Working Paper Series
Department of Economics
University of Verona

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**Abstract**

This paper explores aggregate profitability in Italy from 1994 to 2005 in its connection with structural change and gender employment disparities. The aggregate profit rate declined, but the profit share did not so. Male variables tend to have more weight than female ones in explaining aggregate outcomes. Structural change had a major role too, as the economy specialized in sectors with falling real wages and wage shares, the financial sector especially. Further falls in the wage share and widening wage gaps may not guarantee a rise in profitability.

## Introduction

The present paper investigates the connection between gender employment disparities, structural change and aggregate profitability in Italy from 1994 to 2005, namely before its present long crisis[1].

This is interesting for a number of different reasons. The current dramatic situation of the Italian economy was already effectively depicted in the literature. According to Pianta (2012), this is the result of economic decline, financialization, power relations favouring capital over labor and pro-rich public policies. Many of these trends are common to most advanced countries, but Italy "stands out as an extreme case of decline and privilege". Also the association of Italian firms warns that recession, credit crunch and low profitability put in danger strategic economic activities. Italy is less and less able to keep the pace of emerging countries on international markets (Confindustria, 2012). The present depression has old roots. We show that the weakness of the Italian economy was already evident in our period of observation and we highlight its gender dimension connected to functional income distribution and structural change.

In the second place, we contribute to a recent stream of literature that nested structural change analysis in studies on aggregate profitability dynamics (Wolff, 2003 and Vaona, 2011)[2]. We do so by following in particular the example of Zacharias and Mahoney (2009), which is our main reference. To our knowledge, this study was the first one to highlight gender issues in the connection of structural change and aggregate capital profitability. Their main findings are four.

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[1] The choice of our period of observation is dictated by the availability of data on the unadjusted gender wage gap. However, the years 1994 and 2005 were similar regarding their business cycle position as the economy was recovering from economic recessions.

[2] Studies on the dynamics of the aggregate profit rate have been recently extensively reviewed in Vaona (2011).

First, the increase in the US profit rate from 1982 to 1997 went hand in hand with a decline in the labour share of income. This aggregate trend, however, hides gender differences. Male variables had more weight than female ones in aggregate distribution dynamics, given that the male wage share decreased and the female wage share increased. Structural change played a minor role as opposed to distributional shifts within sectors and in the service sector especially, where productivity decline outstripped wage decline - helping to explain the change in the female wage share.

What distinguishes our contribution from Zacharias and Mahoney (2009) is that they focus on a success story in terms of profitability - the US from 1982 to 1997 - while, unfortunately, we focus on a failure. In this way it is possible to contrast the Italian experience with a benchmark and to check whether the developments highlighted in our main reference also held in a country experiencing a sharp decline in the aggregate profit rate.

The rest of this work is structured as follows. The next section illustrates our definitions and data sources. We then highlight trends in both aggregate profitability and in gender aspects of the functional distribution of income. Before concluding we assess the different roles of distributional and compositional shifts.

## Data sources, definitions and methodology

Regarding the long-term trend of the aggregate rate of profit, our data sources were the OECD STAN database and data from the Italian national statistical agency (ISTAT). For the trend in the labor share of income, we also rely on Eurostat data.

From the OECD STAN database we consider the following variables: gross income at current prices (PROD), the gross GDP deflator (PRDP), labor costs (LABR), total employment (EMPN), the number

of employees (EMPE), gross operating surplus and mixed income (GOPS). Variables from national statistics are the gross capital stock at current replacement cost (GROSSK) and the deflated gross capital stock (GROSSKR).

We neglect the public sector, by focusing solely on private activities. We correct the variable GOPS for the income of the self-employed as below:

$$GOPS' = GOPS - (LABR/EMPE) * (EMPN - EMPE) \qquad (1)$$

where GOPS' is our measure of total profits ($\pi$).

The total wage bill (*wn*), gross real and nominal incomes (GNI and GNIR respectively) are computed as follows:

$$wn = LABR + (LABR/EMPE) * (EMPN - EMPE) \qquad (2)$$

$$GNI = GOPS' + wn \qquad (3)$$

$$GNIR = GNI/PRDP \qquad (4)$$

Aggregate variables are the sum of sectoral ones. The sectors considered in our analysis are: agriculture, hunting and forestry; fisheries; mining and quarrying; food, beverages and tobacco; textile and clothing industries; leather and leather products; wood and wood products; paper, printing and publishing; chemical products; non-metallic mineral products; metallurgy and metal products; machinery and equipment; transport equipment; other manufacturing industries; electricity, gas and water supply; construction; wholesale trade, retail trade and repairs; hotels and restaurants; transport, storage and communication; financial intermediation; real estate and business activities.

