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INTERNATIONALIZATION OF LOMBARDY-BASED COMPANIES

By R&P and Confindustria Lombardia

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CONFINDUSTRIA
LOMBARDIA

THE INTERNATIONALIZATION
OF LOMBARD COMPANIES

Final Report

Prepared by R&P and Confindustria Lombardia

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Overview

This report presents the main findings of the Confindustria Lombardia investigation into Lombard companies' international activities; now a well-established annual exercise, the investigation has once again relied on a survey conducted directly among the member firms of the trade associations within Confindustria Lombardia.

The investigation's findings have proved highly worthwhile for a number of reasons; three of them, at least, deserve particular emphasis.

First, the present stage of the serious economic crisis with which Italy has been struggling for the last six years features a dramatic and worsening decline in the various components of aggregate domestic demand; in such a situation the ability of Italian businesses to tackle international markets and successfully seize new opportunities has become crucial to their very survival.

The second reason is the fact that Lombardy has always been the power-house of the Italian economy in general and of its international activities in particular, accounting for the bulk not only of exports but also of direct investment by Italians abroad and by foreign firms in Italy: this makes Lombardy a "laboratory" of very great importance to any assessment of wider trends affecting the country as a whole.

Thirdly, the extensive nature of the field sample surveyed, which makes it highly representative of the region's businesses and their current situation. The survey was carried out towards the end of 2012 by means of a structured questionnaire administered by Confindustria Lombardia's various trade associations to their member firms. Some 4,000 firms helped to provide data, nearly 2,700 of which reported some kind of relationship abroad, whether by trading (exports and/or imports) and/or direct investment either outward (controlling interests, half-shares or minority shareholdings in foreign firms) or inward (stakes in the firm held by non-Italian companies or venture capital groups). 1,099 of those firms joined in the research by completing every part of the questionnaire: that is the sample analysed for the present Report.

Chapter 1 is devoted to a summary of the overall situation, designed to put the international activities of Italian firms in their national and international context in terms both of international trade and of direct investment to and from abroad (the latter providing an important indication of Lombardy's attractiveness and competitiveness).

The other chapters set out the findings of the survey conducted directly among those of Lombardy's companies which do business outside Italy. Chapter 2 studies the various ways in which respondent firms maintain their presence abroad in the process of international trading and manufacturing activities.

Chapter 3 is devoted to discussion of the geographical targets of Lombard and multinational companies' present and planned commercial expansion; it gives a breakdown by country of their current exports and/or direct presence abroad, and describes the geographical diversification of their activities abroad, and the main thrust of the planned development of their various kinds of activity outside Italy in the three-year period 2013-2015.

Lastly, Chapter 4 concentrates on the obstacles which firms encounter as they venture into foreign markets, and on the services offered by the various organizations engaged in one way or another in supporting their international business activities.

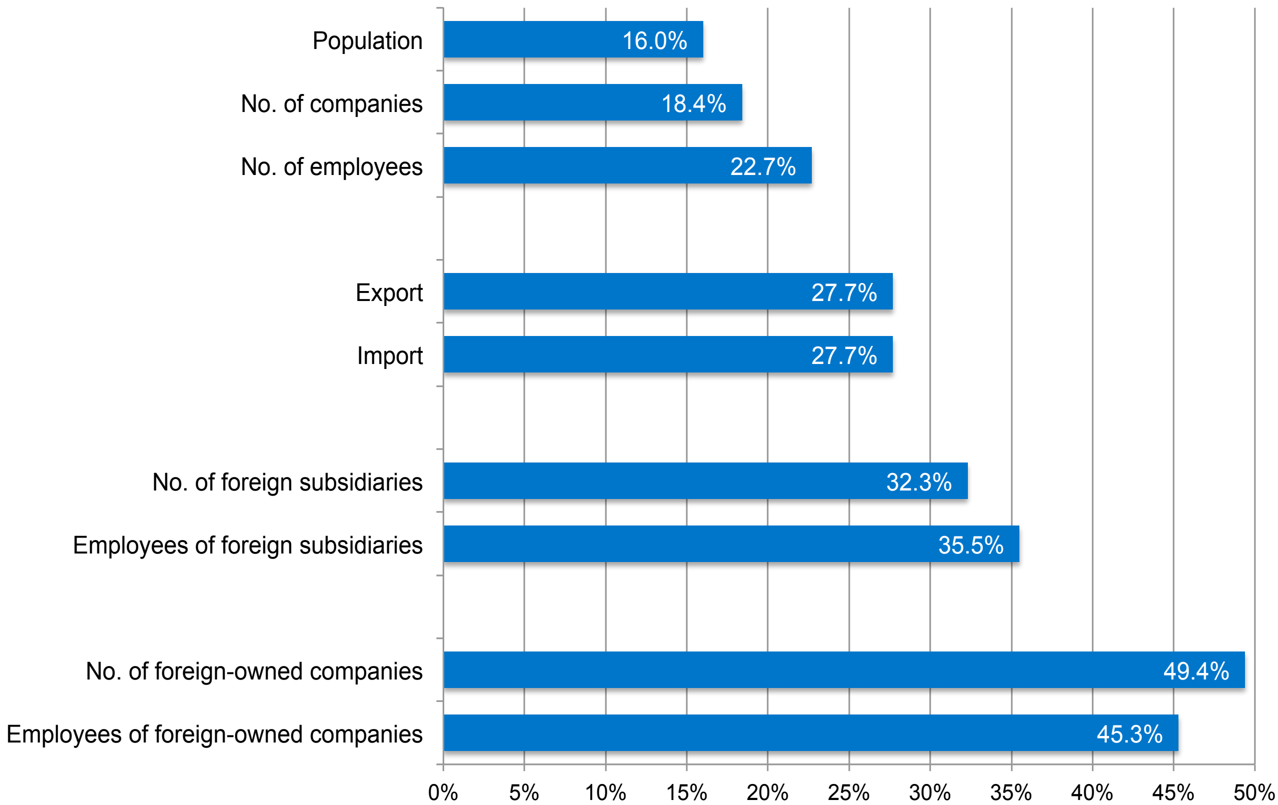
1. Overview

1.1 International expansion: Lombardy's leading role

Compared with the Italian economy as a whole, the Lombardy region has always punched well above its demographic weight. By the latest count, Lombardy has some 9.7m inhabitants, which is 16% of the Italian population. In 2010, the ASIA database (Archivio Statistico delle Imprese Attive) of the national statistical service Istat recorded over 820,000 active firms based in the region, or 18.4% of the national total; altogether more than 3,927,000 people work in them, 22.7% of the total Italian workforce.

