



Italy.

Europe's Investment Opportunity

A White Paper by:

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Why Italy Matters to the World

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ABOUT THE AUTHORS

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Professor Vietor is the Paul Whiton Cherington Professor of Business Management at the Harvard Graduate School of Business Administration and Senior Associate Dean for the Asian Initiative. He teaches courses on the international political economy. He received a B.A. in economics from Union College (1967), an M.A. in history from Hofstra University (1971), and a Ph.D. in history from the University of Pittsburgh (1975).

Before coming to the Business School in 1978, Professor Vietor held faculty appointments at Virginia Polytechnic Institute and the University of Missouri at Columbia. He is the recipient the Newcomen Award in business history and served as President of the Business History Conference in 1993-94.

Professor Vietor's research on business and government policy has been published in numerous journals and books. His books include *Environmental Politics and the Coal Coalition* (1980), *Energy Policy in America Since 1945* (1984), *Telecommunications in Transition* (1986), *Strategic Management in the Regulated Environment* (1989), *Contrived Competition: Regulation and Deregulation in America* (1994); *Business Management and the Natural Environment* (1996); *Globalization and Growth: Case Studies in National Economic Strategies* (2004); *Environmental Protection and the Social Responsibility of Firms* (eds. With Bruce Hay and Robert Stavins) (2007); and *How Countries Compete* (2007); *The Class Moves the World* (2010).

For his courses in business-government relations and environmental management, Professor Vietor has published more than ninety case studies on energy policy, the regulation of transportation, telecommunications and financial services; and on the national development strategies of a dozen countries. He has been a consultant to the Hudson Institute and the Energy Research and Development Administration, serves on the Advisory Boards of IPADE (in Mexico), IESE (in Spain), INALDE (in Columbia), the Luigi Gerardo Napolitano Society (in Italy), and several firms. He is a consultant the Prime Minister of Malaysia.

Professor Alberto Onetti



Alberto Onetti is Professor of business administration and innovation management at the Department of Economics of the Insubria University. He is Head of the CrESIT (Research Centre for Innovation and Life Science Management) since its inception. He acts as Pro-Rector for innovation and academic high-tech spin-offs and leads the Ticino Valley Bio- and Life Science Cluster.

Since 2006 he has been Visiting at San Francisco State University. Since 2009 Alberto is Board Member and Chairman of Mind the Bridge Foundation, the California non-profit organization that connects the most innovative Italian startups with Silicon Valley's partners and investors.

Along the years, Alberto Onetti has developed in-depth expertise in the areas of management and corporate finance. He acts as consultant for leading banking groups and for Italian and multinational companies and sits on the board of some private companies.

Nowadays, his research interests regard corporate strategy and business models for high tech and global companies. Professor Alberto Onetti is author of an extensive list of conference contributions, books and articles. His most recent book "Business Model for Biotech" will be published by Routledge end of this year.

Fernando Napolitano



Fernando Napolitano is Senior Vice President and Managing Director of Booz & Company Italia, formerly Booz Allen Hamilton where he became Partner & VP in 1998. He leads the Organization and Strategy practice in Italy, specialized in telecoms, media, aerospace and energy sectors.

He is the co-author of the book: *Megacommunities: how leaders form government, business and non profits can tackle today's global challenges together.* (2008).

Fernando is a graduate (with honors) of The University of Naples where he earned a degree in Economics. He holds a Master of Science in Technology Management from Brooklyn Polytechnic, NY; AMP Harvard Business School, Cambridge, MA; Diploma from the Chamber of Commerce of Paris. He is a member of the Board of Directors of ENEL S.p.A and a non-executive independent member of the Board of Directors of CIRA (Italian Aerospace Research Center)

INTRODUCTION

The economy of Italy is 7th largest in the world; adjusted for purchasing power parity, 10th. The country is as rich in technology and entrepreneurship as it is in history and culture. From furniture in Matera to machinery in Bologna to ski boots in Montebelluna, Italy's competitive small and medium enterprises export nearly 30% of the country's GDP. Most firms, including utilities, have been privatized. Indeed, Italy operates as a true market economy.

Yet despite its profile of quality and innovation, Italy has grown slowly during the past decade – slower, indeed, than Germany, France or the UK. And its competitiveness – its unit labor costs – has slipped, as wages rose but productivity stagnated. As a consequence, Italian firms and Italian savers chose attractive opportunities elsewhere, and net direct investment turned outward. Italy's investment reputation, however, is far worse than the reality.

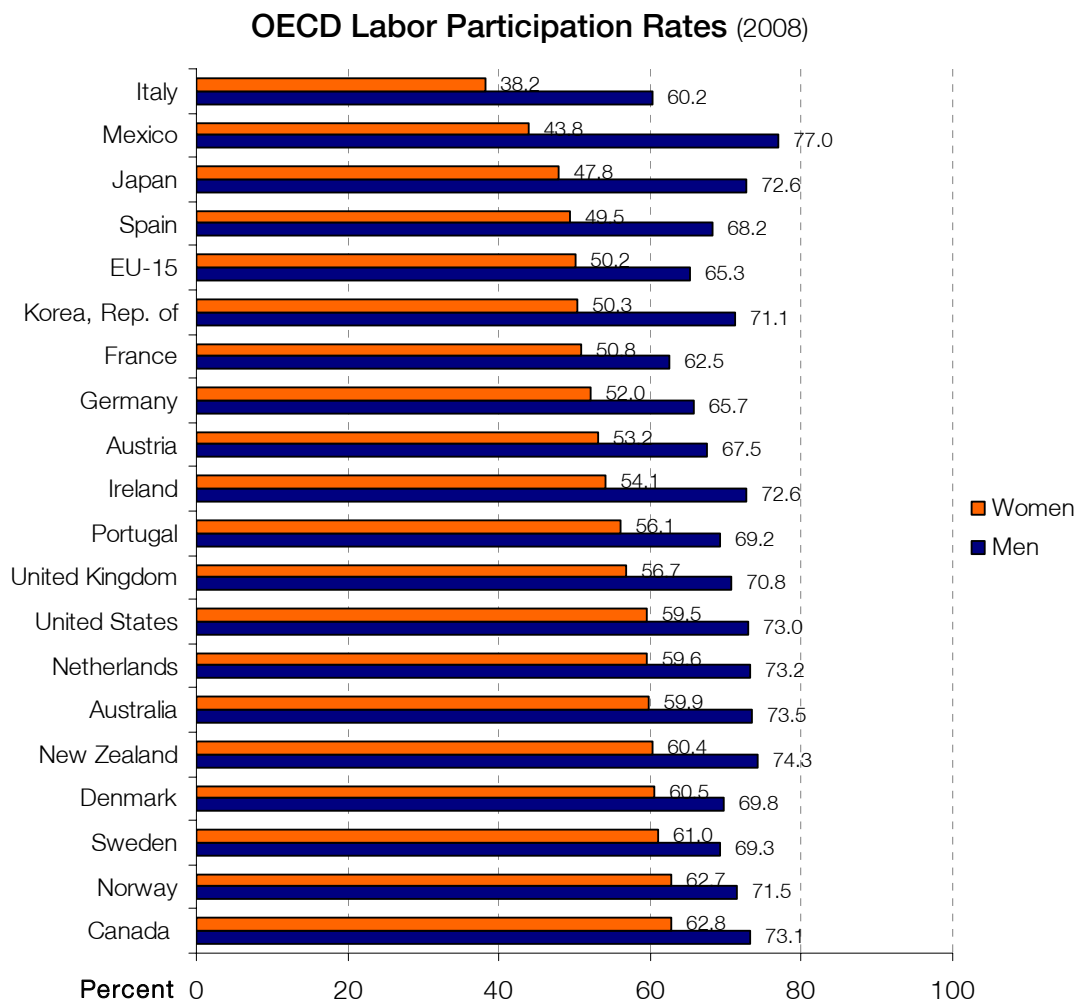
To mitigate these problems, the government of Italy must make changes in national policy. The regulatory and institutional factors that damage productivity must change. Real wages must stop growing, at least for a time, until productivity accelerates. And fiscal policy – the relationship between spending and revenues – must change, so that deficits decline, eventually along with debt and debt service. If the government could focus the Italian people on the need for reform, and the challenges of competitiveness, Italy could again become an export powerhouse and a target for foreign investors, everywhere.

The remainder of this paper examines Italy's macroeconomic environment and the structural problems that inhibit competitiveness; the microeconomic structure of Italy, together with its strengths in R&D, informational technology, design and engineering; the recent record of inbound foreign investment, and the exports associated with it; and finally, a series of recommendations for the government and a forecast of prospects for growth.

ITALY'S MACROECONOMY

Since 2001, Italy's real gross domestic product has grown at 0.27% annually. With the population growing at 0.5% annually, Italy's GDP per capita (adjusted for PPP) has declined, from about \$31,300 in 2008 to \$30,280 by 2010. Inflation, averaging 2% annually, accounts for this. The structure of the economy was stable. Consumption varied slightly, between 58% and 59%; government spending (not including transfer payments) about 19%-21%; and investment about 20%. Italy was deeply invested in the global economy, with the exports and imports adding 56% of GDP¹.

Unemployment was a bright spot for Italy's government during the past decade – although not necessarily for Italian growth. Partly because of the government's policy to allow temporary workers, unemployment had fallen from 9.1% to a low of 6.2% (in 2007), before worsening to 8.3% by 2010. While high by American standards, this was significantly lower than German/French levels. Italy's participation rate in the labor market is low – due both to early retirement and cultural barriers to women in the labor market.

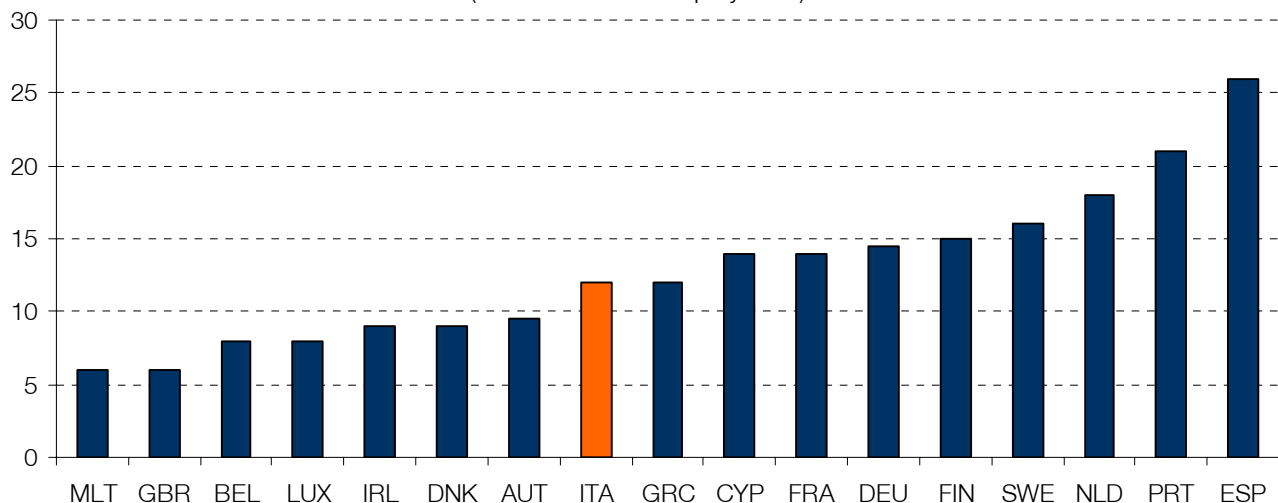


Sources: Bureau of Labor and Statistics and Organization for Economic Cooperation and Development

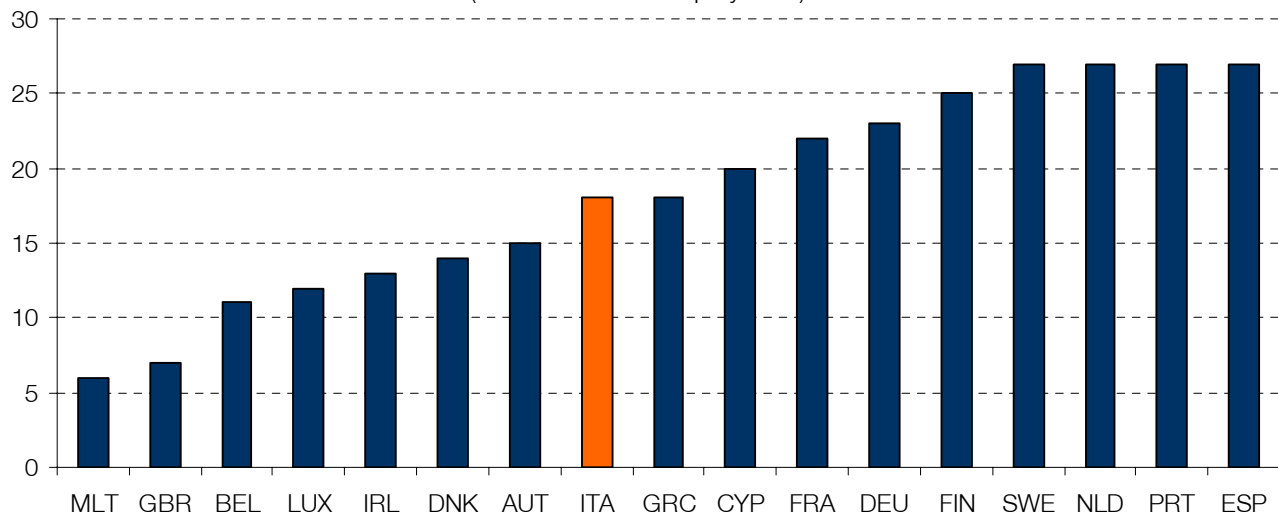
Thus, Italy's participation rate, of about 58%, is the second lowest in Europe. Female employment, at 48.4% of total employment, is lowest.

Temporary employment and part-time employment have taken much of the pressure off of the country's labor market. With about 12-14% of workers in these categories, Italy is about average in Europe, with Spain and Switzerland on the high side and Germany and Greece on the lower end. Certainly the worst employment problem pertains to youth. For potential workers between 15 and 24, unemployment hit 27.9% in September, 2010. This, in turn, forces young adults to live at home, adding to cultural immobility as well as frustration with the government's efforts to reform education.