We define the aggregate profit rate as the ratio between GOPS' and GROSSK. We use gross variables because Vaona (2011) showed that gross and net profit rates had similar trends in Italy in the period under observation[3].

Our variables to study the labour share of income disaggregated by gender are the unadjusted gender wage gap[4] in percentage for the period 1994-2005 ($\delta$), the average working hours of male

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[3] For theoretical arguments about properly measuring profit rates see, for instance, Mueller (1990), Shaikh (199) and Duménil and Levy (2002a, b). Similar trends regarding gross and net profit rates were also found by Wolff (2003) and Vaona (2011).

and female employees by industry[5], and total employment by gender and industry for 15-74 years old workers. We focus on the unadjusted wage gap because we want to study the trend of the actual female wage share and not the one it would have had if men and women were all equal but for their gender[6].

In order to obtain average working hours by gender at the aggregate level ($L^m$ and $L^f$), we consider the same economic sectors as above and we weight average sectoral weekly working hours by the employees of each industry. Finally, we multiply the result by the number of weeks in a year.

Average nominal wages by gender ($w^m$ and $w^f$) are obtained below. Consider that the average hourly wage ($w$) is

$$w = wn/(L^m + L^f) \tag{5}$$

On the basis of the definition of percentage gender wage gap, one has

$$w^f = (1 - \delta)w^m \tag{6}$$

Bearing in mind that

$$w = \frac{w^m L^m + w^f L^f}{(L^m + L^f)} = \frac{w^m L^m + (1-\delta)w^m L^f}{(L^m + L^f)} \tag{7}$$

there follows

$$w^m = \frac{wn}{L^m + (1-\delta)L^f} \tag{8}$$

Under the methodological point of view, we rely on decompositions which are based on a simple identity. If *y=ab*, then *y_{t=2}- y_{t=1}=a^\*(b_{t=2}-b_{t=1})+b^\*(a_{t=2}-a_{t=1})*, where *t* is a time index and asterisk variables are average values between time 1 and 2. Details on the specific computations we perform are given before introducing our results. Decomposition is an accounting technique and it cannot *per se* highlight causal relationships. Economic interpretation is needed to gauge results.

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[4] Eurostat offers this definition: "The unadjusted Gender Pay Gap (GPG) represents the difference between average gross hourly earnings of male paid employees and of female paid employees as a percentage of average gross hourly earnings of male paid employees". GPG data are based on the Structure of Earnings Survey (SES). They are released about 12 months after the end of the reference period.

[5] We consider the same sectors used to compute the aggregate profit rate (NACE rev. 1.1; A-K).

[6] The adjusted gender-wage gap did not have completely different order of magnitude and dynamics than the un-adjusted one (see Dal Prete, 2012).

Under this respect, however, regression analysis is not superior in itself, given that correlation does not imply causality. Economic reasoning, often in the form of model specification, exclusion restrictions and instrument choice, is often necessary in the assessment of regression results too.

## Trends in profitability

The main focus of this paper is assessing the dynamics of the aggregate profit rate (*r*) and share on the eve of Italy's long crisis. Figure 1 gives a picture of these variables. As it is possible to see both variables increased up to 2001 and then they started to decrease. However, at the end of the period of observation, the profit share was still above its 1994 level, but the profit rate was well below it. How to explain this outcome?