Lombardy's leading role in the country as a whole is brought out even more strongly by the figures for international activity in trade and production (see Fig. 1.1): 27.7% of all Italian exports came from Lombardy in 2012, and the region accounted for the same proportion of the country's imports; it bulks even larger in terms of the figures for foreign direct investment (FDI).

Figure 1.1
Lombardy's share of the Italian total on various measures of economic activity, domestic and international



Source: Istat (coeweb database) and Reprint database.

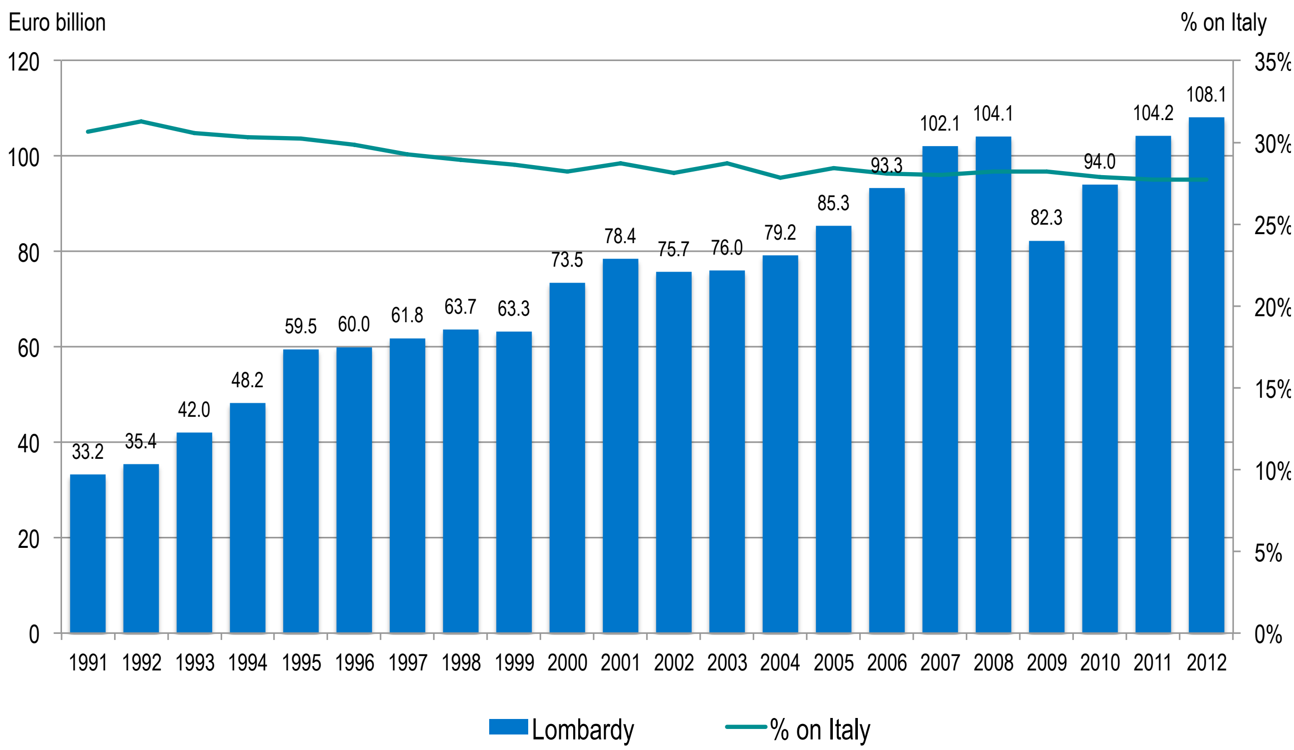
So far as outward foreign direct investment activity is concerned, Lombardy accounts for 32.3% by number of all Italian firms' holdings in foreign companies; in terms of those subsidiaries' staff numbers, that proportion is even higher (35.5%). The "club" of Lombardy's multinational enterprises– all those firms with an established presence abroad – now has nearly 2,300 members, mainly small and medium-sized enterprises (SMEs) which move into the international limelight by investing abroad through acquisitions or greenfield investments, and/or by means of subsidiaries and joint ventures engaged in trade, manufacturing or services.

On the inward foreign direct investment front, Lombardy hosts almost half of Italy's firms wholly or partially-owned or part- by foreign shareholders (49.4%); the proportion of such firms' staff is slightly lower (45.3%).

