indication in advanced societies of a decline in traditional values and relations. Fundamental institutions of the old legal and social order – such as private property – are on the downgrade. The chief political theories of the last century are becoming less and less representative of the economic and social reality and less and less capable of inspiring the policies of the various parties. Power is derived from different forces and expressed in different terms from formerly.

Public intervention in the economy is a result of these changes, but is inevitably affected by their incompleteness. Public enterprise is an instrument of this intervention, but only an instrument. It cannot lay down its own objectives and must take its place in a system of institutions intended to achieve and defend the aims and values of society, just as private enterprise must come within the same framework if its size and type of operation give it a considerable influence on the economic and political life of the nation.

VI

The capitalist world is going through a phase of transition and uncertainty. At the same time a process of revision is going on in the collectivist camp which is beginning to lose ground as a point of reference for the social currents which in the West have thoroughly upset the old equilibrium.

For the developing countries, which have recently entered a new phase in their history, these happenings can serve as a valuable example. Their problems are quite different from those of the older and more advanced countries and their solutions will also be different. But they can make their choices in the light of what has occurred elsewhere and thus perhaps avoid costly experiments.

The various ways in which the West is attempting to find a happy medium between freedom and social purpose in business show that the old capitalist world is trying to progress without turning everything upside down. Not all these ways are equally applicable

or appeal equally to the developing countries.

A formula based, as in the Italian experiment, on firms which have to be efficient because they are operating a competitive market, aims at the distribution of resources and the regulation of capital formation in the interests of economic development. The firms are part of the free market system but affects its mechanism. In other western countries with the highest national product in the world public enterprise does not to any great extent affect the market mechanism, but only removes certain activities, generally in the category of public utilities, from the private sector by means of nationalization.

For a country like India, which already has a vast and expert executive class and is already fairly industrialized, the need for a strong public enterprise would not appear incompatible with a system encouraging the spread of managerial ability within the public sector.

Government action and the Plan ensure that the economy is geared to a socialist pattern of society. "Speedy decisions and a willingness to assume responsibility – decentralization of authority and management along business lines" are the four characteristics which the 1956 Government of India Resolution on Industrial Policy ascribes to public enterprise. It is just these characteristics that distinguish the Italian State holding system from other western public enterprise formulas and make it an up-to-date and efficient instrument of economic progress in a free society.