**Figure 1 - Gross profit rate (left scale) and share (right scale) in Italy (1994-2008).**
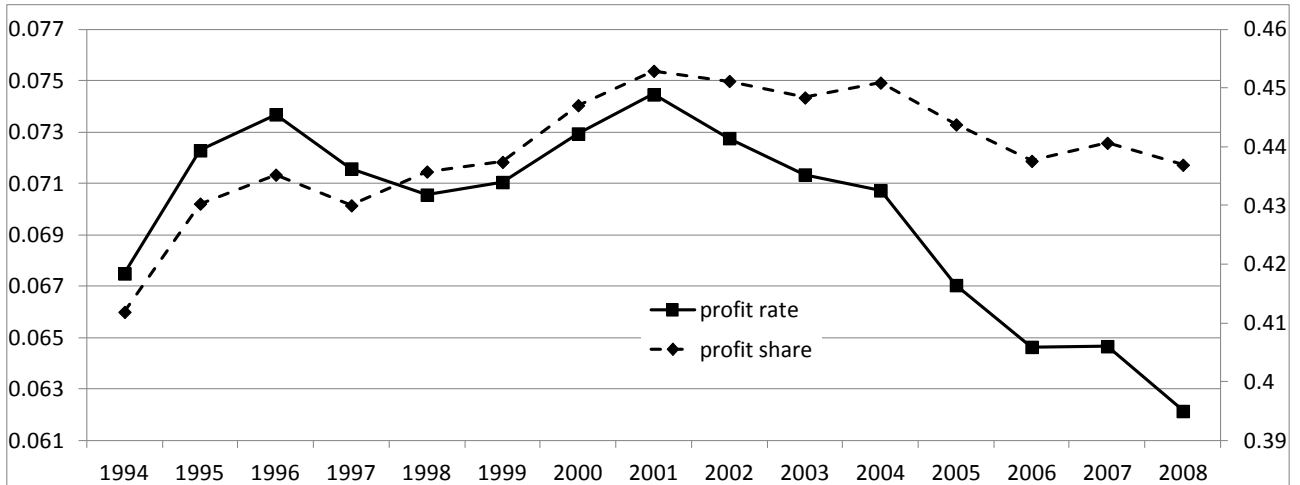


Decomposition analysis offers some more hints. Let us consider the following equation

$$r = \frac{\pi}{p_k k} = \frac{\pi}{p_y y} \frac{y}{k} \frac{p_y}{p_k} \tag{9}$$

where $\pi$ are profits, $k$ is GROSSKR, $p_y$ is PRDP and $p_k = \frac{GROSSK}{GROSSKR}$.

The percentage change of *r* can be decomposed into three terms

$$\frac{r_2 - r_1}{r_1} = \frac{(\pi/p_y y)|^*(p_y/p_k)|^*(y/k|_2 - y/k|_1)}{\pi/p_y y|_1 \, p_y/p_k|_1 \, y/k|_1} + \frac{(p_y/p_k)|^*(y/k)|^*\left(\pi/p_y y|_2 - \pi/p_y y|_1\right)}{\pi/p_y y|_1 \, p_y/p_k|_1 \, y/k|_1} +$$

$$+ \frac{(\pi/p_y y)|^*(y/k)|^*\left(p_y/p_k|_2 - p_y/p_k|_1\right)}{\pi/p_y y|_1 \, p_y/p_k|_1 \, y/k|_1} \tag{10}$$

The first term accounts for the portion of the percentage change in the profit rate that can be attributed to the output-capital ratio, the second term to the profit share of income and the third one to the relative price of output and capital goods.

Table 1 contrasts the results that can be obtained for the US from 1982 to 1997, with those that it is possible to obtain for Italy from 1994 and 2005. The success of the US can be attributed mainly to an increase in the productivity of capital goods, which was accompanied by favourable developments not only in the profit share but also in the relative price of output and capital goods.

**Table 1 - Decomposition of the change in the gross profit rate in the US and in Italy (% points)**

| Country | US | Italy |
|---|---|---|
| Years | 1982-1997 | 1994-2005 |
| Actual change in gross profit rate | 9.92 | -0.67 |
| Contribution of: | | |
|     change in profit share | 1.97 | 7.45 |
|     change in real output-capital ratio | 5.39 | -7.45 |
|     change in relative price of output and capital goods | 2.56 | -0.67 |

Notes: figures about the US are from Zacharias and Mahoney (2009) and they are here reproduced to the reader's convenience.

Italy had a considerably different pattern. Notwithstanding a sizeable positive effect arising from the profit share, the profit rate declined due to the negative effects coming from the output capital ratio and capital goods becoming more expensive compared to output.

It is difficult to escape the interpretation that firms were unable to convert a considerable distributional windfall into innovative products and processes. On this ground, tracing the present long crisis to features of the Italian labor market seems questionable.

We now move to consider what role gender issues played in this picture.

## Women's employment and functional distribution

According to the Italian government and the Italian national statistical office (ISTAT), the Italian economic system is characterized by one of the lowest employment rates at the European level (Presidenza del Consiglio dei Ministri, 2010). In 2008 it was equal to 58.7%, 7 points below the European average. For women it was even lower (47,2%), 12 points below the corresponding European average. Such aggregate figures hide considerable regional divides, as in the South and Islands female employment rates can be 20 percentage points lower than in the North and in the Centre of Italy.