Temporary Employment
(Percent of total employment)



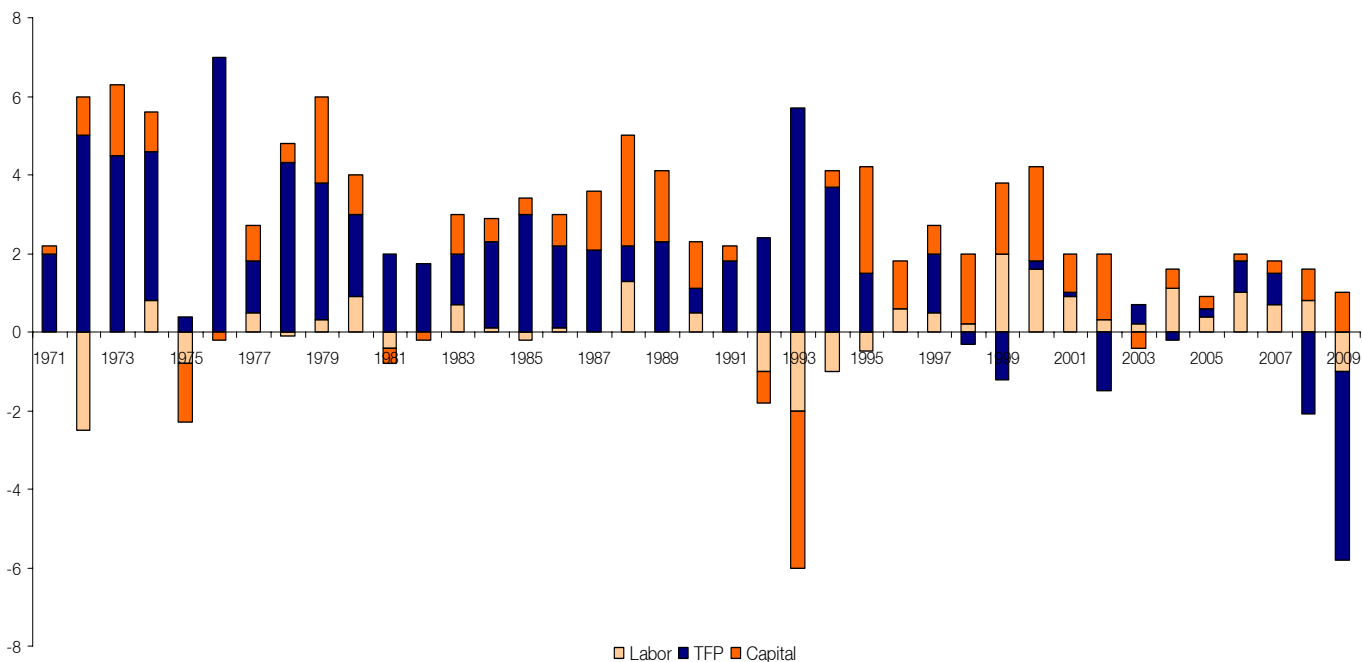
Part-Time Employment
(Percent of total employment)



Source: International Monetary Fund, 2010 Article IV Consultation, May 2010, 28.

Lack of productivity growth, we believe, is Italy’s preeminent problem. Low productivity growth, combined with persistently rising nominal wages, leaves Italy with unit labor costs rising significantly faster than its competitors – Germany, France and the UK.

Contributions to Growth: Historical Developments (Annual percentage changes in real GDP)



Sources: OECD and IMF staff calculations

Italy’s productivity growth has generally been negative for more than a decade. And this is not just labor productivity, but total factor productivity – the essence of growth and competitiveness. In the chart below, one sees that total factor productivity was the driving force in Italian growth until the late 1990s, when it generally turned negative.

Total factor productivity growth is sometimes called the “residual” – the contributions to productivity growth beyond labor and capital inputs. Among these factors economists often include skills, motivation, R&D, diffusion of learning, quality of workforce, regulation, bureaucratic red-tape, economies of scale and business-cycle effects. The following table breaks down growth contributions by sector. One sees, immediately, that the largest negative changes have occurred in manufacturing, construction, wholesale and retail.

Italy: Gross Value-Added Growth and Contributions

(Percent annual average growth rates)

	Contribution of							
	VA	L	H	LC	K	KIT	KNIT	MFP
1980-1995								
Total Industries	2.11	0.49	0.19	0.30	0.89	0.25	0.64	0.73
Manufacturing	2.22	-0.94	-0.99	0.05	0.94	0.19	0.75	2.22
Electricity, Gas and Water Supply	1.66	0.38	0.32	0.06	2.60	0.27	2.33	-1.32
Construction	0.06	-0.34	-0.35	0.01	0.50	0.09	0.41	-0.10
Wholesale and Retail Trade	0.06	-0.34	-0.35	0.01	0.50	0.09	0.41	-0.10
Hotels and Restaurants	0.95	2.63	2.52	0.11	0.26	0.04	0.22	-1.94
Transport, Storage and Communication	3.70	1.12	1.05	0.07	1.15	0.69	0.46	1.43
Financial Intermediation	1.31	1.50	1.28	0.22	1.70	1.18	0.52	-1.89
Business Activities	3.49	2.37	2.25	0.12	1.39	0.21	1.18	-0.27
Personal and Social Services	1.63	1.60	1.99	-0.39	0.52	0.18	0.34	-0.49
1995-2005								
Total Industries	1.33	0.66	0.49	0.17	0.91	0.25	0.66	-0.24
Manufacturing	-0.16	-0.23	-0.41	0.18	0.80	0.21	0.59	-0.73
Electricity, Gas and Water Supply	0.86	-0.91	-0.91	0.00	1.19	0.16	1.03	0.58
Construction	1.79	1.48	1.33	0.15	1.31	0.14	1.17	-1.00
Wholesale and Retail Trade	1.79	1.48	1.33	0.15	1.31	0.14	1.17	-1.00
Hotels and Restaurants	1.49	2.04	1.86	0.18	0.97	0.12	0.85	-1.52
Transport, Storage and Communication	3.68	0.80	0.66	0.14	1.41	0.32	1.09	1.47
Financial Intermediation	0.74	-0.08	-0.18	0.10	0.16	0.77	-0.61	0.66
Business Activities	2.21	1.82	1.71	0.11	0.83	0.23	0.60	-0.44
Personal and Social Services	1.19	0.78	0.95	-0.17	0.68	0.24	0.44	-0.27

1 / where:

- VA = Gross value added growth
- L = Labour Input Growth
- H = Total Hours Worked
- LC = Labour Composition
- K = Capital Input Growth
- KIT = ICT Capital
- KNIT = Non-ICT Capital
- MFP = Multi factor productivity growth

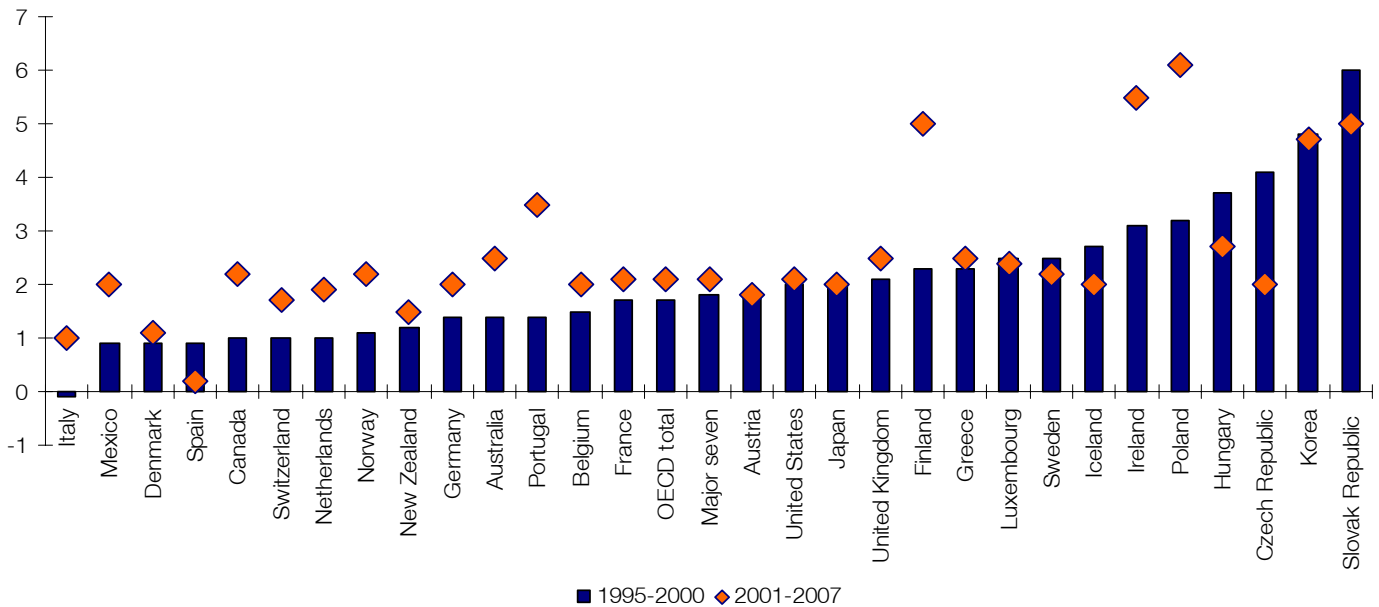
Sources: Hanan Morsy and Silvia Sgheri, "After the Crisis: Assessing the Damage in Italy," IMF Working Paper WP/10/244, October, 2010/ EU KLEMS database

In its latest assessment of Italy, the International Monetary Fund attributed Italy’s low productivity growth to a variety of structural causes:

- (1) Policy and regulatory rigidities limiting competition and hindering the business environment;
- (2) Low efficiency, linked to the preponderance of small and medium-sized enterprises typically unable to exploit fully economies of scale;
- (3) Limited process and product innovation, hindered by labor market rigidities;
- (4) Outdated specialization patterns, given a production structure (especially in manufacturing) based on traditional low skill products; and
- (5) Relatively poor human capital.

Italy’s labor productivity and its total factor productivity were low in comparison to competitors. Only Spain has underperformed Italy during the 2000s. While Total Factor Productivity (TFP) growth slowed in most countries, it actually increased in the USA.

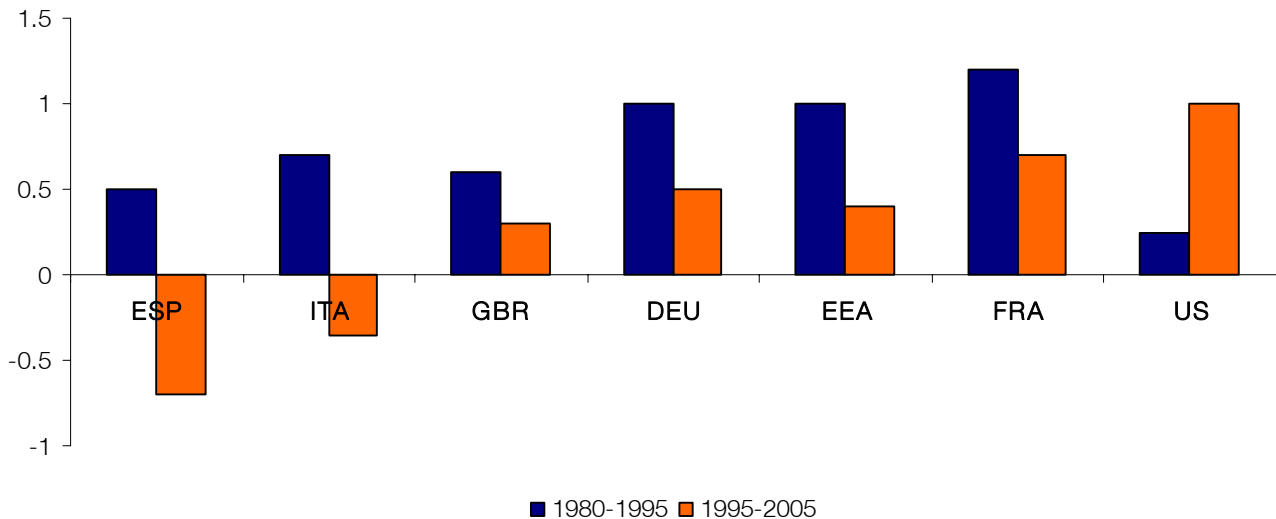
Growth in GDP per Hour Worked
(Labor Productivity)



Source: OECD

Comparative Growth in Total Factor Productivity

Average TFP Growth (Percent)

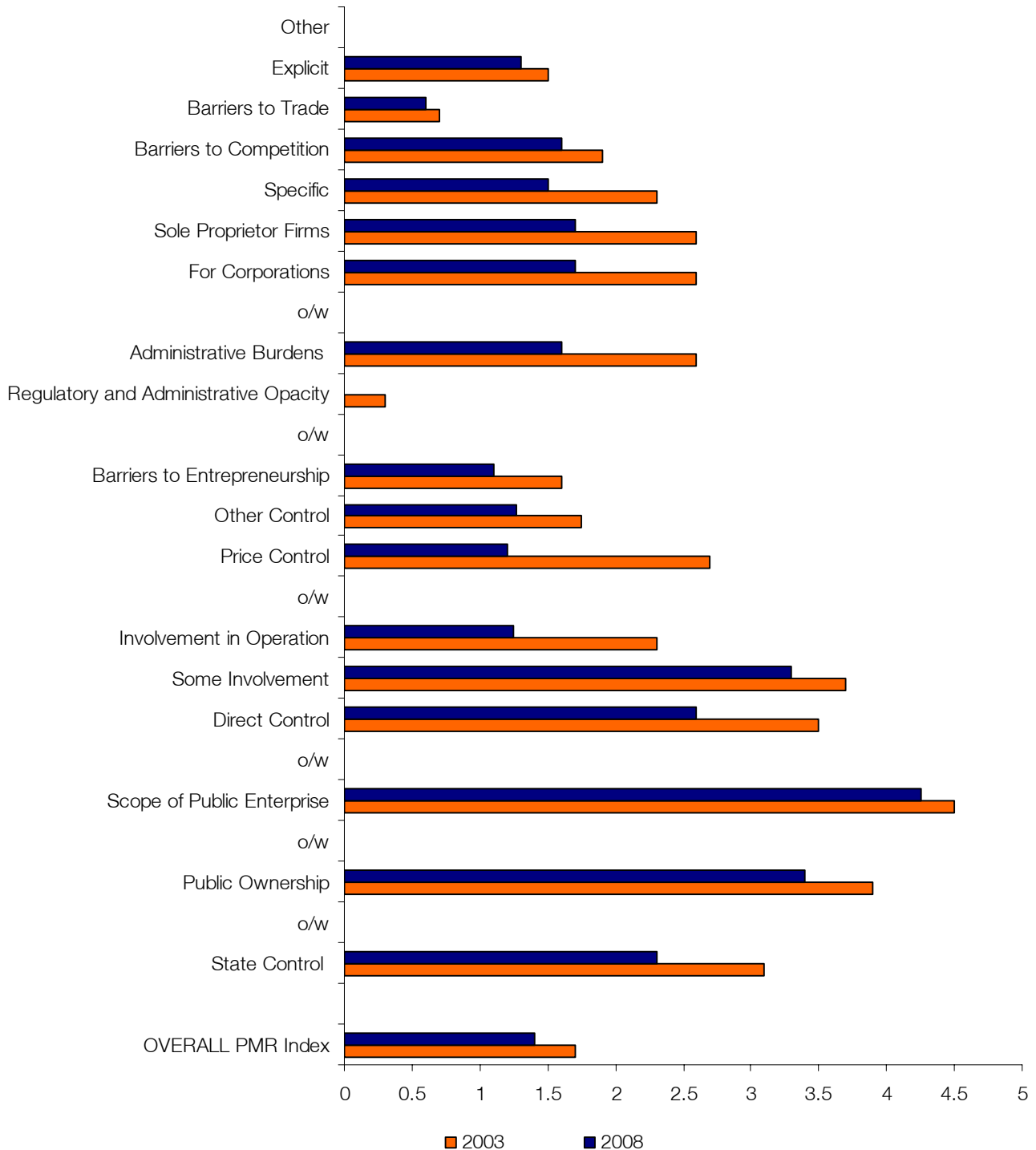


Source: KU KLEMS Database

Although the IMF report notes approvingly that some structural reforms have been undertaken in recent years, further progress was needed.² In July of 2006, for example, and again in January 2007, the legislature approved two rounds of “Bersani reforms.” Taxi licenses, airline ticket pricing, service charges for phone-card users, distances between gas stations, drug-stores, and a ban on barbershops operating Mondays were amongst these reforms. Most important, perhaps, was a reduction in the length of time needed to open a business in Italy, from 35 days to one week³.