1.2 Exports

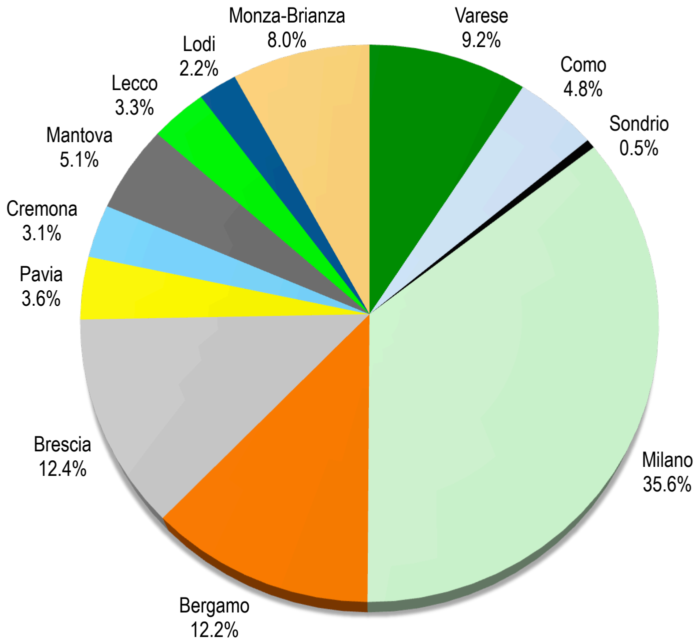
Having regained in 2011 the levels reached before the economic crisis of 2008, Lombardy's exports achieved a new record in 2012, topping €108bn (see Fig. 1.2).

Figure 1.2
Lombardy's exports, 1991-2012
(€bn and % of Italian total)



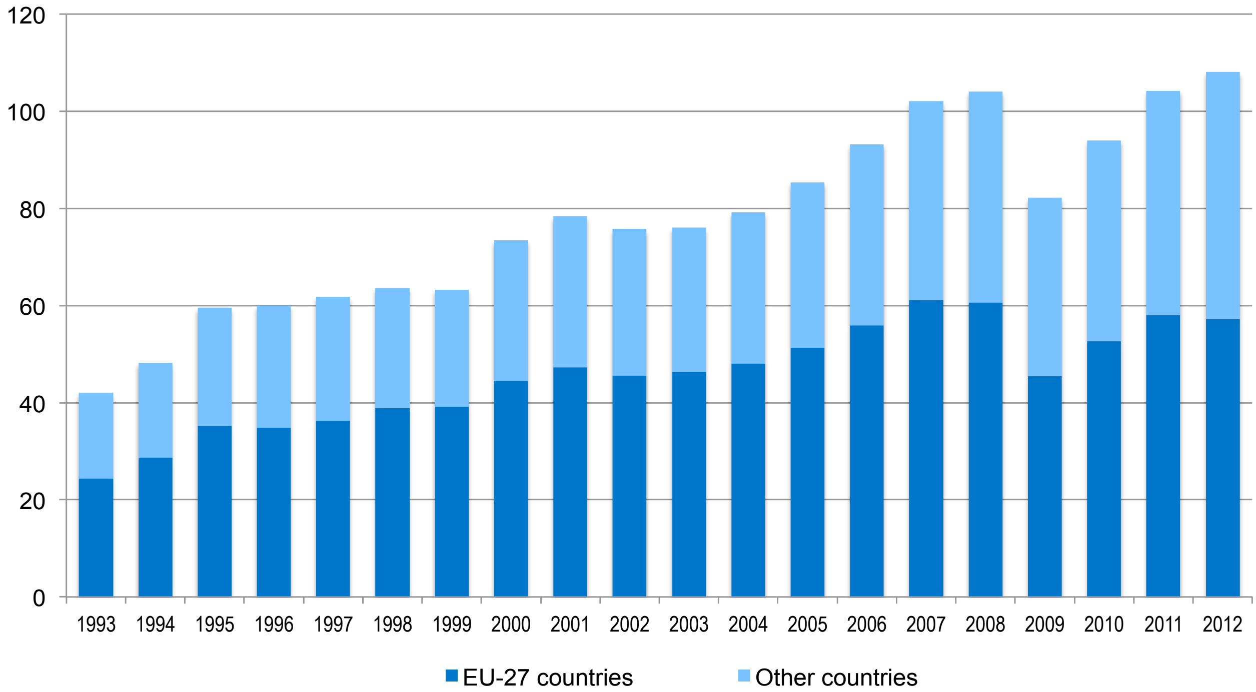
Source: Istat (coeweb database).

Figure 1.3
Breakdown of Lombardy's exports by province, 2012



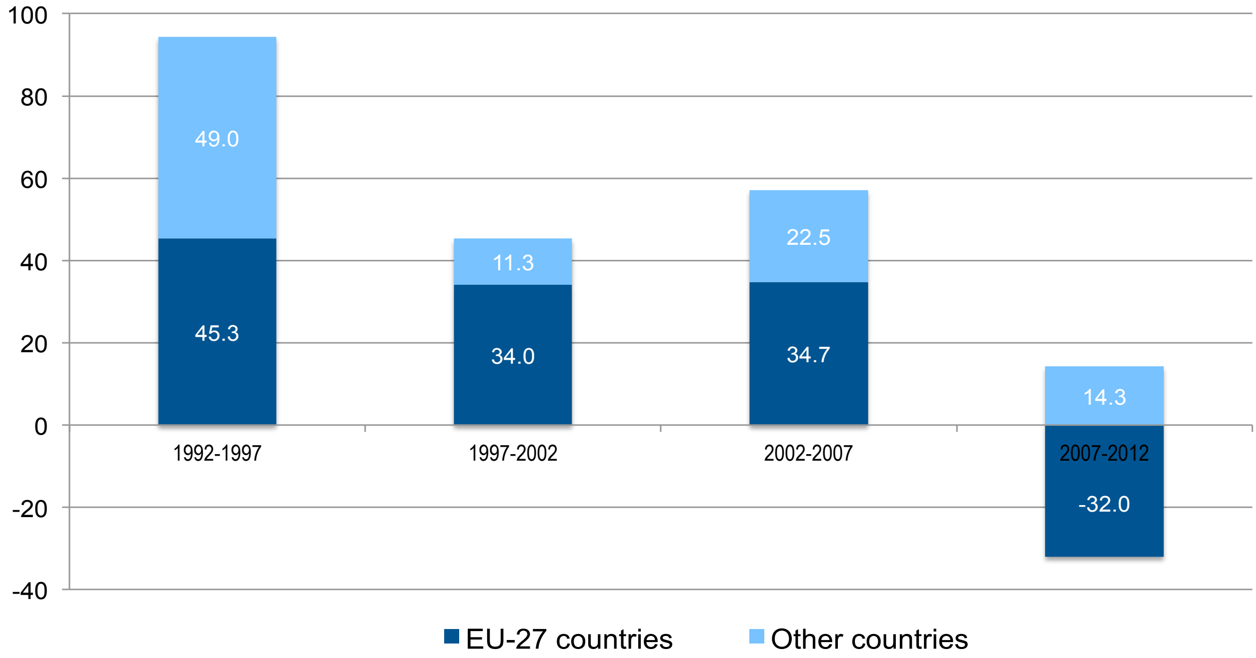
Source: Istat (coeweb database).