**Figure 2 - Share of women in total employment and hours worked in Italy (in percent), 1994-2005.**
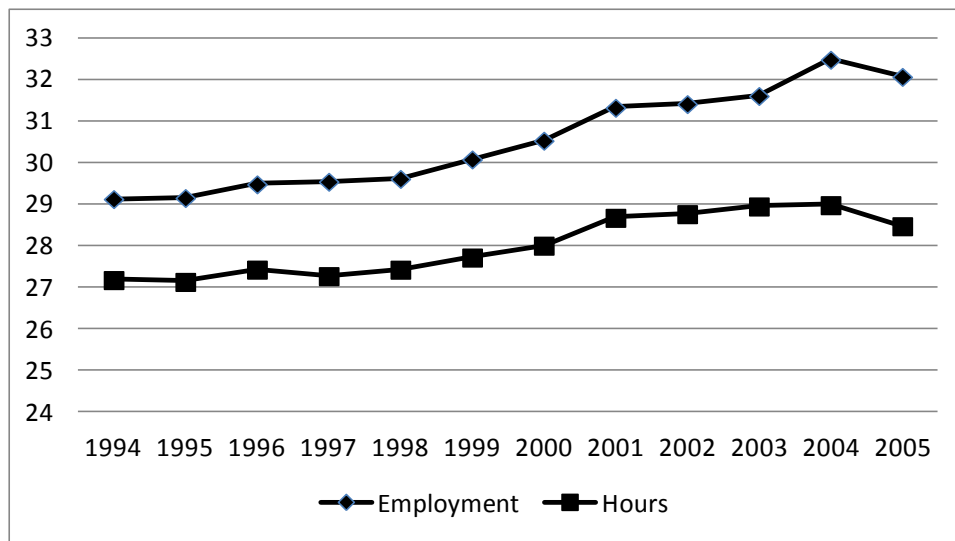


A similar gender divide can be found in the duration of the working life. Men work on average 35 years, while women 24. When it comes, however, to the unadjusted wage gap, during the period of observation it averaged - according to Eurostat data - at about 7.4%, while, for instance, in the countries belonging to the Euro area it was 15%.

Figure 2 shows two indicators of the relative role of women in the Italian economy as compared to that of men over the period of observation. The share of women in total employment and in worked hours increased. However, such an increase was more muted for the latter variable. Therefore, also the Italian workforce experienced an increasing feminization. Zacharias and Mahoney (2009) point to a number of different causes for this phenomenon in the US, including an attempt to defend family living standards from declines in male compensation, social and educational factors changing women's preferences, declines in fertility and marriage rates and increases in the rate of divorces. The Italian society went through similar changes in the past decades.

Regarding real hourly labor compensation, the gap between men and women did not dramatically change over the period of observation as showed by Table 2, though it recently reversed its previous downward trend. It was 8% in 1994, 7% in 1998, 6% in 2001 and 9% in 2005. What is worth mentioning is that with difference to the US from 1982 to 1997, where the average real hourly compensation increased, in Italy it was lower in 2005 compared to 1994.

**Table 2 - Average real hourly compensation by gender (in 2000 Euros), selected years**

| Year | 1994 | 1998 | 2001 | 2005 |
|---|---|---|---|---|
| Average | 13.87 | 14.15 | 14.05 | 13.75 |
| Men | 14.18 | 14.42 | 14.30 | 14.11 |
| Women | 13.04 | 13.41 | 13.44 | 12.84 |

We now move to consider a decomposition of the aggregate wage share in Italy able to account for gender differences and to contrast our results with our benchmark.

The wage share of income ($\omega$) is composed of two terms: labour per euro of real income (L/Y)- the inverse of labor productivity - and the real wage (w/$p_y$). Our aim is to disaggregate these terms by gender

$$\omega = \frac{w^m}{p_y}\frac{L^m}{Y_r} + \frac{w^f}{p_y}\frac{L^f}{Y_r} = w_r^m \lambda^m + w_r^f \lambda^f \tag{11}$$

where $w^m$ and $w^f$ are the average hourly wage for men and women respectively, $L^m$ and $L^f$ are male and female working hours, $Y_r$ is real gross national income and $\lambda^m$ and $\lambda^f$ are the female and male labour ratios. The index $r$ denotes real variables.

If $y = ab + cd$, then

$$\frac{y_2 - y_1}{y_1} = \frac{[a^*(b_2-b_1)+b^*(a_2-a_1)]+[c^*(d_2-d_1)+d^*(c_2-c_1)]}{(a_1 b_1)+(c_1 d_1)} \tag{12}$$

where $a^* = \frac{(a_1+a_2)}{2}$, $b^* = \frac{(b_1+b_2)}{2}$, $c^* = \frac{(c_1+c_2)}{2}$, $d^* = \frac{(d_1+d_2)}{2}$ and indexes denote time periods.

