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The economic consequences of Mr. Volpi: An analysis of "quota 90"

Las consecuencias económicas del Sr. Volpi: un análisis de la "quota 90"

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A N A L Y T I C A L   S U M M A R Y

In 1926/27 the fascist government fixed the exchange rate of the lira against the pound at 90:1 (the so-called "quota 90"), causing a revaluation. This decision was part of a broader plan to return to the Gold Exchange Standard, which characterized the interwar period. Traditionally, the literature has been mostly interested in the causes of "quota 90", the international relations behind this decision, and the policy change represented by the substitution of Mr. de' Stefani with Mr. Volpi at the helm of the Treasury, without delving into a formal analysis. This paper attempts to fill this gap in the literature by providing an econometric analysis of the effects of changes in the terms of trade on GDP, and of the price deflation through wage reduction that occurred, using data from 1911 to 1939. We identify the average effect, which is used to interpret the economic consequences of the revaluation of the lira.

We first analyze the time-series properties of the variables involved in the study and find that GDP and terms of trade are I (1) then, using the Johansen cointegration test, we find that a long-run relationship between them exists. Second, through a Vector Error Correction Model, we investigate the short-term adjustment and find that the adjustment to a terms of trade shock is relatively fast. Taken together, these results maintain that the effects of "quota 90" were mild. Third, Granger-causality tests show that changes in terms of trade anticipate changes in wages, supporting the idea that the weakening of the trade unions was a source for regaining competitiveness. In fact, the implementation of "quota 90" was preceded by labor market reforms that tilted the balance in favor of the firms. This is not surprising: had the terms-of-trade remained unadjusted, a balance of payment crisis would have emerged, with the likely relinquishment of the newly gained membership to the Gold Exchange Standard. Political considerations outweighed economic concerns: "quota 90" was the way that the fascist government sought to gain some international standing in the wake of the return to the Gold Standard system.

We perform some robustness checks that support the main conclusions of the baseline estimates. However, given the limited sample size and the related need to estimate the most parsimonious models, some caution should be taken in interpreting the results, which we should take as the first evidence that challenges some of the received wisdom of the qualitative literature.