Figure 1.4
Breakdown of Lombardy's exports by destination, 1993-2012



Source: Istat (coeweb database).

Figure 1.5
Comulate contribution to the growth of Lombardy's exports by destination, 1993-2012 (€bn)



Cumulative contribution: sum of variations in the period compared to the first year of the period considered as base year.

Source: re-worked Istat data (coeweb database).

Lombardy's new record level of exports has been possible because growth in its exports to countries outside the European Union have made up for a decline in exports within it, as EU economies have been particularly hard hit by the crisis which began in the United States in 2007 and from 2008 onwards exploded in Europe as well (see Fig. 1.4 and Fig. 1.5)

1.3 Outward foreign direct investments

In their activity abroad – at least their outward FDIs – the response of Lombardy-based companies to the present long-lasting crisis has been somewhat different from what it had been in earlier recessions such as the oil shocks of 1992 and 2001: then, many firms had decided to ride out the crisis by refocusing their business on the domestic market, letting go some sizeable assets abroad and sometimes actually withdrawing from international markets completely.

In the last few years, by contrast, the scale of these companies' disengagement has been much smaller; indeed, it is clear that in the face of poor performance by the domestic market international business expansion is increasingly taking a central role in their strategies. One important sign of this, among others, is the completion of various cross-border M&A operations in recent years – not only by Lombardy's big and medium/big firms (some of which have strengthened their position in world markets in their particular lines of business), but also by many SMEs which have deployed worthwhile growth strategies despite the difficult macroeconomic situation.

The Financial Times database "FDI Intelligence" offers an interesting way of comparing Lombardy companies' degree of internationalization with that of firms in other European countries. The database has a worldwide record of cross-border FDIs for the launch of new business activities or the expansion of existing ones (i.e. excluding the takeover of existing businesses).

Table 1.1
Western European firms' new greenfield expansion projects involving direct investment abroad, by region of origin, 2003 – 2012

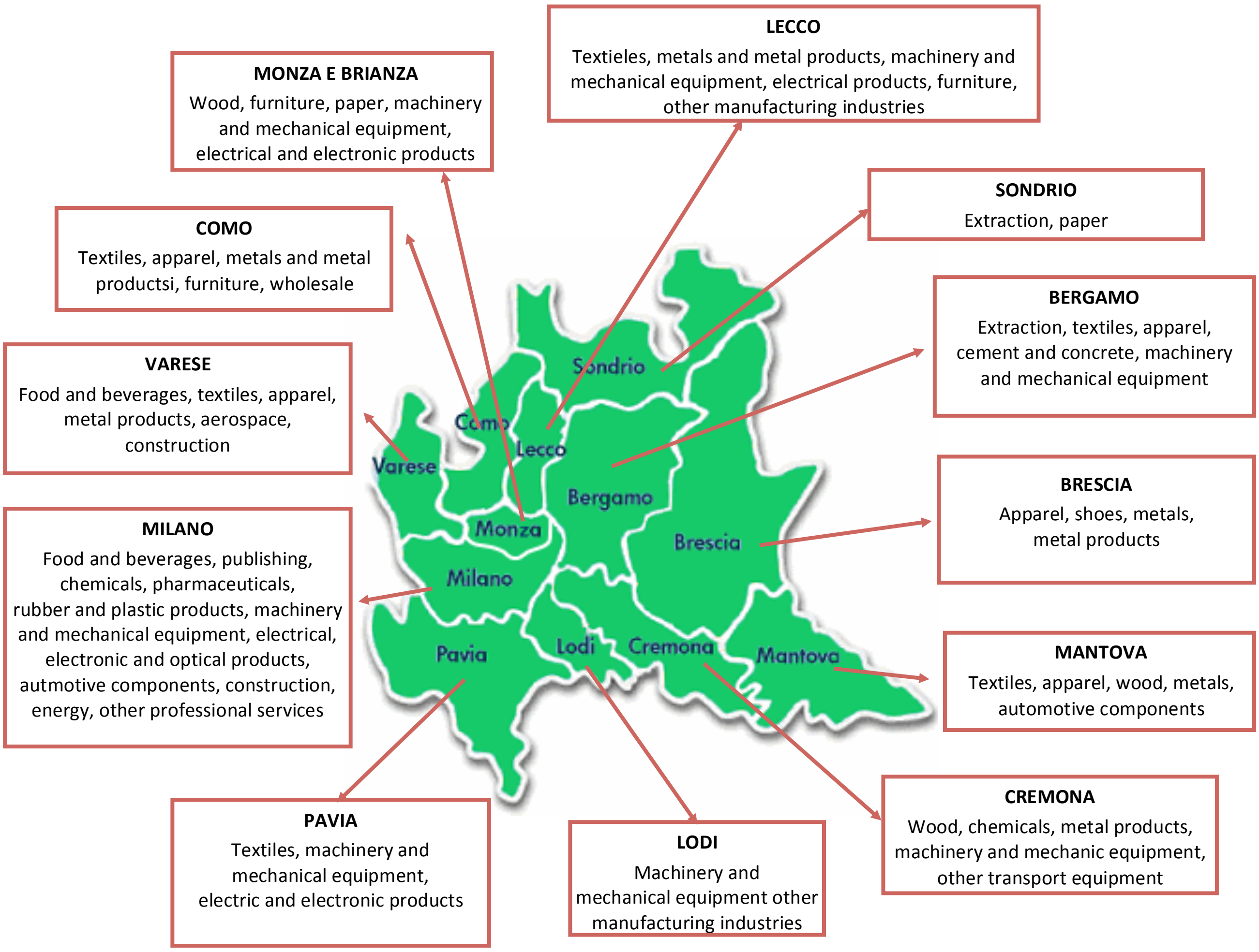
	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	Totale
South East (UK)	495	597	644	822	807	1.061	983	1.011	1.066	947	8.433
Île-de-France	369	444	482	525	671	867	789	640	623	563	5.973
Nordrhein-Westfalen	208	276	363	411	439	442	433	447	403	390	3.812
West-Nederland	196	239	191	303	252	370	341	303	305	231	2.731
Bayern	155	203	202	243	282	322	286	278	321	236	2.528
Baden-Württemberg	153	174	212	280	221	283	256	276	285	292	2.432
Östösterreich	90	121	137	191	175	201	141	135	102	70	1.363
Etela-Suomen laani	79	87	150	169	166	181	120	117	120	108	1.297
Lombardia	91	107	97	86	117	206	164	162	130	109	1.269
Comunidad de Madrid	57	68	59	81	132	165	186	178	157	137	1.220
Cataluña	29	78	64	60	139	182	190	183	138	124	1.187
Niedersachsen	65	71	53	93	92	130	112	119	118	93	946
Hessen	48	56	63	94	93	144	108	97	122	93	918
Scotland	35	22	40	43	67	73	98	86	120	87	671
Reg. Bruxelles-Cap.	38	32	70	68	103	98	60	70	62	59	660
Vlaams Gewest	22	64	54	71	68	112	70	69	67	34	631
Galicia	13	40	33	46	46	73	94	94	108	66	613
Veneto	28	57	58	58	69	74	60	60	46	44	554
Centre-Est (FR)	26	42	56	42	80	71	59	70	64	44	554
Westösterreich	21	50	35	36	50	58	48	72	80	60	510
Rheinland-Pfalz	54	28	28	45	50	50	53	57	67	56	488
Zuid-Nederland	21	52	30	33	40	69	42	69	49	40	445
Hamburg	37	28	28	27	52	54	53	52	55	54	440
Piedmont	13	29	30	48	47	63	53	52	50	53	438
Pais Vasco	12	24	23	33	44	77	61	54	70	36	434