As a consequence, one can write:

$$\frac{\omega_2-\omega_1}{\omega_1} = \left[\frac{w_r^m|^*(\lambda_2^m-\lambda_1^m)}{w_{r,1}^m \lambda_1^m+w_{r,1}^f \lambda_1^f} + \frac{\lambda^m|^*(w_{r,2}^m-w_{r,1}^m)}{w_{r,1}^m \lambda_1^m+w_{r,1}^f \lambda_1^f}\right] + \left[\frac{w_r^f|^*(\lambda_2^f-\lambda_1^f)}{w_{r,1}^m \lambda_1^m+w_{r,1}^f \lambda_1^f} + \frac{\lambda^f|^*(w_{r,2}^f-w_{r,1}^f)}{w_{r,1}^m \lambda_1^m+w_{r,1}^f \lambda_1^f}\right] \tag{13}$$

where $w_r^m|^* = \frac{(w_{r,1}^m+w_{r,2}^m)}{2}$, $\lambda^m|^* = \frac{(\lambda_1^m+\lambda_2^m)}{2}$, $w_r^f|^* = \frac{(w_{r,1}^f+w_{r,2}^f)}{2}$, $\lambda^f|^* = \frac{(\lambda_1^f+\lambda_2^f)}{2}$.

Table 3 sets out our results regarding the decomposition above. The decline in the wage share in Italy was about twice as big as that of our benchmark. This was mainly the result of the increase in male labour productivity, whose effect was ten times larger compared to the effect of real male compensation. Female variables had a smaller magnitude, but both the decline in the real wage of

women and the increase in their productivity contributed to decreasing the wage share. This is in contrast with the US experience. There the gap between the contributions of increases in productivity and real compensation was proportionally much smaller for men. Women instead managed to secure a rising wage share, thanks to a positive contribution of real compensation outstripping the negative one by their labor ratio. Bearing in mind the persistent fall in capital profitability discussed above, the Italian story is clearly one of a decline marked by either falling living standards and productivity or by living standards unable to keep the pace with productivity growth[7].

**Table 3 - Decomposition of the change in the US and Italian wage shares (% points)**

| Country | US | Italy |
|---|---|---|
| Years | 1982-1997 | 1994-2005 |
| Actual change in wage share | -2.73 | -5.43 |
| Contribution of | | |
|     change in male hourly compensation | 4.03 | 0.48 |
|     change in female hourly compensation | 4.41 | -0.11 |
|     change in male labor ratio | -8.59 | -5.49 |
|     change in female labor ratio | -2.59 | -0.30 |

Notes: figures about the US are from Zacharias and Mahoney (2009) and they are here reproduced to the reader's convenience.

## Distributional shifts and compositional shifts

The present section is devoted to answering two questions. Our first question is to what extent the trend highlighted above was due to the Italian economy shifting from sectors with high wage shares to sectors with low wage shares. Our second question is whether industry gender dynamics were either similar or different to aggregate ones.

In order to answer our first question, we notice that the aggregate wage share is equal to the sum of the industry ones weighted by industry shares in total value added. Therefore we can apply a similar decomposition to those explained above (see equation 12).

In this section we aggregate sectors so to make our results comparable to those in Zacharias and Mahoney (2009), where it was found that, in the US, structural change contributed to the wage share dynamics only by 10% between 1982 and 1997. Table 4 shows that it had a much greater role in Italy from 1994 to 2005, when the economy was shifting from sectors where income

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[7] Zacharias and Mahoney (2009) also provide counterfactual analyses by keeping the gender wage gap and the share of women in total working hours at their initial level. Similar exercises were performed by Tescari (2012), however, since these variables did not markedly change over the period of observation, actual results are not dramatically different from counterfactual ones.

distribution had a positive contribution to the aggregate wage share - especially manufacturing and trade - to sectors with negative contributions - especially financial intermediation.