The OECD was more positive still. In its 2009 review of regulatory reform, the OECD reported “steep apparent progress with regulatory reform” in Italy, in almost every indicator measured.⁴ In fact, the report found it puzzling that other sets of indicators, like the World Economic Forum’s *Global Competitiveness Guide* and the World Bank’s *Doing Business* data, painted a less favorable picture. The former ranks Italy 48th (out of 133 countries), primarily due to labor-market rigidities, corruption and crime. The latter cites access to credit and effectiveness of enforcing contracts as problems. Yet the OECD concluded that such national perspectives “fail to reflect the regionally diverse situations in Italy, where laws of 23 regions often offer a complex environment for doing business at the local level.”⁵ In its comparative study, the OECD placed Italy in the middle of the OECD – halfway between the United States and Poland – somewhat less restrictive than Germany or France.⁶

Italy's Product Market Regulation Indicators



Source: OECD Regulatory Database

In a recent *Economic Bulletin*, the Bank of Italy compared the country's productivity growth to its wage growth. Wages were growing at 2-4 percent annually (during the past five years). Growing wages increase unit labor costs, while growing productivity reduces them. Thus, as the following chart indicates, unit labor costs have grown at 2, 4 and even 5 percent annually.

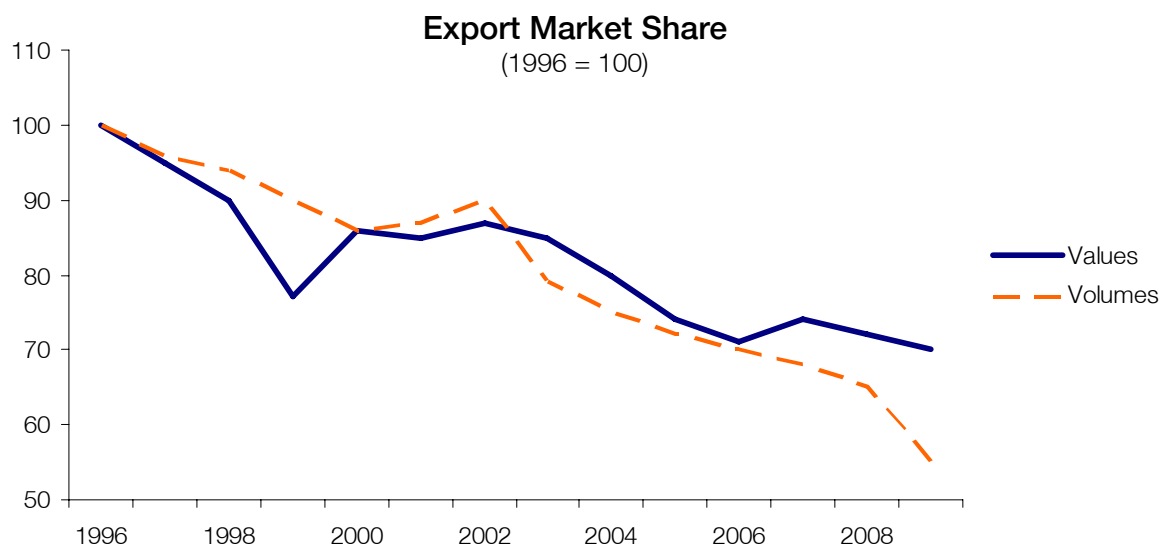
Manufacturing Unit Labor Costs in US Dollars and National Currencies

(Annual % change)

Country of area	Indicator	1979-2009	1979-1990	1990-2000	2000-2007	2007-2008	2008-2009
United States	ULC in U.S. dollars	0.3	2.5	-0.4	-2.3	3.5	-2.3
	ULC in nat cur.	0.3	2.5	-0.4	-2.3	3.5	-2.3
	Exchange rates						
France	ULC in U.S. dollars	1.9	2.7	-3	6.2	11.4	3.8
	ULC in nat cur.	2.2	5.1	-0.4	0.4	3.7	9.7
	Exchange rates	-0.3	-2.2	-2.6	5.8	7.4	-5.4
Germany	ULC in U.S. dollars	2.9	4.5	-1.3	4.4	10	9.6
	ULC in nat cur.	2	3.3	1.4	-1.3	2.8	15.8
	Exchange rates	0.9	1.1	-2.7	5.8	7.4	-5.4
Italy	ULC in U.S. dollars	3.2	5.2	-3.8	8.7	15.2	6
	ULC in nat cur.	5	8.8	1.7	2.8	7.2	12
	Exchange rates	-1.7	-3.3	-5.4	5.8	7.4	-5.4
Japan	ULC in U.S. dollars	2.3	4.6	2.1	-5	15.7	23.3
	ULC in nat cur.	-0.5	0.7	-0.9	-3.8	1.6	11.8
	Exchange rates	2.9	3.8	3	-1.3	13.9	10.4
United Kingdom	ULC in U.S. dollars	2.2	4.5	-0.2	4.9	-5.7	-10.2
	ULC in nat cur.	3.2	6.2	1.5	0.9	1.8	6.3
	Exchange rates	-1	-1.6	-1.6	4.1	-7.4	-15.6

Source: Bureau of Labor Statistics, *International Comparisons of Manufacturing Productivity and Unit Labor Cost Trends, 2009 (USDL-10-1749)*, December 21, 2010.

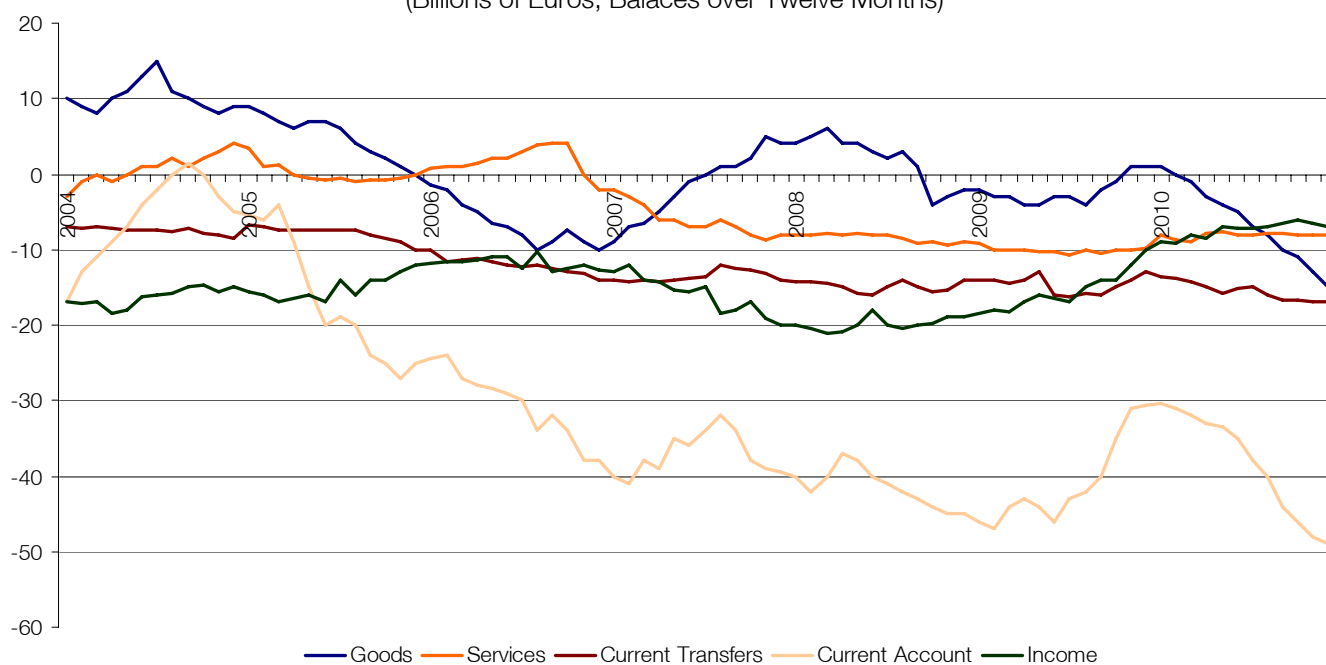
As a consequence of this decline in Italy's competitiveness, its market share of global exports has shrunk in value by 30% since 1996, and even more by volume. This decline in the competitiveness of Italian exports only added to a negative balance on the current account, Italy's cash flow, beginning in 2000. Despite Italy's excellent tourism, services were negative, as was income, largely due to debt service on public-sector debt, and transfers.



Source: IMF, *2010 Article IV Consultation – Staff Report, May 2010, 4.*

Current Account

(Billions of Euros; Balaces over Twelve Months)



Source: Banca d'Italia, Supplement to the Statistical Bulletin, Balance of Payments and International Investment Position, Vol. XXI, January 24, 2011, 5.

To balance this negative current account, capital needed to flow into Italy. Most of this came as portfolio acquisitions of stocks and corporate bonds, with some purchases as well of public sector debt. Direct investment, while significant, was less than outward foreign direct investment, as Italian companies sought to expand their market presence elsewhere.

Italy's Balance of Payments (1)

(Billions of Euros)

	2008	2009	Jan. - Oct. 2009	Jan. - Oct. 2010
Current account	-46	-31.7	-28.8	-43
Goods	-2.1	0.8	0.9	-13.1
Non-energy products (2)	55.3	41.5	34.6	27.2
Energy products (2)	-57.5	-40.7	-33.7	-40.3
Services	-9	-9.9	-7.7	-6.7
Income	-19.2	-10	-9.8	-7.7
Current transfers	-15.6	-12.6	-12.2	-15.5
Capital account	-0.2	-0.1	0.4	0.2
Financial account	29.8	24.4	19.8	61.4
Direct investments	-55	-15.9	-17.3	-4.2
Portfolio investment	75.2	28.1	75.7	26.7
Financial derivatives	2.9	4.8	4.4	-2.2
Other investment	12.2	7.4	-42.4	42.2
Change in official reserves	-5.6	0.1	-0.6	-1.1
Errors and omissions	16.4	7.3	9.3	-18.5

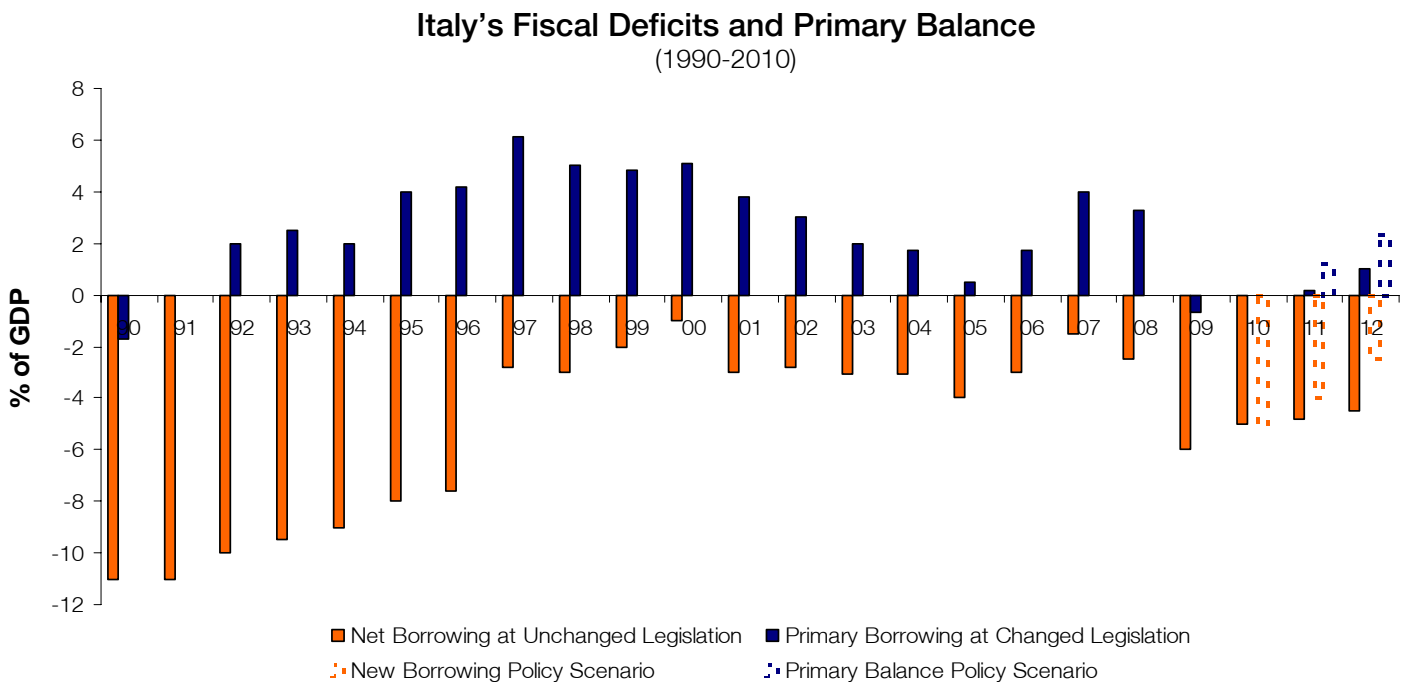
(1) Provisional data for October 2010

(2) Based on Istat foreign trade data

Source: Banca d'Italia, Economic Bulletin, No. 59, January 2011, 28.

We will return to the microeconomic flows of FDI in a later section of this paper.

The final, important aspect of Italy's macroeconomic performance is fiscal policy. Entry into monetary union required Italy to bring its budget under control. From an annual deficit of more than 10%, the government reduced it, in part by privatizing more than €100 billion state-owned companies, to just over 1%. But with lagging exports and slowing growth, Italy's deficit expanded to 4.4% in 2005. The Berlusconi government worked assiduously during the next three years to again reduce it, holding the average to 2.8% of GDP. The shock of financial crisis, in 2009, dramatically reduced revenues and forced an increase in expenditures. The deficit ballooned to 5% by 2010.



Source: Italy Ministry of Finance, Combined Report on the Economy and Public Finance for 2010, May 6, 2010, 45.

The details of the budget, shown in the following table, show that social benefits – primarily pensions – are the largest single item among current expenditures, at €238 billion for 2010; compensation for government employees follows, at €175 billion, followed by interest on the debt (€72 billion). All of these items dwarf capital expenditures, at €59.4 billion. On the revenue side, one sees the drop-off of direct taxes after 2008, and indirect taxes after 2007. Social contributions fall a bit in 2009, but begin recovering by 2010.

In the Berlusconi government's latest budget proposal, controllable expenditures would flatten out. That is, employee compensation would remain flat through 2013, and capital expenditures would actually fall. Uncontrollable items, including pensions and interest expenditures, would still rise. On the revenue side, tax revenues, due to faster growth, would rise by €50 billion. The deficit of 5% of GDP would fall to 2.2% by 2013, and the primary balance would actually turn positive, reaching 2.6% of GDP.