Source: Politecnico di Milano and R&P, based on fDi Markets database, Financial Times FDI Intelligence.

Table 1.1 shows the number of new greenfield expansion projects involving direct investment abroad undertaken by Western European firms in the years 2003-2012, by region of origin of the investing company. It is easy to see that throughout the period shown Lombardy has managed to stay between eighth and eleventh place among the regions of Western Europe.

In the most recent period, too, despite the troubles connected with the economic crisis and the increasingly difficult access to credit, Lombardy has managed to remain one of Europe's most dynamic regions, and ever since 2008 has been among the top ten regions in the number of investment projects.

Figure 1.6
Le specializzazioni provinciali delle partecipazioni delle imprese lombarde all'estero



Source: based on REPRINT *database, ICE-R&P-Politecnico di Milano.*

SMEs now play a fundamental role in the Lombard economy's international growth processes: this is confirmed by the breakdown of the various industrial classifications in which its foreign subsidiaries specialize, as a function of the investing company's province of origin (see Fig. 1.6): they reflect the specialization of the local SME systems of their home territories.

This emphasizes the vitality which those systems have so far managed to show; it seems to be confirmed by the findings presented in this report, despite the serious crisis now savaging the Italian economy.

1.4 Inward foreign direct investments

When we turn to inward foreign direct investments (FDIs) – foreign firms' presence in the region, an aspect of no less importance – the effects of the crisis are certainly more evident. Total employment by foreign-owned firms active in Lombardy stopped growing some years ago, and indeed employment in industry has been steadily shrinking, compensated only in part by a rise in tertiary sector employment.

New inward investment in the most recent period has shown a steady decline in the component which does most to boost a region's economy: greenfield investment and the expansion of existing activities. This is clear from the international comparison available in the FT's FDI Intelligence database: Table 1.2 shows the number of such projects in the main Western European regions in the period 2003-2012.

Lombardy's worsening position is clear from the figures: in the first five years (2003-2007) the region was among the top ten in Europe no fewer than four times out of five for attracting new investment projects (and indeed came fifth in 2003), but has never made the top ten in any year since.

What needs stressing above all, though, is the widening of the gulf between Lombardy and the continent's more attractive regions. In 2012 Lombardy attracted only 41 investment projects, against 72 projects in 2010 and 46 in 2011; of all Western Europe's main industrialized regions, only Baden-Württemberg and Flanders show so sharp a decline.

Even more worrying is the fact that investments for the development of high-tech or R&D activities from scratch are becoming far more rare.

Admittedly new cross-border investments throughout the industrialized world now mainly take the form of acquisitions; but the increasing rarity of greenfield investments seems particularly alarming in the case of the Italy – and of Lombardy in particular.