**Table 4 - Decomposition of the change in the aggregate wage share in the US by sector (in % points), 1994-2005**

| Sector | Total contribution of the sector to the change in aggregate wage share($\kappa_i$) | Contribution of the change in the sector's | |
| --- | --- | --- | --- |
| | | Share in value added ($\gamma_i$) | Wage share ($\omega_i$) |
| *Agri* | -1.99 | -1.32 | -0.67 |
| *Min-Quar* | -0.05 | -0.10 | 0.05 |
| *Mfg* | -4.03 | -5.29 | 1.26 |
| *Elec* | -0.81 | -0.22 | -0.60 |
| *Const* | 0.34 | 0.61 | -0.28 |
| *Trade* | -0.60 | -2.20 | 1.60 |
| *Transp* | -0.99 | 0.74 | -1.73 |
| *FIRE* | 2.70 | 4.71 | -2.02 |
| Total | -5.43 | -3.05 | -2.38 |

Notes: *Agri*=agriculture, hunting, forestry and fishing; *Min-Quar*=mining and quarrying; *Mfg*=manufacturing; *Elec*=electricity, gas and water supply; *Constr*= construction; *Transp*= transportation, communication and public utilities; *Trade*= wholesale and retail trade; repair of motor vehicles, motorcycles and personal and household goods, restaurants and hotels; *FIRE*= financial intermediation, real estate, renting and business services.

Such shift involved also women as testified by Figure 3, that concerns the distribution of women's worked hours across sectors in 1994 and in 2005. It is also worth noting that while the female real compensation was marginally increasing in manufacturing activities, in financial activities it was markedly decreasing (Figure 4).

Figure 5 makes instead clear that male variables had a greater effect than female ones, with the sole exception of the sector "wholesale and retail trade, repair of motor vehicles, motorcycles and personal and household goods, restaurants and hotels".

Inspecting Table 5, it is possible to compare gender dynamics at the sectoral level. Male and female variables tend to have qualitatively similar contributions on the wage share. The only two exceptions are electricity, gas and water supply and transportation, communication and public utilities, where female productivity decreased over the period of observation, while that of men increased.

**Figure 3 - Distribution of women's total hours of market work in Italy by sector in 1994 and 2005 (in percent)**
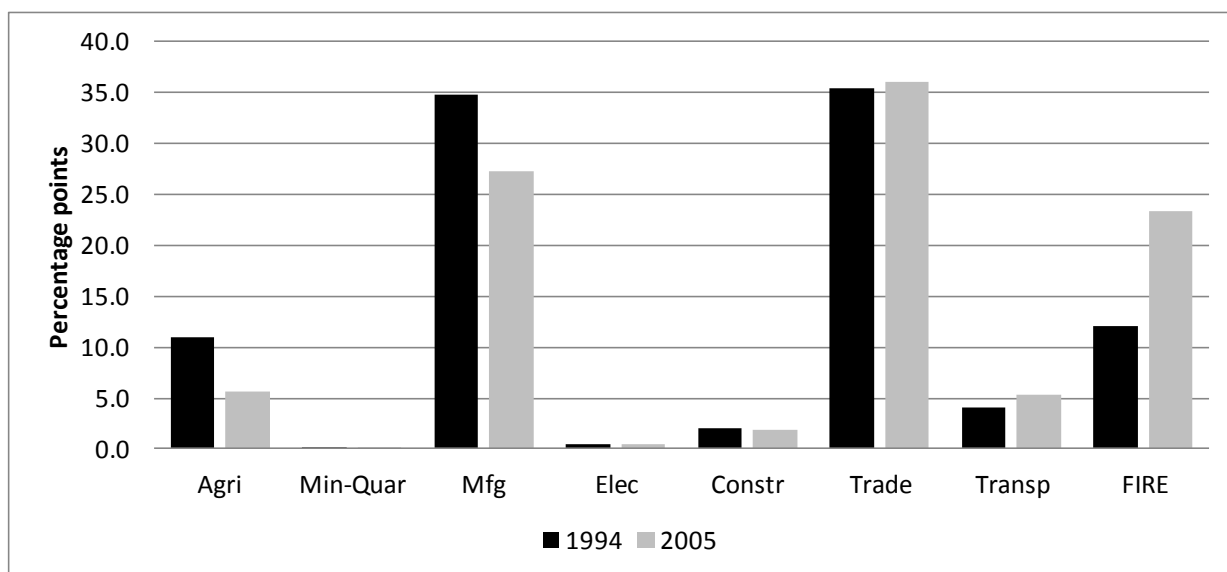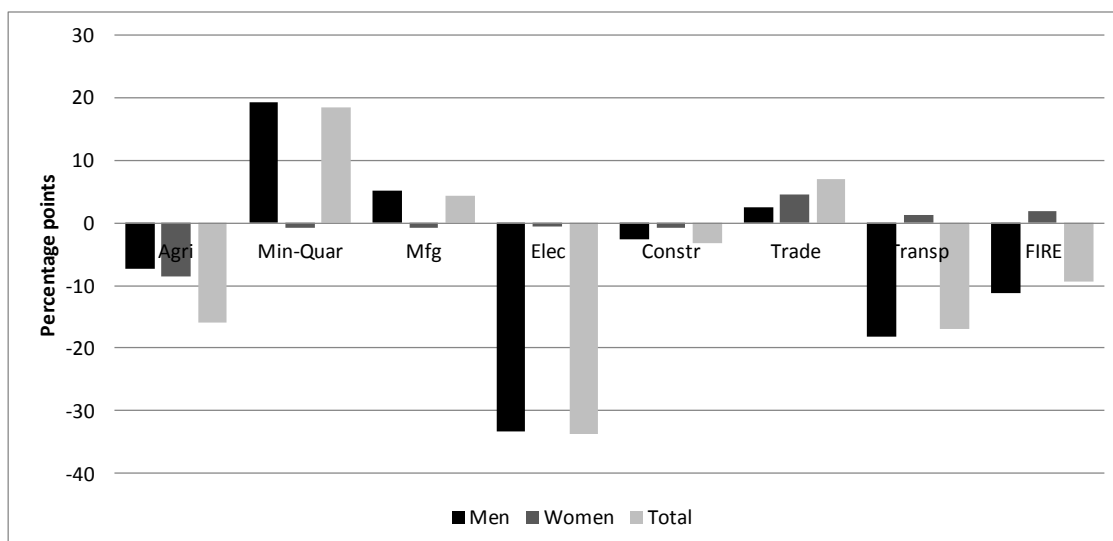