Italy's General Government Expenditures and Revenues

(Millions of Euro) 2008-2013

	2008	2009	2010	2011	2012	2013
EXPENDITURES						
Employee compensation	169,813	171,578	174,964	173,893	174,102	174,707
Gross wages	120,703	121,605	123,609	122,166	122,205	122,548
Employer social security contributions	49,110	49,973	51,335	51,728	51,898	52,160
Intermediate consumption	129,009	137,199	139,528	138,960	141,605	145,929
Social security benefits	277,263	291,335	298,130	305,600	313,130	324,490
Pensions	222,854	232,323	238,270	246,280	252,398	261,060
Other social security benefits	54,409	59,012	59,860	59,320	60,732	63,430
Other current expenditures	59,022	61,684	63,523	60,716	59,940	60,611
Total current expenditures, net of interest (% of GDP)	635,107 40.50%	661,796 43.50%	676,145 43.50%	679,169 42.40%	688,777 41.40%	705,737 40.80%
Interest expenditure (% of GDP)	81,161 5.20%	71,288 4.70%	72,069 4.60%	75,670 4.70%	80,151 4.80%	83,780 4.80%
Total current expenditures incl: Healthcare expenditure	716,268 108,486	733,084 110,588	748,214 114,962	754,839 116,116	768,928 119,048	789,517 123,846
Total capital expenditures	58,368	65,770	59,439	54,369	52,323	51,902
Fixed capital formation	34,602	37,040	33,447	30,800	28,550	29,480
Transfers to capital account	22,154	24,445	23,678	21,496	21,587	20,465
Other transfers	1,612	4,285	2,314	2,073	2,186	1,957
Total expenditures, net of interest	693,475	727,566	735,584	733,539	741,100	757,639
Total expenditures	774,636	798,854	807,653	809,209	821,251	841,419
Revenues						
Total tax revenues	456,237	441,858	447,786	456,501	480,120	497,773
Direct taxes	239,740	222,655	226,355	228,659	243,496	252,617
Indirect taxes	216,009	206,956	219,181	226,817	235,721	244,474
Capital account taxes	488	12,247	2,250	1,025	903	683
Social contributions	215,911	215,003	217,238	223,140	229,239	235,893
Cash contributions	212,031	210,917	213,083	218,917	224,948	231,531
Non-cash contributions	3,880	4,086	4,156	4,223	4,291	4,362
Other current revenues	56,695	57,341	59,404	60,412	61,542	62,833
Total current revenues	728,355	701,955	722,179	739,028	769,998	795,816
Non-tax capital account revenues	3,218	3,852	6,100	6,019	6,032	6,074
Total revenues	732,061	718,054	730,529	746,072	776,933	802,573
<i>Memo item: Tax burden</i>	42.90%	43.20%	42.80%	42.40%	42.60%	42.40%
Balances						
Primary balance (% of GDP)	38,586 2.50%	-9,512 -0.60%	-5,056 -0.30%	12,533 0.80%	35,832 2.20%	44,934 2.60%
Current account balance (% of GDP)	12,087 0.80%	-31,129 -2%	-26,036 -1.70%	-15,811 -1%	1,069 0.10%	6,299 0.40%
Net borrowing (% of GDP)	-42,575 -2.70%	-80,800 -5.30%	-77,125 -5%	-63,137 -3.90%	-44,319 -2.70%	-38,846 -2.20%
Nominal GDP	1,567,851	1,520,870	1,554,718	1,602,836	1,664,899	1,730,115

Note: The account includes the effects of the 2010 budget balancing provision and of Decree-Law no 78/2010 converted into Law no. 122/2010 containing the fiscal consolidation plan.

Source: Italy Ministry of Finance, 2011-2013 Public Finance Decision, submitted by Silvio Berlusconi and Giulio Tremonti, 29 September, 2010, 22.

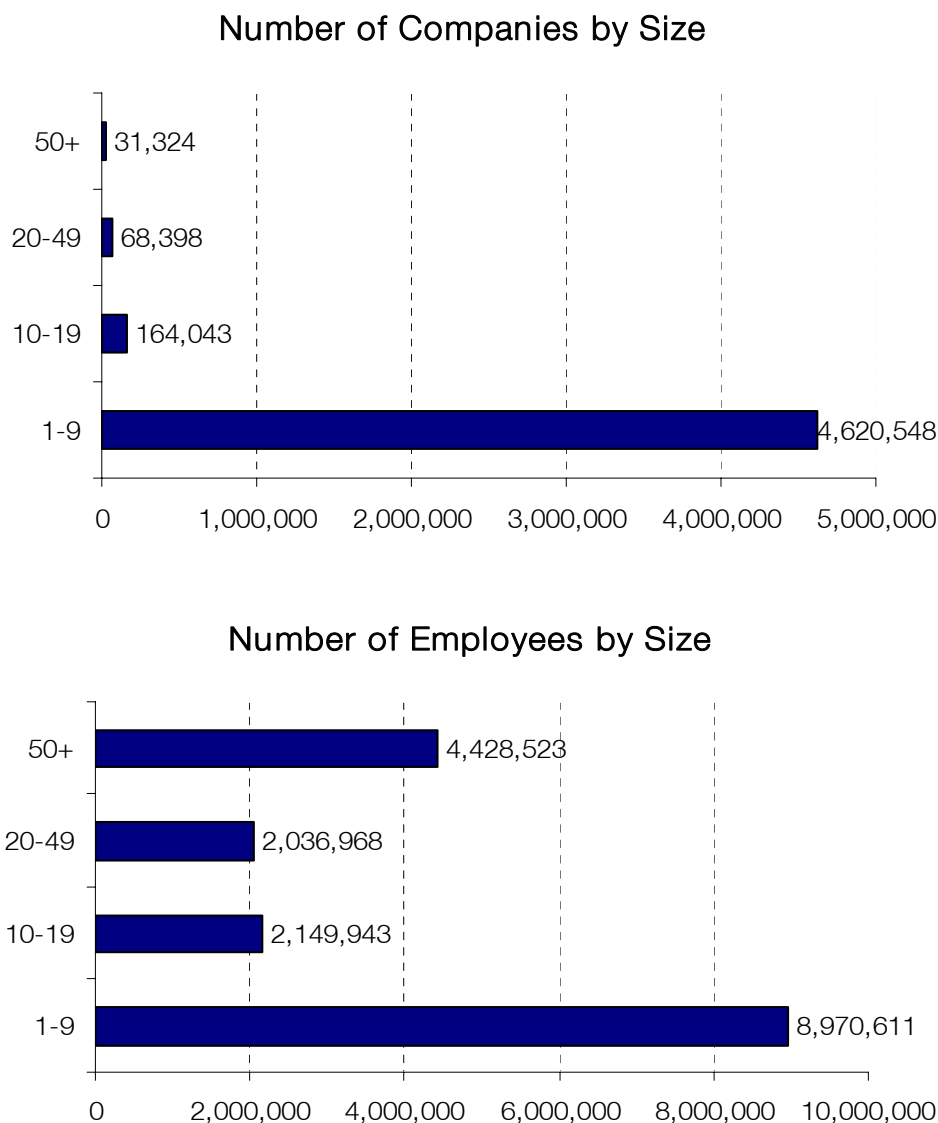
Having reached a low point of 103.5% in 2007, the ratio of debt to GDP has risen sharply in the past three years, reaching 118.4% by 2010. Yet with the budget currently envisioned, the government's debt ratio would flatten out and shrink, to 115% by 2013.⁸

MICROECONOMIC STRUCTURE OF ITALY. THE MORPHOLOGY OF THE COUNTRY

In Italy, SMEs play a dominant role, in particular small and micro companies.

Ninety-nine percent of the approximately five million Italian firms have less than 50 employees and 95% less than ten. Large companies (over 250 employees) in Italy number less than 4,000 but they contribute heavily to employment. Twenty percent of the total Italian workforce is estimated to be employed by large corporate (250+ employees), 25% if we include also medium size firms (50-250 employees)⁹.

Figure 1: Number of Companies and Employees by Size



Source: ISTAT, *Struttura e dimensione delle unità locali delle imprese. Anno 2007. Dicembre 2009.*

Figure 2: Average Corporate Size – International Comparison

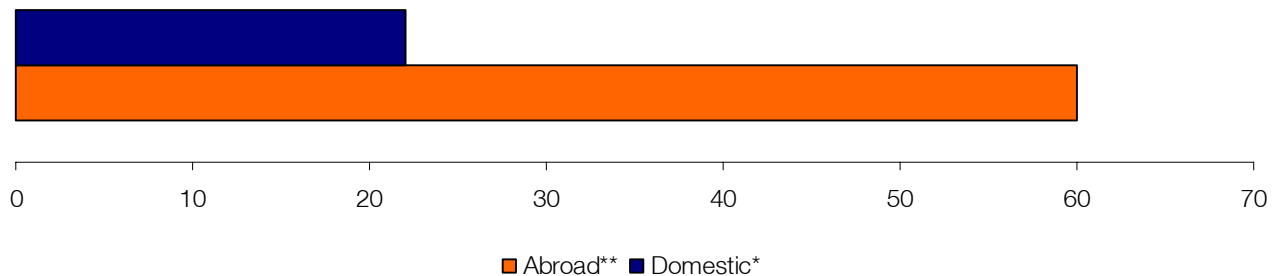
Average Number of Employees		Growth Rate of Average Size	
	2007		% var. 99-07
Italy	4.0	Italy	0.08
France	5.8	France	-0.12
Germany	13.3	Germany	0.25
Spain	5.3	Spain	0.08
United Kingdom	11.1	United Kingdom	-0.06
EU-15	6.4	EU-15	-0.04

Source: Bank of Italy, 2010 Annual Report

The average company size in Italy is four employees – a figure that is slightly lower than European average of 6.4. The generally small company size can represent a competitive issue in the current scenario, characterized by increasing competition and more distant outlets, that calls for a strengthening of R&D, marketing and distribution. Larger sized companies may help to gain economies of scale in these crucial activities. Italian SMEs seem to be not passive onlookers of these developments: during the past decade the average size in Italy increased by 8%.

Figure 3: Growth Rate in Production of Italian Companies

(Current Prices, 2002-2008)



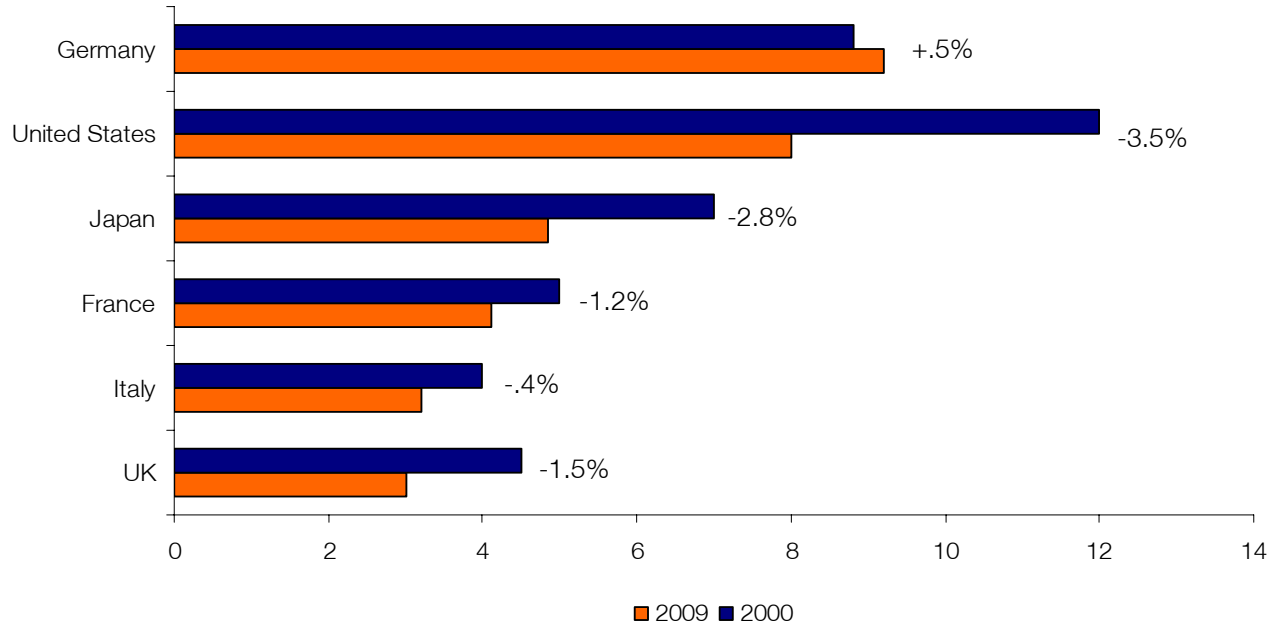
*GDP growth at current prices, ** Sales of foreign subsidiaries (rate of growth)

Source: Reprint and Istat

Despite their small sizes, Italian SMEs are largely global and account for around 70% of the country's exports. Internationalization rates seem to increase over the time and in the period between 2002-2008, the growth rate of production abroad has been three times greater than that achieved at domestic plants.

During the last decade almost all advanced economies showed a significant decrease in their international market shares. Compared to most other industrialized countries (except for Germany that was able to gain new market shares), the decrease rate of Italy was smaller.

Figure 4: International Market Shares – International Comparison



In terms of geographical distribution, over 50% of the companies and 57% of the workforce are located in the Northern part of Italy. The Lombardy region plays a dominant role, attracting over 18% of the firms (over 890,000 firms) and contributing 21% of overall employment (approx. 4 million people). Piedmont, Veneto and Emilia Romagna are other important areas in terms of number of companies (8-9% as an average each) and employment (8-10%).

In the Center, Lazio and Toscana are the most significant industrial regions, while, in the Southern part of Italy, Campania is the most densely industrialized.

Table 1: Number of Companies and Employees by Region

Regions	Companies		Employees	
	Number	Percent	Number	Percent
Piedmont	376,847	7.70%	1,469,241	8.4
Aosta Valley	13,218	0.30%	44,053	0.3
Lombardy	899,584	18.40%	3,696,865	21
Liguria	145,392	3.00%	478,802	2.7
Trentino Alto Adige	91,610	1.90%	361,906	2.1
Veneto	444,578	9.10%	1,801,251	10.2
Friuli Venezia Giulia	99,097	2.00%	410,783	2.3
Emilia Romagna	421,906	8.60%	1,674,425	9.5
Toscana	366,807	7.50%	1,247,395	7.1
Umbria	76,963	1.60%	266,341	1.5
Marche	146,328	3.00%	541,539	3.1
Lazio	448,790	9.20%	1,586,660	9
Abruzzo	110,217	2.30%	377,858	2.1
Molise	23,326	0.50%	69,922	0.4
Campania	373,993	7.70%	1,096,313	6.2
Apulia	268,395	5.50%	807,304	4.6
Basilicata	39,175	0.80%	122,229	0.7
Calabria	120,873	2.50%	312,720	1.8
Sicily	296,149	6.10%	848,689	4.8
Sardinia	121,065	2.50%	371,748	2.1
North-Western Italy	1,435,041	29.4	5,688,962	32.3
North-Eastern Italy	1,057,191	21.6	4,248,365	24.2
Central Italy	1,038,888	21.3	3,641,936	20.7
Southern Italy	935,979	19.2	2,786,344	15.8
Insular Italy	417,214	8.5	1,220,438	6.9
ITALY	4,884,313	100	17,586,044	100

Source: ISTAT, *Struttura e dimensione delle unità locali delle imprese. Anno 2007. December 2009.*

Table 2: Number of Companies by Size and Macro-Region

	1-Sep	Oct-19	20-49	50+	Total
North-Western Italy	1,349,112	51,374	22,719	11,836	1,435,041
North-Eastern Italy	987,750	42,140	18,955	8,346	1,057,191
Northern Italy	2,336,862	93,514	41,674	20,182	2,492,232
Central Italy	985,270	34,366	13,333	5,919	1,038,888
Southern Italy	897,881	24,923	9,419	3,756	935,979
Insular Italy	400,535	11,240	3,972	1,467	417,214
Southern Italy	1,298,416	36,163	13,391	5,223	1,353,193
ITALY	4,620,548	164,043	68,398	31,324	4,884,313
%	94.60%	3.40%	1.40%	0.60%	100.00%

Source: ISTAT, *Struttura e dimensione delle unità locali delle imprese. Anno 2007. December 2009.*

The data above confirms that the Italian economy is characterized by important differences among its regions. The top 9 regions, located in the North and Center of Italy, have a higher rate of performance as compared to the rest of Italy, and also those of other European countries.