Table 1.2
Western Europe: new greenfield expansion projects involving direct inward investment, by destination region, 2003 – 2012

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	Totale
South East (UK)	193	244	328	361	369	450	454	418	475	462	3.754
Île-de-France	53	84	194	221	215	259	151	165	151	126	1.619
Nordrhein-Westfalen	38	34	50	58	75	96	152	173	210	151	1.037
Comunidad de Madrid	51	60	48	83	131	143	90	112	78	106	902
Cataluña	66	74	53	83	103	115	100	88	95	92	869
West-Nederland	51	43	71	81	92	103	93	103	111	98	846
Bayern	44	56	54	81	96	130	88	86	83	69	787
Scotland	34	73	41	78	53	86	120	101	88	91	765
Baden-Württemberg	19	17	19	31	30	137	132	157	155	34	731
Hessen	16	14	52	55	67	90	99	108	115	51	667
Vlaams Gewest	24	79	56	58	101	80	43	94	45	29	609
Lombardy	50	45	33	62	77	82	55	72	46	41	563
North West	28	39	36	41	41	75	85	75	65	59	544
Östösterreich	33	46	50	54	71	66	50	47	50	42	509
Centre-Est (FR)	15	24	62	61	75	79	51	44	24	27	462
West Midlands	23	31	44	33	24	42	65	44	63	61	430
Berlin	27	19	25	37	32	58	57	43	65	60	423
Bassin Parisien	11	20	62	72	70	79	31	27	18	26	416
Reg. Bruxelles-Cap.	25	21	37	38	51	52	31	29	52	28	364
Est (FR)	15	36	59	63	45	64	21	17	24	15	359
Méditerranée	22	19	29	48	54	56	47	33	16	21	345
Andalucia	14	26	12	24	48	83	41	29	31	27	335
Northern Ireland	15	27	38	33	43	33	32	41	27	25	314

Source: based on Politecnico di Milano and R&P on fDi Markets database, Financial Times FDI Intelligence.

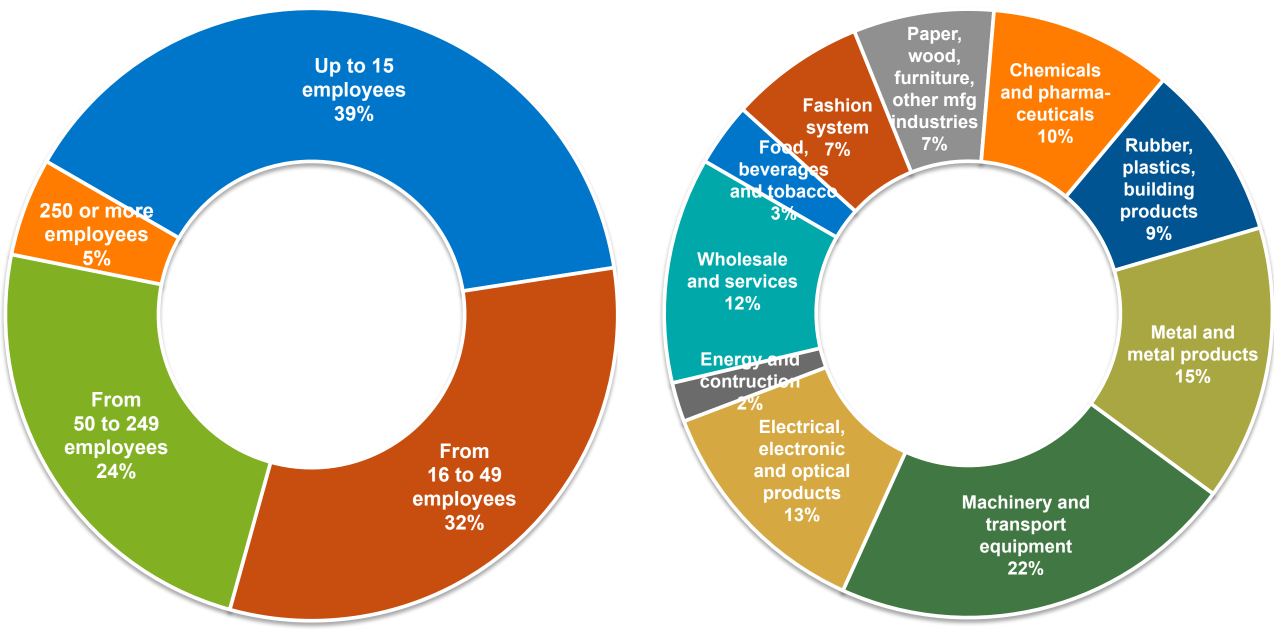
2. The qualitative survey of Lombardy-based companies: forms of international activity

2.1 The composition of the sample

The direct survey carried out in late 2012 by the local trade associations belonging to Confindustria Lombardia has furnished detailed information on the foreign dealings of 1,099 Lombardy-based companies which reported some kind of relationship abroad, whether by trading (exports and/or imports) and/or direct investment either outward (controlling interests, half-shares or minority shareholdings in foreign firms) or inward (stakes in the firm held by non-Italian groups or venture capital). The sample is accordingly a reasonably broad one, and sufficiently representative of the more dynamic portion of Lombardy's business in terms of company size and line of business.

Figure 2.1 shows the breakdown of the sample by company size and industry sector.

Figure 2.1
Breakdown of the sample of firms with dealings abroad (1,099 firms), by number of employees and industry sector



In terms of company size, "small" and "very small" enterprises are predominant, accounting for more than two thirds of the total: 39% are firms with no more than 15 employees, while another 32% have staff numbers between 16 and 49. Medium-sized firms (50-249 employees) account for just under a quarter of the sample (24%), and those with 250 or more staff make up only 5%.

In terms of industrial classification the sample of firms considered reflects the wide range of sectors which is one of Lombardy's major economic strengths. All the region's highly-competitive manufacturing sectors are well represented: metal engineering, chemical products, pharmaceuticals, rubber products, plastic products, and electrical, electronic and optical products. Nor are the traditional "Made in Italy" sectors absent (textiles, clothing, leather and footwear, wood products & furniture, etc.), nor the more advanced elements of the energy, construction and tertiary sectors.