Notes: *Agri*=agriculture, hunting, forestry and fishing; *Min-Quar*=mining and quarrying; *Mfg*=manufacturing; *Elec*=electricity, gas and water supply; *Constr*= construction; *Transp*= transportation, communication and public utilities; *Trade*= wholesale and retail trade; repair of motor vehicles, motorcycles and personal and household goods, restaurants and hotels; *FIRE*= financial intermediation, real estate, renting and business services.

**Figure 4 - Women's real hourly compensation by sector in Italy, 1994 and 2005 (in 2000 Euros)**
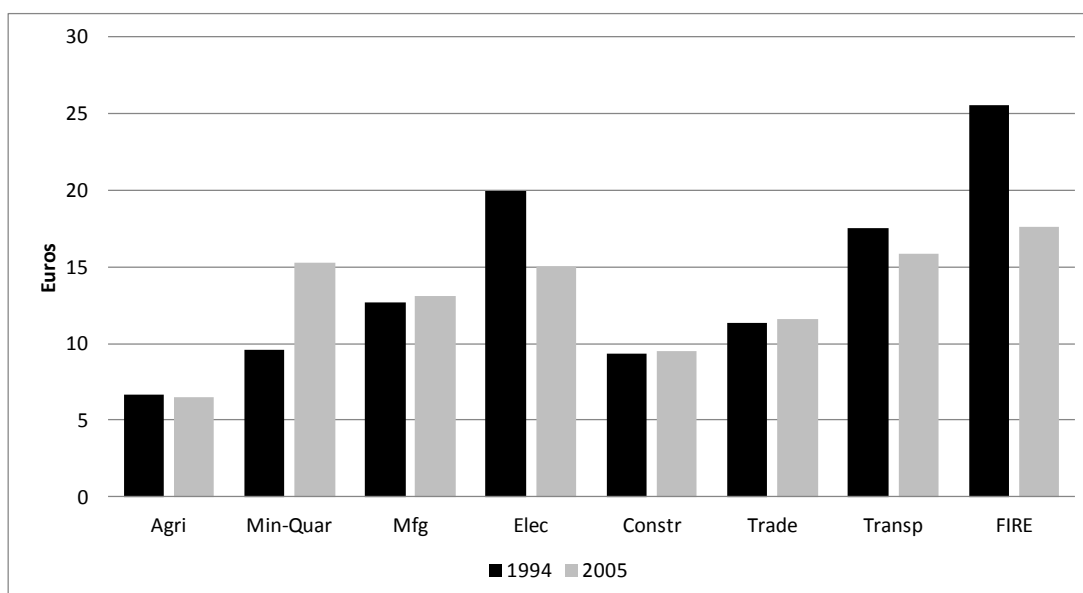


Notes: *Agri*=agriculture, hunting, forestry and fishing; *Min-Quar*=mining and quarrying; *Mfg*=manufacturing; *Elec*=electricity, gas and water supply; *Constr*= construction; *Transp*= transportation, communication and public utilities; *Trade*= wholesale and retail trade; repair of motor vehicles, motorcycles and personal and household goods, restaurants and hotels; *FIRE*= financial intermediation, real estate, renting and business services. Compensation were deflated by the aggregate gross output deflator.