Figure 5: Selected Italian Regions: International Comparison
(Index Numbers: Italy = 100)

Geographic Areas	GDP (Per Capita*)	Industrial Vocation**	Export Propensity***
Top Nine Italian Regions****	119	124	134
Germany	112	118	179
United Kingdom	110	80	85
France	103	66	93
Italy	100	100	100

* GDP per capita in 2008 Purchasing Power Parity (PPP)

** Industrial value added (net of constructions) as a % of total value added in 2009

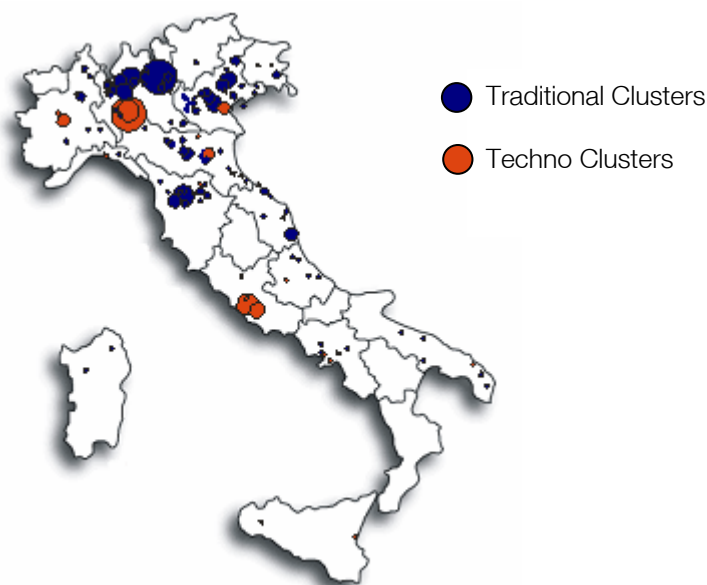
*** Exports/GDP

**** Emilia Romagna, Friuli Venezia Giulia, Lombardia, Marche, Piemonte - Valle d'Aosta, Toscana, Trentino Alto Adige, Veneto.

Source: Eurostat, Istat

Agglomeration economies traditionally play an important role in Italy. The Italian industrial structure is characterized by the clustering of industrial activities in specific locations, known as industrial districts or clusters. In these “distretti” we have a geographic concentration of interconnected firms and suppliers with a narrow specialization profile. Distretti are widespread all over Italy. World famous examples are Carrara in marble, Sassuolo in tiles and ceramics, Vicenza and Arezzo in jewelry, Como in silk fabric, Arzignano and Santa Croce sull’Arno in leather, Biella and Prato in textiles, and Belluno in glass.

Figure 6: Italian Districts and Techno Clusters



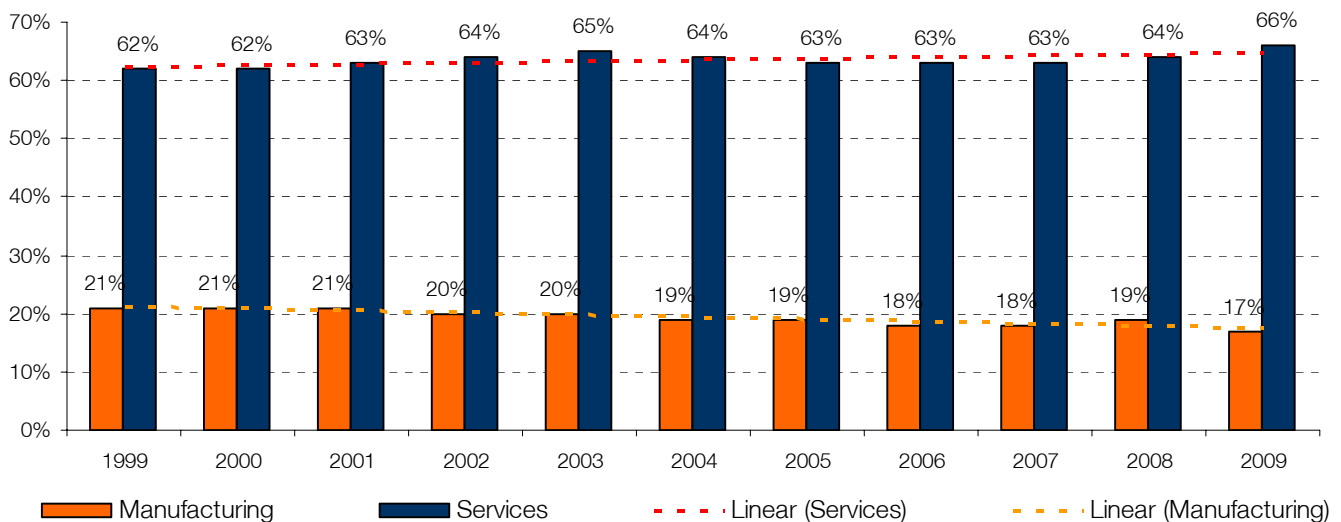
Source: Intesa Sanpaolo, *Economia e finanza dei distretti industriali. Annual report, No.3. December 2010.*

Data about Italian districts are not homogeneous. Banca Intesa Sanpaolo, in a recent report (2010), lists 101 traditional districts (marked in blue in Figure 6) and 18 techno clusters (8 in ICTs, 5 in pharma and biotech, 5 in aero-space, (marked in orange in Figure 6). Italian Regions identify - as of September 2009¹⁰- 170 industrial districts. 106 are located in the North, while 41 are in the Centre and 23 in the Southern part of Italy. Districts in the textile sector are the most numerous (41), followed by the mechanical sector (34) and furniture (28).

The prevalence and success of districts has been explained in analytical literature as an effective way for SMEs to compete¹¹. Inter-organizational networks allow small firms to reach a critical competitive threshold and benefit from economies of scale. More recently, the model of Italian industrial districts has been questioned and linked to Italy's poor growth performance. The main question refers to the ability of small firms in industrial districts to internationalize activities and invest in research and development. Notwithstanding this, some districts are still leaders or significant players in world exports markets. Sassuolo was credited in 1999 with having approximately 40% of the tile world export market, while Como has over 25% share of the silk fabrics market (Fortis 1999; Helg 1999). More recent data seem to confirm this position¹². In 2010, for the first time since the beginning of this century, export from districts has grown more than export from companies not belonging to “distretti” (+16% vs 15.6%).

In the Italian economy, manufacturing accounts for over 25% of the employment (and 11% of the overall number of companies), but the services sector has, over time, assumed a dominant role. In 2009 services account for 66% of the GDP, while manufacturing contributed only 17% of GDP, with a declining role (it was 21% ten years ago as shown in Figure 7).

Figure 7: Contribution to GDP by Sector - Manufacturing vs. Services
(1999-2009)

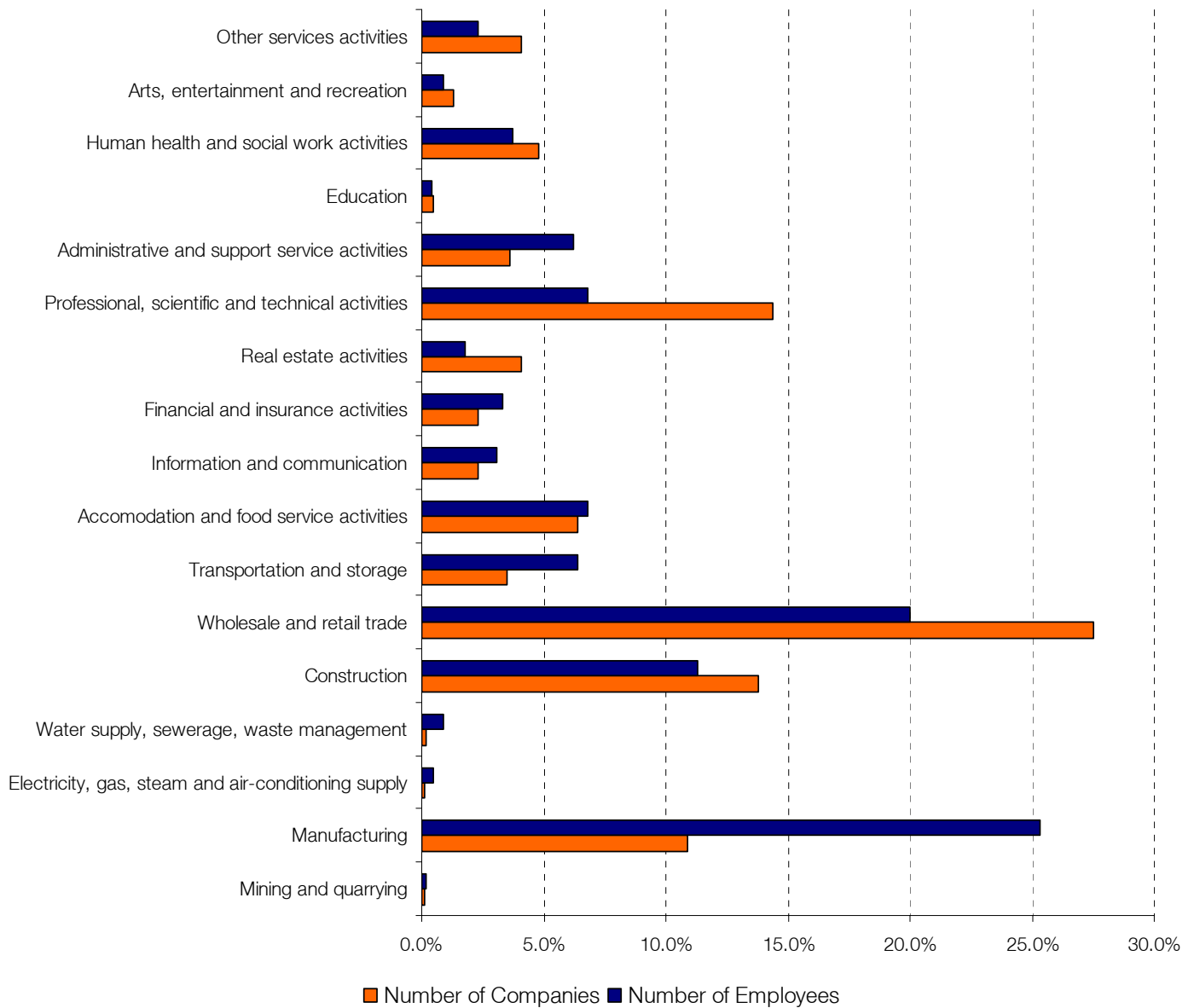


Source: ISTAT, EUROSTAT (several years).

In services wholesale and retail trade firms account for over 27% of the total and employ 20% of the labor force.

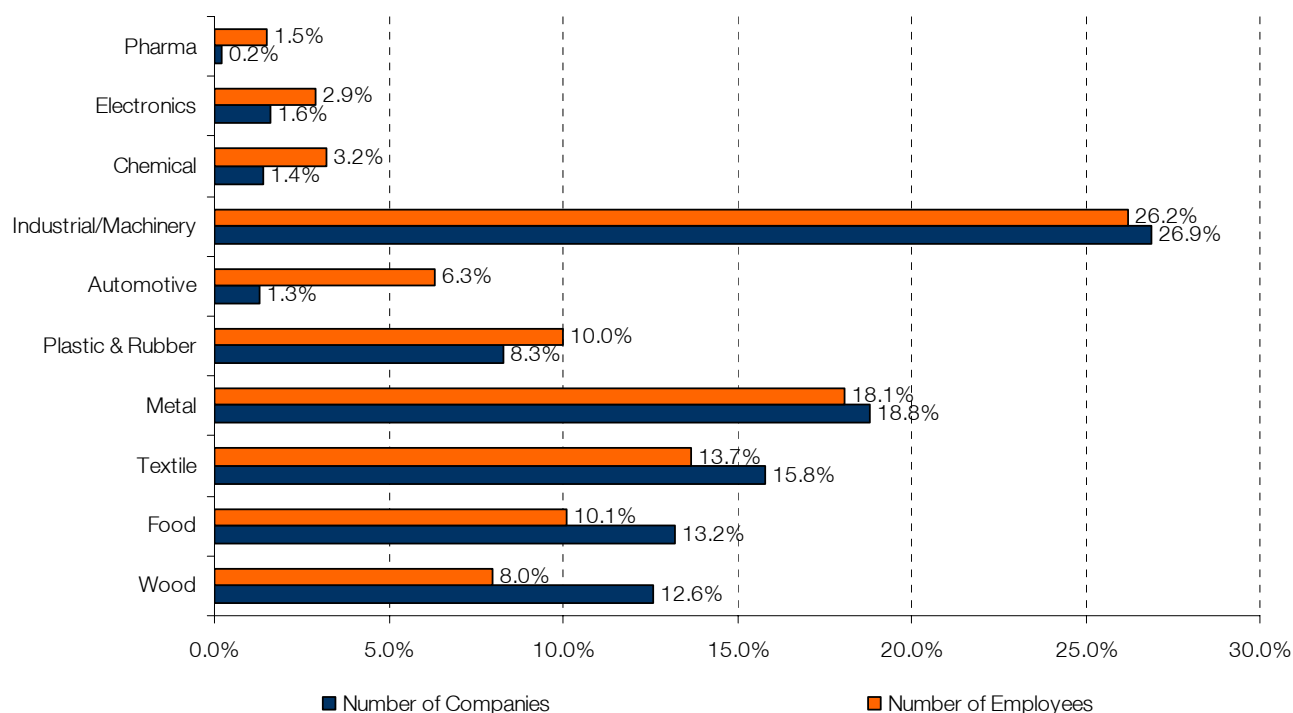
Real estate and construction are other important activities (accounting for approx. 18% of the total number of companies and 13% of the workforce).