2.2 Forms of international activity

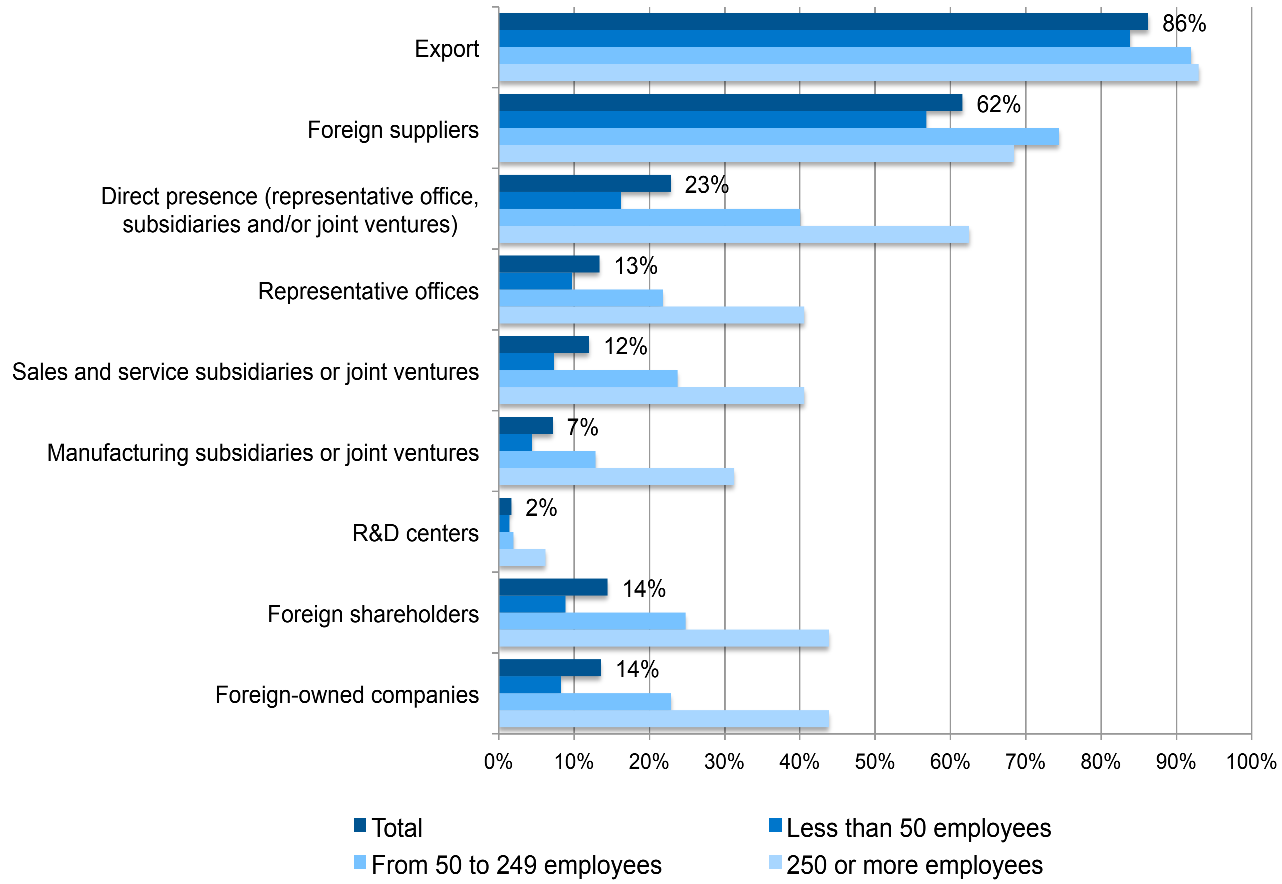
Firms were first asked what form(s) their international activity took: purely trading relationships (exports and/or imports), or a direct presence abroad of one kind or another (representative offices, holdings in foreign companies, joint ventures, sales and service and/or manufacturing affiliates, or research and development centres), or inward foreign investment (ownership of some or all of the Italian firm's shares by foreign companies or private equity groups).

Figure 2.2 shows the various forms of international relationship engaged in by the firms in the sample. As will often be the case throughout this Report, the figure gives each item as a proportion of the sample total and also for each the subgroup separately (small, medium-sized and big firms, defined in terms of employee numbers: under 50; 50 – 249; 250 or more, respectively).

As might be expected, the most common form of international relationship in the sample is exporting, engaged in by 86% of the respondent firms in 2012. Foreign markets were also a source of supply of raw materials, semi-finished goods and/or finished products for 62% of these firms.

14% of the firms in the sample were companies owned or part-owned by foreign multinationals or private equity groups; in most cases, the foreign investor had a controlling interest in the investee. If those foreign-controlled subsidiaries are excluded – as their international activities will be able to count on their parent company's support network – this leaves the Italian-owned firms, 23% of which do business in at least one foreign country through an established presence of their own (company office abroad, joint venture or subsidiary). In detail, 13% of these firms do foreign business through representative offices; 12% have at least one sales and service affiliate or joint venture, while 7% have at least one manufacturing affiliate or joint venture; finally, 2% of them have at least one R&D centre abroad.

Figure 2.2
Forms of international activity of the firms in the sample



Note: percentage figures for direct forms of presence abroad are on the basis of Italian firms only (excluding firms under foreign control).

The figure clearly shows that the percentages of exporting and importing firms are much the same for all company size groups, while in the case of inward and outward foreign direct investment there are considerably more marked differences.

Specifically, a little under half (44%) of firms with 250+ employees are controlled by foreign companies or private equity groups, but the proportion is below 10% in the case of firms with fewer than 50 employees.

So far as outward investment is concerned, almost a third of firms with 250+ employees have a manufacturing affiliate or joint venture abroad, but only 4% of firms with fewer than 50 employees. 7% of the latter group have at least one sales and service affiliate or joint venture abroad, while the proportion is 41% among the bigger firms.