**Figure 5 - Contribution to the total change in wage share between 1994 and 2005 by men and women in Italy, by sector (in % points)**



Notes: *Agri*=agriculture, hunting, forestry and fishing; *Min-Quar*=mining and quarrying; *Mfg*=manufacturing; *Elec*=electricity, gas and water supply; *Constr*= construction; *Transp*= transportation, communication and public utilities; *Trade*= wholesale and retail trade; repair of motor vehicles, motorcycles and personal and household goods, restaurants and hotels; *FIRE*= financial intermediation, real estate, renting and business services.

In five out of the eight sectors considered the wage share declined. However, underlying tendencies were diverse. In agriculture, hunting, forestry and fishing and in construction this was the result of the contribution of productivity growth outstripping the one of real hourly compensation.

In electricity, gas and water supply and in transportation, communication and public utilities the wage share declined mainly because of falls in real compensations coupled with increasing male productivity. In both the cases, female labor ratios had a positive impact on the wage share. The absolute size of such impact was though smaller than that of real compensation in the former sector and greater in the latter one.

The finance sector is different than those above. There real compensations had a negative impact on the wage share and the labor ratio a positive one. The ultimate fall in the wage share was due to male variables, given that the contribution of the labor ratio was not too far in absolute terms from that of their real wage.

**Table 5 - Decomposition of the change in sectoral wage shares in Italy (in % points), 1994-2005**

| Sector | Contribution to the change in wage share from change in: | | | | Actual change in wage share |
| --- | --- | --- | --- | --- | --- |
| | Labor ratios | | Real hourly compensation | | |
| | Male | Female | Male | Female | |
| *Agri* | -22.36 | -13.97 | 14.94 | 5.38 | -16.01 |
| *Min-Quar* | -33.75 | -6.5 | 53.04 | 5.65 | 18.44 |
| *Mfg* | -1.58 | -2.92 | 6.71 | 2.07 | 4.27 |
| *Elec* | -12.61 | 1.76 | -20.62 | -2.35 | -33.81 |
| *Const* | -6.22 | -0.8 | 3.59 | 0.12 | -3.31 |
| *Trade* | -7.65 | -0.36 | 10.17 | 4.84 | 7.01 |
| *Transp* | -1.72 | 4.65 | -16.45 | -3.38 | -16.9 |
| *FIRE* | 8.36 | 12.6 | -19.57 | -10.72 | -9.33 |

Notes: *Agri*=agriculture, hunting, forestry and fishing; *Min-Quar*=mining and quarrying; *Mfg*=manufacturing; *Elec*=electricity, gas and water supply; *Constr*= construction; *Transp*= transportation, communication and public utilities; *Trade*= wholesale and retail trade; repair of motor vehicles, motorcycles and personal and household goods, restaurants and hotels; *FIRE*= financial intermediation, real estate, renting and business services. In this table the hourly compensation was deflated by the sector specific gross output deflator.

In the remaining three sectors - mining and quarrying, manufacturing, wholesale and retail trade - the wage share increased due to a positive contribution of real compensation not offset by productivity growth. In the last sector this pattern held true both for men and for women. In the first two, instead, women's real compensation had a smaller contribution in absolute terms than productivity growth.

## Conclusions

The present paper investigates the trend of aggregate capital profitability in Italy on the eve of its present long crisis, also in the light of structural and gender changes. We show that a decline in profitability started at least in 2001. This can hardly be traced back to the strength of labor over capital as the profit share was higher in 2005 compared to 1994.

We contrast these results with those that were obtained for the US between 1982 and 1997, a period of rising profitability. Similarly to that experience, male variables drove aggregate trends more than female ones. However, differently to the US, structural change had a major role, as the economy specialized in sectors where real wages and wage shares were falling. The financial sector was particularly important in this development.

On the ground of these distributive patterns, it is fair to conclude that declines in the labor share of income are not a sufficient condition for restoring capital profitability. Therefore, widening the gender wage gap in Italy, even if it contributed to increase the female employment rate, would not *per se* guarantee economic success.

Italy in fact experienced a long-term realization failure on grand scale. By international standards, this country customarily ranks very low in indicators of innovation performance. It is important for this economy to recover competitiveness by filling its considerable innovation gap vis à vis other developed countries (Bugamelli et al., 2012).

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