Figure 8: Number of Companies and Employees by Industry



Source: ISTAT, *Struttura e dimensione delle unità locali delle imprese. Anno 2007. Dicembre 2009.*

Figure 9: Manufacturing Industry (Detail) - Number of Companies and Employees



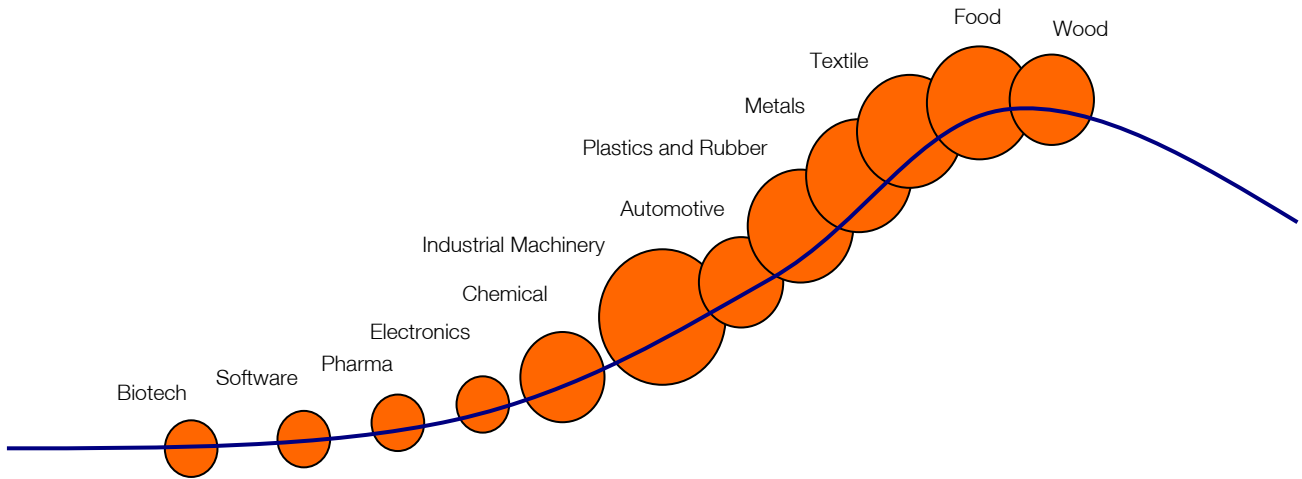
Source: CrESIT 2010 based on ISTAT data¹³.

In manufacturing, industrial machinery is the dominant industry (27% of the total firms and over 26% of employment), followed by textiles (16% of firm population and 14% of employment). Other important contributors to the country’s economy are food, wood and plastic and rubber (42% of the total and 32% of the workforce).

All these industries are composed of SMEs. Conversely automotive, chemical and pharma industries are mostly made up of medium and large firms. They jointly account for less than 3% of the firm population but 11% of the employment.

A study carried out by the Research Centre for Innovation and Life Sciences Management of University of Insubria ([CrESIT](#)) in 2010 shows how the Italian industrial system is mostly built upon mature business. As shown in Figure 10 larger GDP contributors are mostly positioned on the right side of the life-cycle curve, while emerging and innovative industries do play a minor role, estimated ranging from 2 to 6%. A concern often raised is whether this pattern of specialization makes Italy vulnerable to the competition from labor-abundant emerging countries. Additionally the ability of Italy to innovate is similarly questioned.

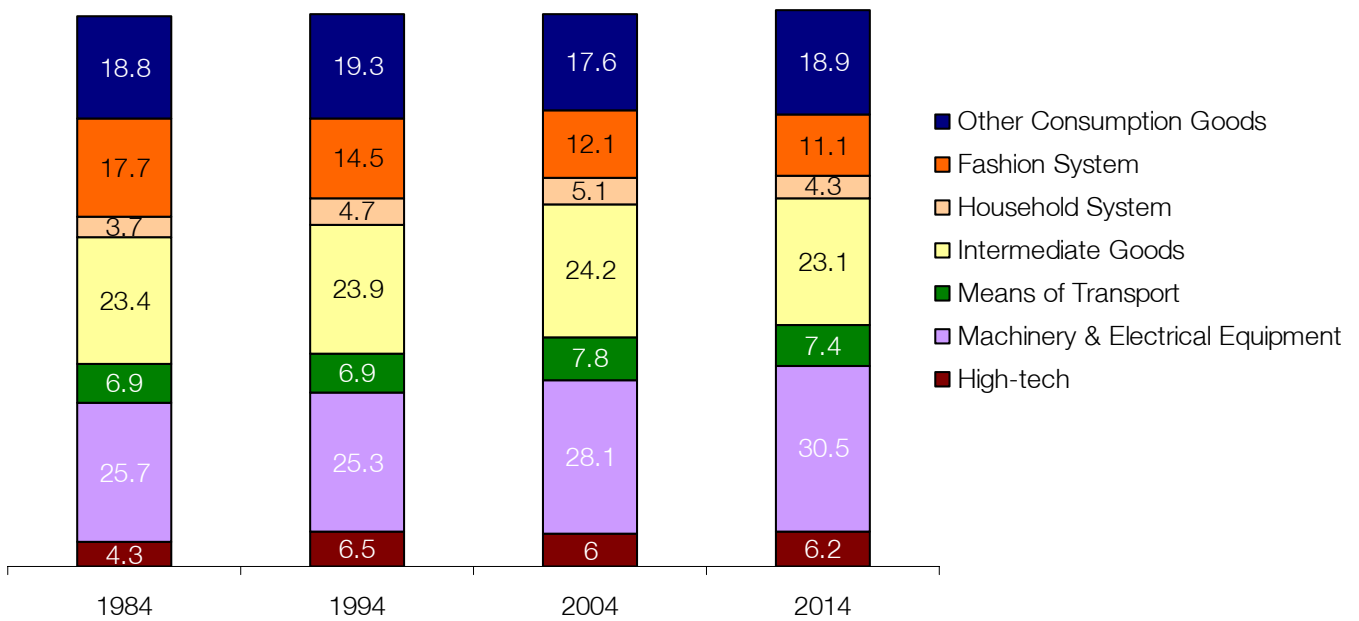
Figure 10: Italy: Industry Contribution to GDP
(2009)



Source: CrESIT 2010, based on EUROSTAT data

None withstanding, the Italian main specialization in low-tech and traditional sectors seem to be slowly reducing, while high-tech and particularly mid-tech industries seem to be increasing their weight over the time.

Figure 11: The Italian Manufacturing Structure - Historical Evolution
(Sales at constant prices)



Source: Intesa Sanpaolo – Prometeia (2011)

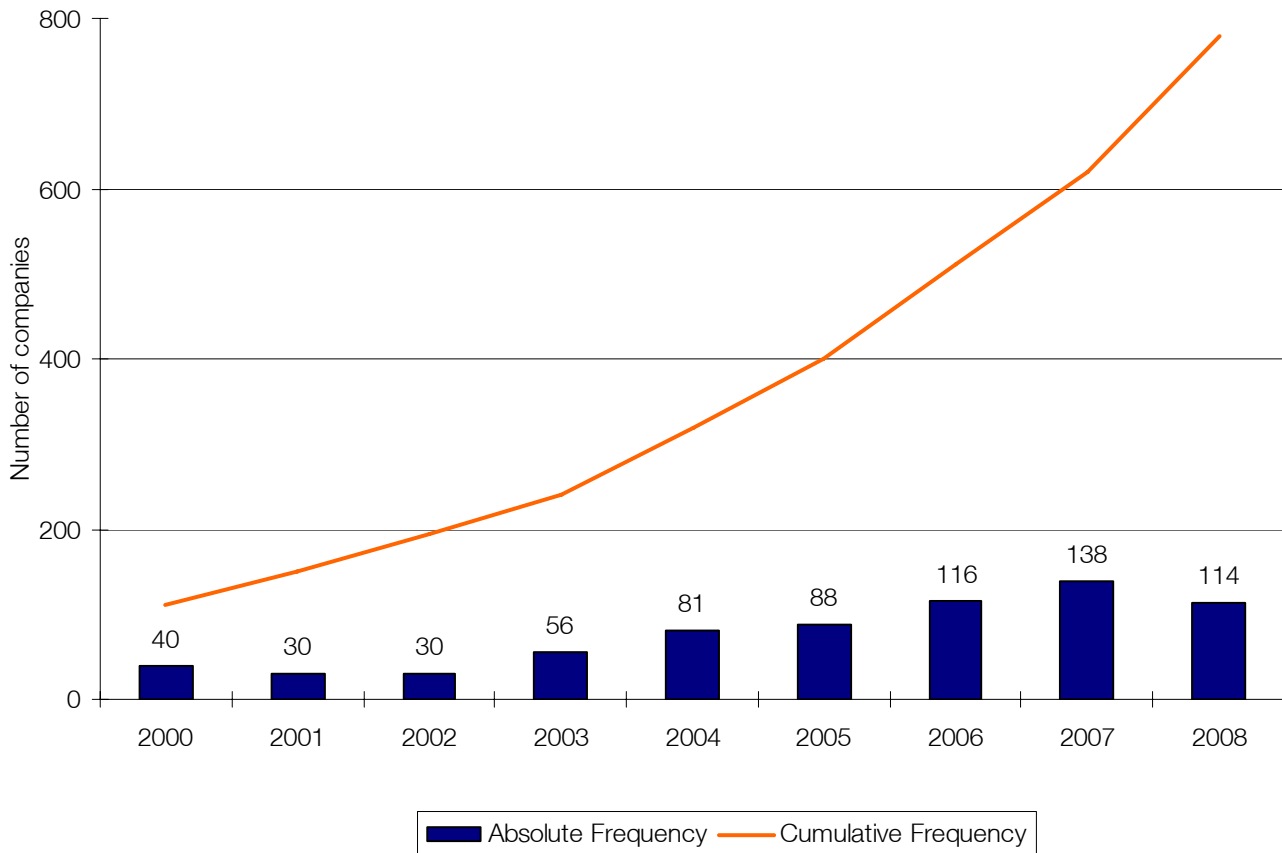
It is important to understand the business culture and approach of Italian companies. Below are some typical themes that exemplify the traditional business Italian culture (Onetti, Versaggi & Mackler 2009; Segal 2010)¹⁴. These cultural themes are not necessarily unique to Italy, but are true for many business cultures that have had to evolve from a conservative mindset. Looking at these themes may help to read the data we provided above.

- Lifestyle companies are the industry-wide reference model in Italy. People start a company from a strong family business vocation where the founder is supposed to both own and run the business. Not just in the early stage, but also later on as the company grows bigger. “The first goal of many entrepreneurs here isn’t growth, so much as keeping the business in the family” (Segal 2010). Having investors on board brings equity, however the owner expects to also share the right to make crucial decisions. Having board guidance from investors is thus often perceived as an interference, since it means giving up at least some control. So “thousands of companies in Italy remain stubbornly small” and rely on debt financing from banks as main source of funding.
- The concept of exit and serial entrepreneurship are foreign to the Italian business traditional culture. Companies are mostly perceived as “life-long enterprises”. Selling a company or stepping aside is typically perceived as a failure rather than a success.
- The business approach in Italy is inspired by “gradualism” and “pragmatism”. Rather than grow with venture capital, the money for developing a business idea is supposed to come from revenue. This implies longer development cycles and product concepts that are strongly influenced by customer requirements that often drive the business far from its original focus on innovation. Additionally Italian entrepreneurs are used to keeping both feet grounded. As a consequence, when they face venture capitalists their plans sound like micro-initiatives with modest goals that do not underscore value creation that can be shared with investors.
- Italian companies have crowded operations and technical departments, while there is a substantial lack of managerial competence in corporate strategy, marketing, product management, finance, HR, legal, and so on - which are critical for the growth and success of the company.

While this is the dominant cultural heritage in Italy, there is a new wave of Italian businessperson who are learning to overcome these challenges by looking at how other countries have surmounted these obstacles. Often this new wave of entrepreneurs is thinking globally, as they start and grow their businesses both in Italy and abroad¹⁵. These entrepreneurs are able to go beyond the traditional boundaries, providing the vanguard to make Italy globally competitive and innovative.

At the present time, there are limited data about new technology-based startups. A growing number of spin offs have been created in Italy as a sign that entrepreneurship among scientists and researchers is growing. In the last few years approximately 800 academic spin-offs¹⁶ were founded; since 2005, over 100 new technology-based companies annually originated from universities.

Figure 12: Spin off of Italian Universities and Public Research Centers

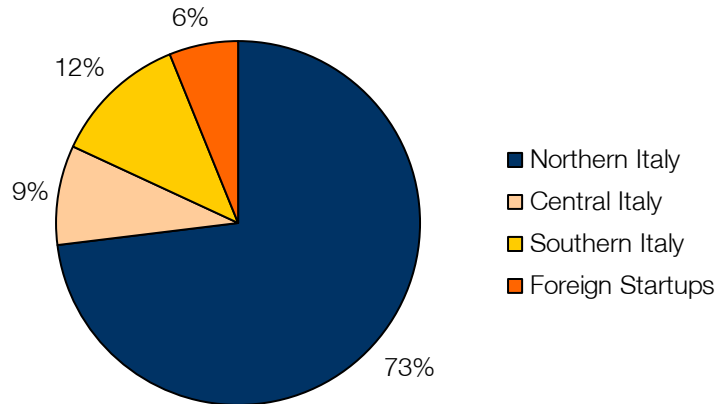


Source: Balderi & Piccaluga, *Settimo Rapporto Netval sulla Valorizzazione della Ricerca nelle Università Italiane*, Marzo 2010.

More importantly, a new business approach is emerging. Based on a 2010 survey from the [Mind the Bridge Foundation](#), several characteristics were identified with this new generation of start-up companies:

- 45% are Web-based firms
- 73% originate in Northern Italy
- 16% are incubated in a technology park
- 19% are an academic spin-off
- The founder's team is composed of 3/4 people, while only 9% have just one founder
- 97% are looking for funding
- Initial capital investment is €34k
- 19% received some external funding (mostly research grants)

Figure 13: Italian Startups by Geography

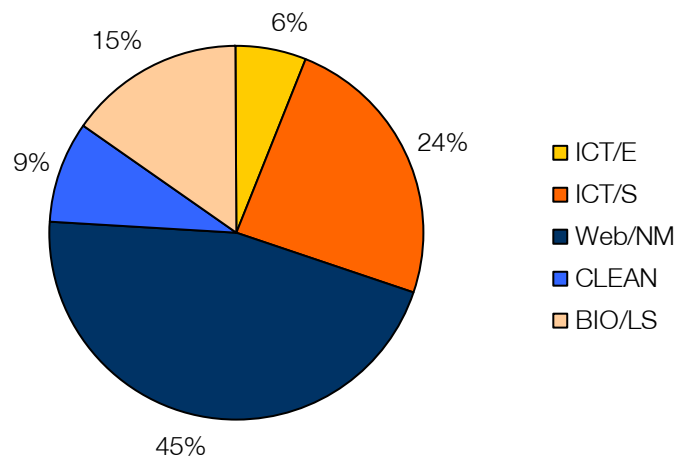


Source: Mind the Bridge - CrESIT 2010.

Below is a depiction of the profile of entrepreneurs who have launched these new high tech startups:

- He/she is 34
- 87% is male, while 13% is female
- 62% has a scientific/technological background, while 38% has a business/humanistic education
- 42% holds a Ph.D. or MBA and 13% of them got it abroad
- Only 6% does not hold a university degree
- 35% has prior entrepreneurial experience

Figure 14: Italian Startups by Industry

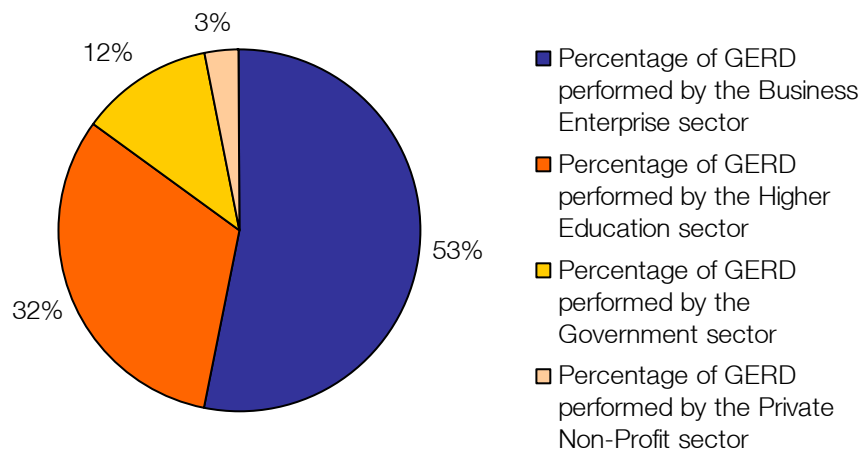


Source: Mind the Bridge - CrESIT 2010.

This emerging entrepreneurial approach can leverage the solid research and knowledge base that is traditionally available in Italy. Although there is still considerable room for improvement, in recent years Italy registered a gradual but significant increase in R&D expenditure. From 2003 to 2008, the cumulative R&D investments made by private companies, public administration entities, non for profit private institutions and universities all together increased from € 14.8 billion up to € 19.3 billion, which equates to annual growth in real terms of 6%. The positive trend in the growth of R&D expenditures is confirmed also if compared to GDP. The R&D expenditure as percentage of GDP increased from 1.05% up to 1.23% from 2007 through 2008.

The most significant contribution to the Gross Domestic Expenditure on Research and Development (GERD) comes from the private sector with a quota of 53% over the total amount. Universities contribute for 32%, while other public institutions for 13% and non for profit private institutions for 3%.

Figure 16: % GD Expenditure on Research and Development by Sector (2008)



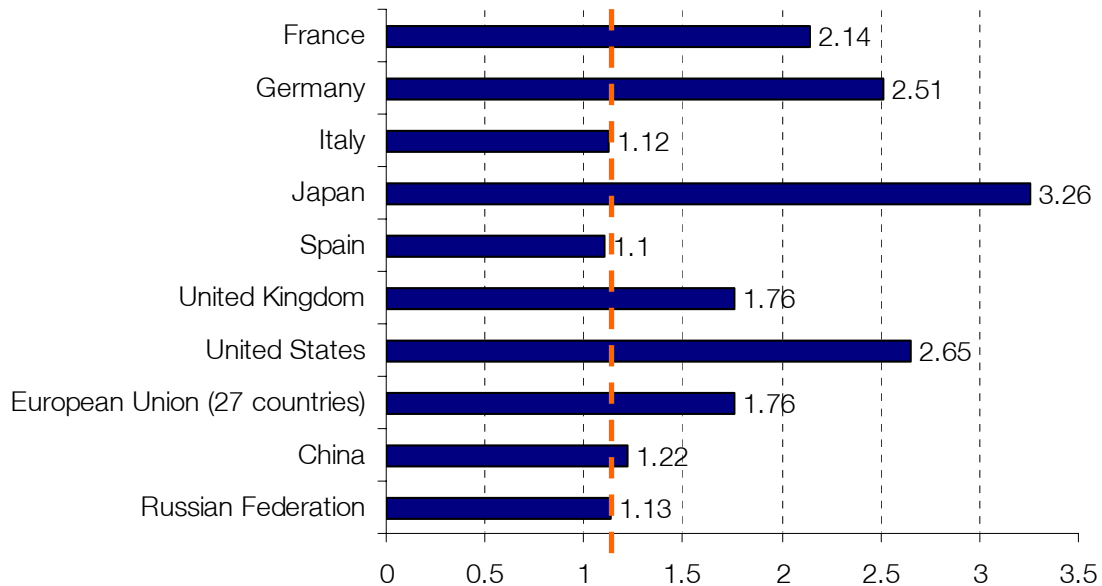
Source: OECD, 2011.

Table 3: R&D expenditure as percentage of GDP

	2000	2001	2002	2003	2004	2005	2006	2007	2008
France	2.15	2.2	2.23	2.17	2.15	2.1	2.1	2.07	2.11
Germany	2.45	2.46	2.49	2.52	2.49	2.49	2.53	2.53	2.68
Italy	1.05	1.09	1.13	1.11	1.1	1.09	1.13	1.18	1.23
Japan	3.04	3.12	3.17	3.2	3.17	3.32	3.4	3.44	3.44
Spain	0.91	0.91	0.99	1.05	1.06	1.12	1.2	1.27	1.35
United Kingdom	1.81	1.79	1.79	1.75	1.68	1.73	1.75	1.78	1.77
United States	2.71	2.72	2.62	2.61	2.54	2.57	2.61	2.67	2.79
European Union (27 countries)	1.74	1.75	1.76	1.76	1.73	1.74	1.77	1.77	1.84
China	0.9	0.95	1.07	1.13	1.23	1.34	1.42	1.44	1.54
Russian Federation	1.05	1.18	1.25	1.28	1.15	1.07	1.07	1.12	1.03

Source: OECD, 2011.

Figure 17: R&D expenditure as percentage of GDP
(Average 2003-2008)



Source: OECD, 2011.

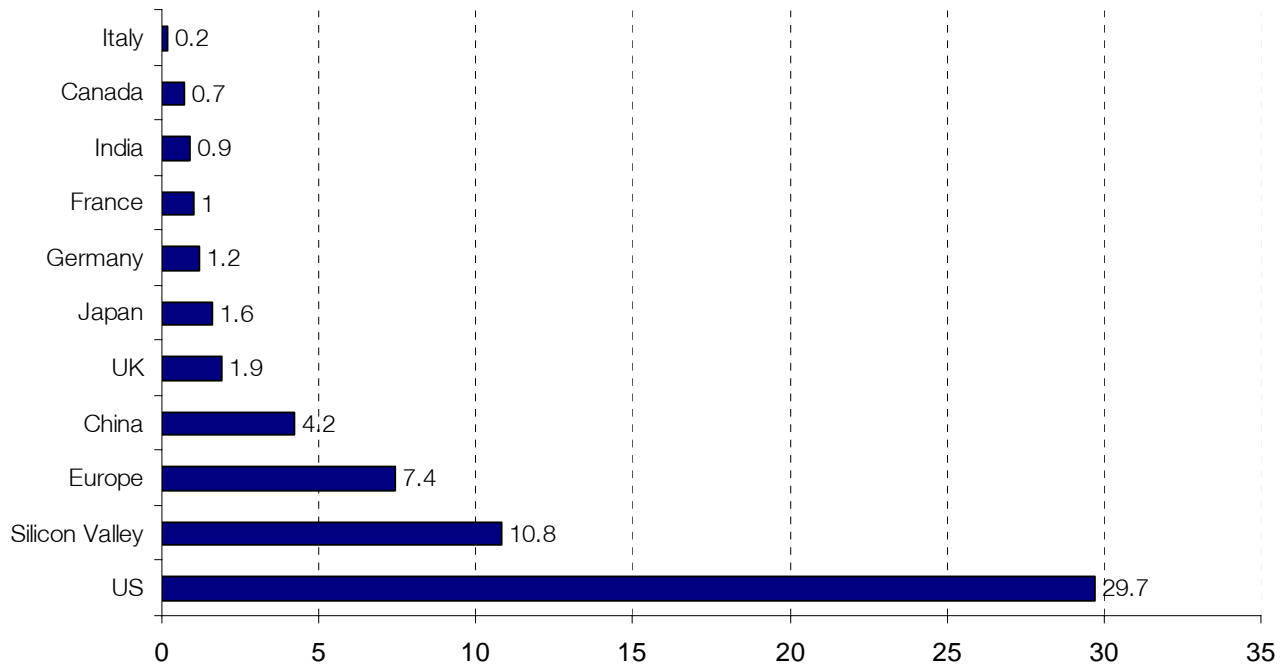
Although Italian R&D expenditure remains below the EU average and significantly below US and Japan, the high quality of research occurring in the Italian infrastructure as well as the strength of Italy's scientific community and the gradual but constant increase in the number of patents and clinical trials are interesting features that emerge from the most recent reports on research outcomes.

From 1998-2008, Italy has ranked 8th in the global classification of scientific publication, with over 400,000 articles (Thomson Reuters 2008). This number is significantly higher than countries such as Spain (below 300,000 publications) and is not far behind France (548,000). If we consider the number of citations an article gets, Italy positions itself in 7th place (Thomson Reuters 2008). This index is important since it correlates with quality the quality and scientific relevance of research outcomes.

Another important criteria to be taken into consideration is the number of triadic patents filed at the three larger patent offices: the European Patent Office (EPO), the United States Patent and Trademark Office (USPTO) and the Japan Patent Office (JPO). The last statistics available (ICE 2009) - referred to the time period 2001-2006 - suggest that for Italy patent filing increased by 21%.

If we look at research outputs in the life science and biotech field, Ernst & Young (2010) reports 233 clinical trials in progress in 2009¹⁷., definitively higher if compared to the same number two years ago (in 2008 it was 147).

Figure 18: Annual VC Investments Billion of US \$
(2008)



Source: Dow Jones Venture Source, AIFI – PricewaterhouseCoopers, 2009.

Italy is still experiencing a significant lack of venture capital activity and the venture capital industry is small compared to the other European countries, not to mention the US - specifically Silicon Valley. The chart above provides an international comparison of venture capital investments. Italian venture capital investments are lower than \$200,000¹⁸, while Germany and France invest over \$1 million and UK slightly less than \$2 million.

However, the venture capital industry, though in its infancy, is growing in Italy. There are several active seed and venture capital funds, both private and public or a combination of the two. These firms could support prospective foreign players by co-investing in early stage companies.

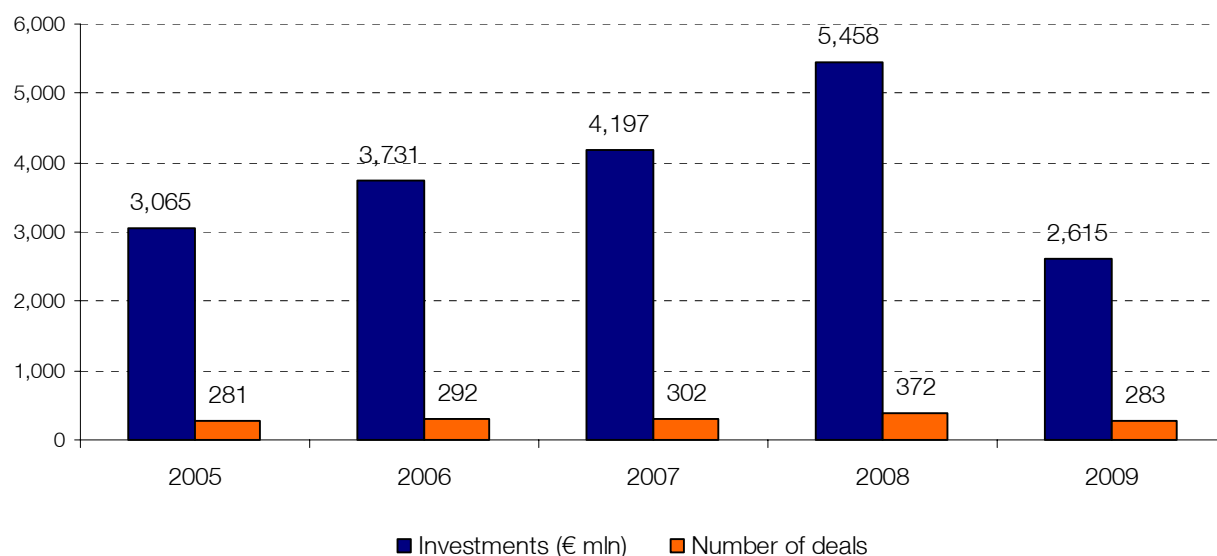
In the last five years 373 innovative start-ups were able to attract funding, 75 per year on average. Venture capital investments grew by 40% per year from 2005 to 2008. In 2009, despite the worldwide financial crisis, €98 million was invested, meaning that venture capital investments in Italy declined only by 14% vs. 37% in Europe¹⁹.

Table 4: Evolution of Private Equity and Venture Capital Investments in Italy

Total Investments	2005	2006	2007	2008	2009
Investments (€ mln)	3,065	3,731	4,197	5,458	2,615
Number of deals	281	292	302	372	283
% Variation of investments from previous year	107%	22%	12,5%	30%	-52%

Source: AIFI - PricewaterhouseCoopers 2009.

Figure 19: Evolution of Private Equity and Venture Capital Investments in Italy



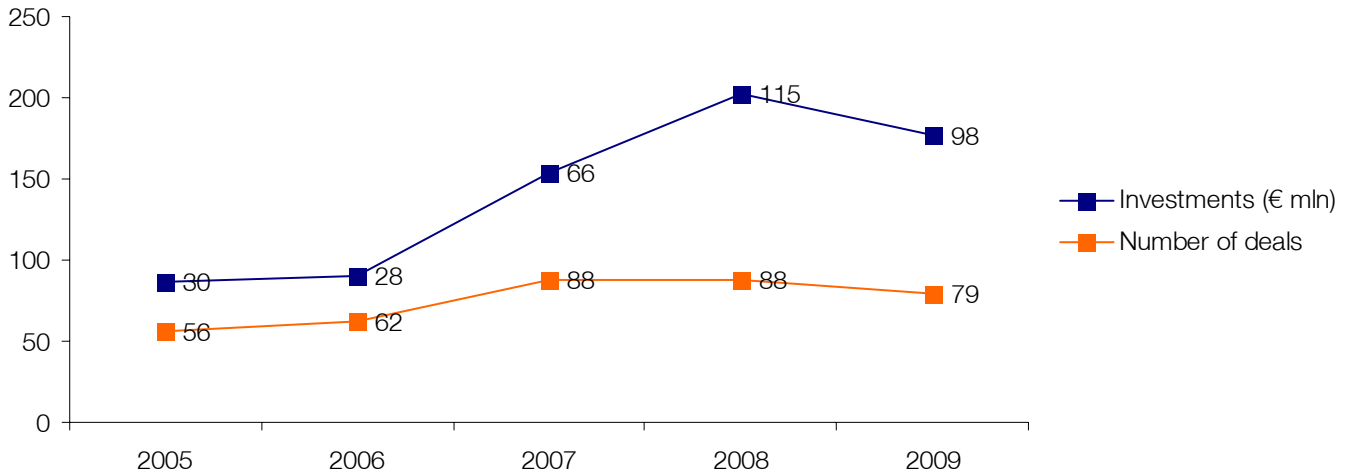
Source: AIFI - PricewaterhouseCoopers 2009.

Table 5: Venture Capital Investments in Italy

Early Stage investments	2005	2006	2007	2008	2009
Investments (€ mln)	30	28	66	115	98
Number of deals	56	62	88	88	79
Average Investment per deal in Early stage (€ mln)	0.54	0.5	0.7	1.3	1.2

Source: AIFI - PricewaterhouseCoopers 2009.

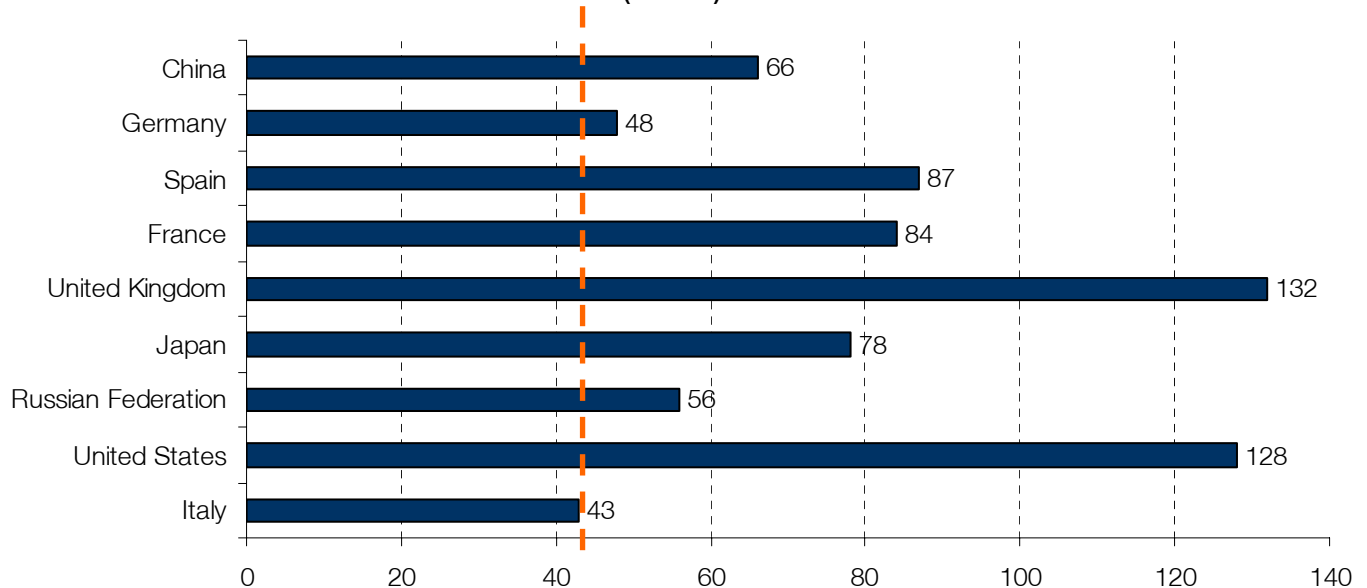
Figure 20: Evolution of Venture Capital Investments in Italy



Source: AIFI - PricewaterhouseCoopers 2009.

A lack of large companies makes an exit strategy difficult, at least in the domestic market. Similarly the small size of the stock market does not help. As shown in Figure 21, the stock market capitalization to GDP ratio is in Italy slightly above 40%, versus 128% in the US and 132% in the UK²⁰.

Figure 21: Market Capitalization of listed companies (%GDP)



Source: The World Bank, 2010.

FOREIGN DIRECT INVESTMENT

Since Italy's adoption of the Euro, foreign direct investment, except in 2000 and 2003, has registered a net outflow. Interestingly, this is not consistent with the country's current account deficits. That is, capital flows inward through portfolio investment and purchases of government debt. But Italian companies have been investing more abroad than foreign firms invest in Italy. The following table shows the aggregate figures for the decade. One sees that inward-flowing direct investments peaked in 2006-2007, before reversing in 2008 and dropping sharply in 2009-10. Outward-flowing investment peaked in 2007-08, before dropping in the financial crisis.

Table 1: Foreign Direct Investment in Italy, 2000-2010
(Billions of euro)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Italians investing abroad	-13.2	-23.9	-18.2	-8	-15.5	-33.6	-33.5	-66.3	-45.6	-28.2	-10.9
Investment into Italy	14.5	16.6	15.5	14.5	13.5	16	31.2	29.4	-9.3	12.3	3.2
NET FDI	1.3	-7.3	-2.7	6.5	-2	-17.6	-2.3	-37.9	-54.9	-15.9	-7.7

Source: Banca d'Italia, *Economic Bulletins, statistical appendicse, 2000-2010*.

Some finer-textured, monthly data is available from the Banca d'Italia historical data base. Take 2009, for example. In January of that year, foreigners bought €3.432 billion of private corporations in Italy, but sold €1.844 billion for a net investment of €1.587 billion. The same month, financial companies bought €797 million, but sold €400.5 million, for a net acquisition of €396.9 million. As the table above indicates, 2007 was a more active year for FDI, both in and out of Italy. In the last quarter of that year, foreigners bought €53.4 billion of private firms, but sold €48.3 billion for a net gain of €5.1 billion.²¹ As of 2008, the largest, national sources of foreign investment in Italy were the Netherlands (\$81 billion), France (\$45 billion), the UK (\$35 billion), Luxembourg (\$34 billion), and the USA (\$31 billion).²² The United States, however, has the largest number of companies (2,400) and the most employees (283,000), followed by Germany and Switzerland.²³

To get some sense of the sectors into which capital was flowing, and what sectors were investing outward, it is necessary to turn to the OECD database. Here the detailed data is only current through 2007, with some broader sectors through 2008. Nonetheless, one can see that manufacturing dominated in 2005, whereas financial services were dominant in 2007. One also notes that outflowing manufacturing investment increased from 2005 to 2007, before dropping off again in the financial crisis. And finance companies made huge outward investments in all three years. In 2007, outward investment in petroleum of €21 billion stands out.

Table 2: Italy's FDI Flows by Sector

	2005	2006	2007	2008	2009	2010 (J-N)
Foreign direct investment inflow (€)	16,062	31,279	29,373	-9,355	12,336	3,209
Manufacturing	10,097	6,482	5,284	3,821	n/a	n/a
Textiles	461	646	957			
Petroleum	772	285	305			
Mechanical products	272	796	1,057			
Office equipment	-2	668	840			
Radio/tv	768	863	1,437			
Motor vehicles	-8	1,503	495			
Electric/gas/water	1,810	1,722	1,837	2,768		
Transport/logistics/communications	-3,227	1,626	3,943	1,416		
Financial intermediation	1,105	13,421	10,228	-3,275		
Foreign direct investment outflow (€)	-33,633	-33,534	-66,327	-45,595	-28,195	-10,963
Manufacturing	6,302	7,813	9,690	5,885	n/a	n/a
Textiles	329	225	557			
Petroleum	1,824	2,254	21,188			
Mechanical products	615	449	1,043			
Office equipment	790	1,184	1,218			
Radio/tv	1,391	1,402	1,836			
Motor vehicles	227	475	361			
Electric/gas/water	122	165	1,593	428		
Transport/logistics/communications	114	717	1,232	-369		
Financial intermediation	22,445	13,884	23,455			
Net FDI	-17,571	-2,215	-36,954	54,950	-15,859	7,754

Source: Data extracted from OECD.Stat, 19 May, 2010.

Finally, the United Nations, *World Investment Report* provides data on cross-border mergers and acquisitions. Here, one sees foreign firms most active between 2005 and 2007, while Italian firms clearly peaked in 2007 [ENEL, the Italian utility, purchased the Spanish utility, Endesa, for €42 billion.] Italian buyers continued doing deals through 2009.

Cross-border Mergers & Acquisitions by Foreign Firms purchasing Italian Companies

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Number	129	62	61	72	118	111	140	150	85	25
Value*	2,739	8,889	8,931	17,044	40,445	25,760	23,630	-2,377	1,109	3,351

Number of Cross-border Mergers & Acquisitions by Italian Purchasers

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Number	132	61	39	12	52	59	129	119	48	19
Value*	6,031	1,910	-2,408	3,325	23,565	6,887	55,880	21,358	17,505	-666

*millions of US dollars

Source: United Nations, *World Investment Report*, 2010.

The Italian Trade Commission (ICE) reported (in January 2009) that 7,162 foreign companies were operating in Italy, with overall sales of €429.5 billion. They employed 853,000 workers. However, the stock of FDI, at 12% of GDP, was lower than that of Italy's major European competitors. There was, as well, a distinct regional component to FDI in Italy. Some 77% of foreign firms operated in the north, with 46% in Lombardy alone.²⁴

Somewhat different statistics were reported in December 2009, by Istat (Istituto nazionale di statistica). It published figures showing some 14,400 foreign-controlled firms were operating in Italy – employing 1.2 million workers. They accounted for 16% of industrial and services turnover, 12.9% of investment, 27.4% of R&D expenditures and 21% of exports.²⁵

“The Government of Italy,” opines the U.S. Department of State, “maintains a welcoming posture to foreign investment...” While the State Department was still critical of rigid labor laws, inefficient public services and the high input cost of taxes, it appreciated the tax benefits for start-ups and efforts to reduce red tape.²⁶ Tax incentives for investing in depressed regions, particularly in Southern Italy, apply equally to foreign and domestic firms. Eleven technology districts, to facilitate cooperation between researchers and venture capitalists, also apply equally.

Italy has bilateral investment treaties with 96 nations (although not with the United States), and provides national treatment to foreign investors (excepting subsidies for the film industry, capital requirements for banks, and restrictions on non-EU-based airlines). Foreign investors may invest in privatized companies, although the Italian government generally retains a “golden share” in its major firms.

In dispute resolution, “though slow,” the Italian legal system meets generally recognized principles of international law. Italy is a member of the World Bank's International Center for the Settlement of Investment Disputes (ICSID), and recently enacted bankruptcy regulations analogous to U.S. Chapter 11 restructuring.²⁷

As to protection of intellectual property, Italy has had serious problems. However, the Economic Development Ministry in 2009 created a General Directorate for Intellectual Property, to collect better data on intellectual property protection and to educate business on the importance of IPP.

Bank credit is readily available in Italy to foreign investors; equity less so. Financial service companies incorporated in another EU member states may also offer investment services and products in Italy, and there are no restrictions on foreigners engaging in portfolio investment in Italy. “As of 2008, 82 subsidiaries of foreign (financial) groups accounted for 11.7 percent of (the financial) system assets.”²⁸

Public-purchasing contracts are generally open to all comers, yet the process is sometimes opaque. The European Commission has, on occasion, found that tendering by local authorities has not complied with EU rules on open competition.²⁹

Considerable progress has been made with the introduction of one-stop shops (Sportello Unico), in local councils. This provides “a single reference point for potential investors seeking information, advise and authorizations.” Some public-sector agencies have online one-stop shops. Law n. 133/2008, enacted in 2008, stipulated a 25% reduction in administrative burden by 2012.³⁰ And the Berlusconi government has made administrative efficiency a priority. Building and related permits also receive one-stop shop procedures, pursuant to decree n. 112/1998. Foreign corporations and limited-liability companies are now required to register with the Chamber of Commerce (where the company will be located), but can then benefit from a one-stop process for many of Italy’s registration requirements.

Real-estate acquisitions in Italy must be via a notary public, who must check for any barriers to the sale. Yet most foreigners will not encounter any problems acquiring commercial or industrial land.³¹

For the south, where economic development lagged, Italy created Invitalia – a foreign-investment-promotion agency, in 2003. For companies planning to invest at least €40 million, the Italian government would provide loans or interest-rate subsidies. These incentives were available for feasibility studies, purchases of land, manufacturing facilities, new equipment, software and patents.

Italy also provides export incentives, in the form of tax refunds and financial assistance. These incentives are managed by Simest³².

GROWTH AND PRODUCTIVITY PROSPECTS

The government is now projecting real GDP growth at 1.2% annually, 2011-2013. Inflation is thought to remain low (1.6%), with unemployment constant (8.7%).³³

Similar statistics were reported in December 2010 by OECD. The following table shows the prospect figures in international comparison. Real GDP in Italy is forecast to grow less than the average of the Euro Area. On the other hand, unemployment rates are lower than the average of the Euro area.

	Real GDP			Consumer Price Index			Unemployment		
	2010	2011	2012	2010	2011	2012	2010	2011	2012
Italy	1.04	1.31	1.61	1.55	1.5	1.39	8.57	8.53	8.28
France	1.61	1.61	2.04	1.48	1.19	1.25	9.32	9.09	8.84
Spain	-0.18	0.85	1.82	na	na	na	19.8	19.07	17.35
Germany	3.5	2.54	2.23	na	na	na	6.9	6.3	6.19
UK	1.76	1.72	1.95	na	na	na	7.88	7.84	7.64
USA	2.71	2.23	3.13	1.56	1.05	1.05	9.66	9.5	8.65
Japan	3.68	1.73	1.31	-0.88	-0.82	-0.48	5.05	4.85	4.45
China	na	na	na	3.06	3.27	3.01	na	na	na
Russian Federation	na	na	na	6.8	7.68	6.02	na	na	na
Euro Area	1.71	1.65	1.98	na	na	na	na	na	na
Euro Area (14)	na	na	na	na	na	na	9.86	9.64	9.23

Source: *Economic Outlook No 88 - December 2010 - Annual Projections for OECD Countries*

RECOMMENDATIONS TO THE ITALIAN GOVERNMENT

1. Labor markets must become more flexible.

Rigidity in terminating employees represents a barrier to investments both for startups (that by definition need flexibility) and foreign entities (particularly US companies are used to “at will” employment schemes). Reforming the employment law in the direction of more flexibility (at least for companies operating in the high tech industries) could boost company creation and foreign investments.

2. Investing in Italy must become even more simple, fast, and inexpensive

Government should reduce the costs of doing business and create a true, electronic one-stop shop for investment. As successfully proven in other countries such as Singapore and Saudi Arabia, the OSS could facilitate and accelerate foreign investments by short-circuiting and bypassing lengthy bureaucratic and administrative procedures and providing investors with a single point of contact for all dealings with the Italian authorities, both at national, regional and local level. Additionally, government should try to streamline judiciary for commercial cases.

3. Starting up a company in Italy must become more simple and less expensive

In Italy incorporating a new company (as well as closing an existing business) is neither an easy nor inexpensive process. There are still legal and fiscal barriers to entry to the corporate market that make Italy as of today not a “corporate haven”. Government should reduce the costs of doing business and create a true, electronic one-stop shop for investment. On this side measures aimed at reducing the administrative burdens to Italian corporate are in the government agenda but further effort is required.

4. Fiscal deficit must be reduced

Government should continue in its effort to lower the fiscal deficit, preferably to a percent of GDP that is below the real GDP growth rate. Judging from the existing budget, this entails spending cuts in anything but infrastructure, education and R&D. Pensions and retirement ages, revenue sharing with provinces and welfare should all be cut or curtailed. Additionally wages should be tied to productivity growth and grow slower than productivity. Unit labor costs must be brought back into competitive condition with other European Union countries.

5. Equity capital must be more readily available to Italian entrepreneurs.

Government should incentivize equity investments to Italian companies as well as support the exit process. With regards to this it is key to provide support both to the venture capital funds and companies interested in acquiring Italian technology startups.

CONCLUSION

This paper provides additional data and facts which lends the current broad perception some crucial context. There are issues, but the concept of “Italy in decline” is likely overemphasized. Italy still plays a role in the international markets. Thanks to its SMEs, Italy’s future will be based on the strength and diversity of its unique business community – rooted in a vibrant entrepreneurial spirit.

There is no question that structural reforms as suggested above are needed to leverage these strengths to deliver growth. These reforms can further stimulate an economy that still remains the world’s 7th largest.

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¹⁶ It includes spin-offs both from universities and public research centres and institutions such as CNR, ENEA, INFN, INFN-CNR, INFS).

¹⁷ These data take into consideration only products at the preclinical and clinical development stage; and do not include projects at the discovery stage.

¹⁸ Private equity deals still represent the biggest part of equity transactions in Italy. Of the € 3.8 billion invested yearly (avg. 2005-2009), approximately only € 70 million (avg. 2005-2009) went to early-stage investments (AIFI - PricewaterhouseCoopers 2005-2009).

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