There are also considerable differences according to industrial classification. The highest proportion of firms with establishments or affiliates abroad is found in machinery and vehicle manufacture (30%), followed by electrical, electronic and optical products (29%), the energy & construction sector (26%), rubber, plastic and other non-metal mineral products (26%) and chemical and pharmaceutical production (25%).

Sectors with levels of international activity lower than the sample mean (23%), on the other hand, were the service sector (19%), food and beverages (16%), metal-working and metal products (14%) and the division comprising firms engaged in the paper, wood products & furniture and other manufacturing industries (12%).

The survey also confirms the high degree of international engagement among Lombardy's foreign-controlled companies, already emphasized in last year's Report. No fewer than 80% of all these foreign-controlled firms are exporters, which is not far from the overall average.

Furthermore, nearly a quarter of the foreign-controlled firms have their own established presence in at least one country outside Italy, sometimes through the network of the multinational group to which they belong, but sometimes also through representative offices, points of sale, joint ventures or subsidiaries under their own financial and managerial control.

2.3 Exports as a percentage of turnover

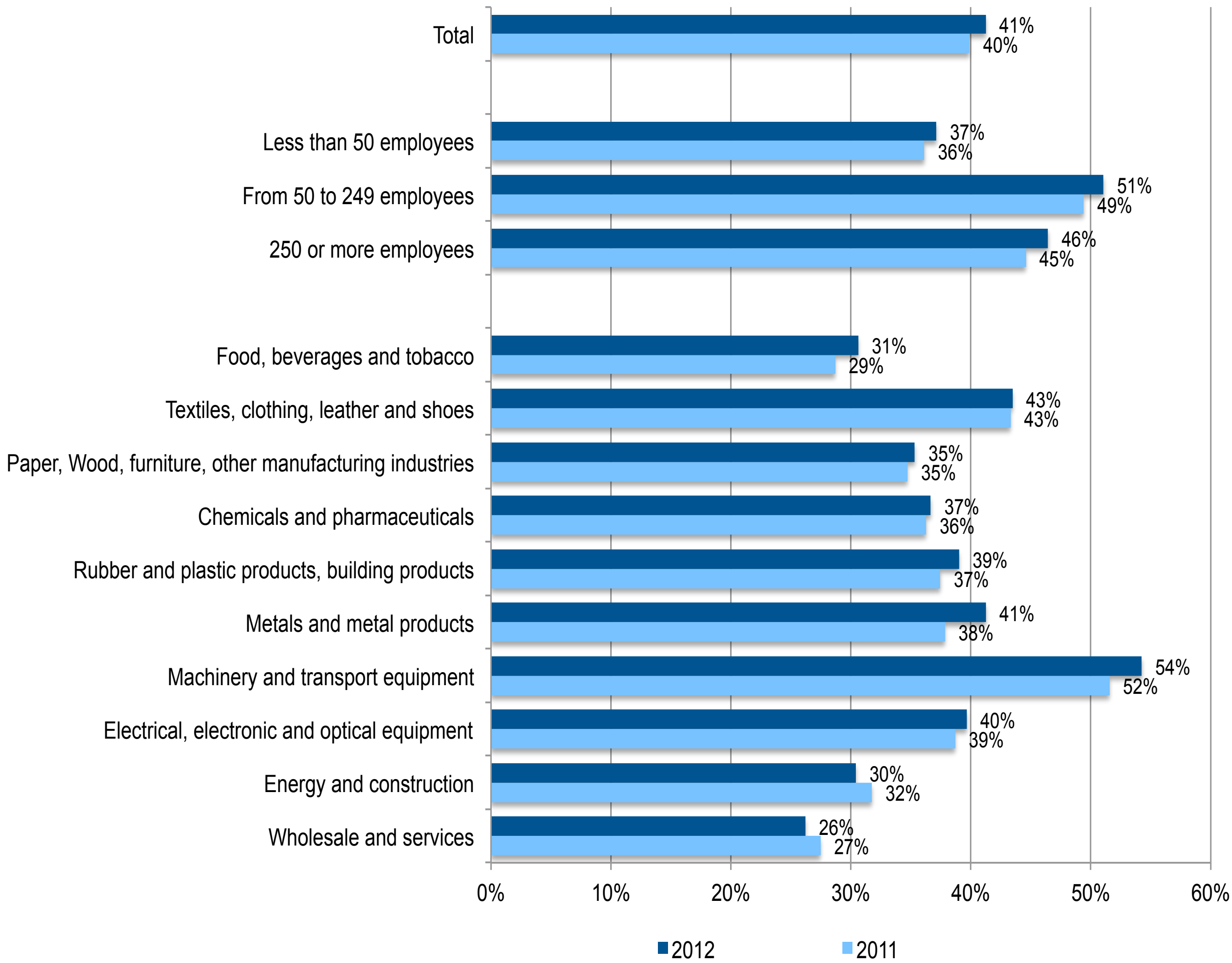
In 2012 exports accounted on average for 41.2% of total sales of those respondent firms with international activities, a rise of more than one percentage point over the figure of 39.9% for 2011 (see Fig. 2.3). Last year's survey had found a similar rise compared with the figure for the previous year.

This rise in the percentage of exports is general, affecting all company size groups and all the manufacturing sectors; only firms in energy & construction, retail and services did not join the trend.

As for company size, medium-sized exporters appeared to be especially dynamic: they exported over half their turnover on average in 2012, their export percentage being nearly two points higher than last year.

The sectors with the highest propensity to export were in manufacturing: in particular, firms engaged in machinery & vehicle manufacturing made 54% of their turnover abroad on average, two percentage points higher than last year. Exports were also above 40% of sales, on average, for fashion firms (43%) and for those in the metal-working and metal products industry (41%); the latter recorded the biggest increase over the previous year, their exports as a proportion of turnover rising by three percentage points.

Figure 2.3
Exporting firms: mean ratio of exports to turnover, 2011 and 2012



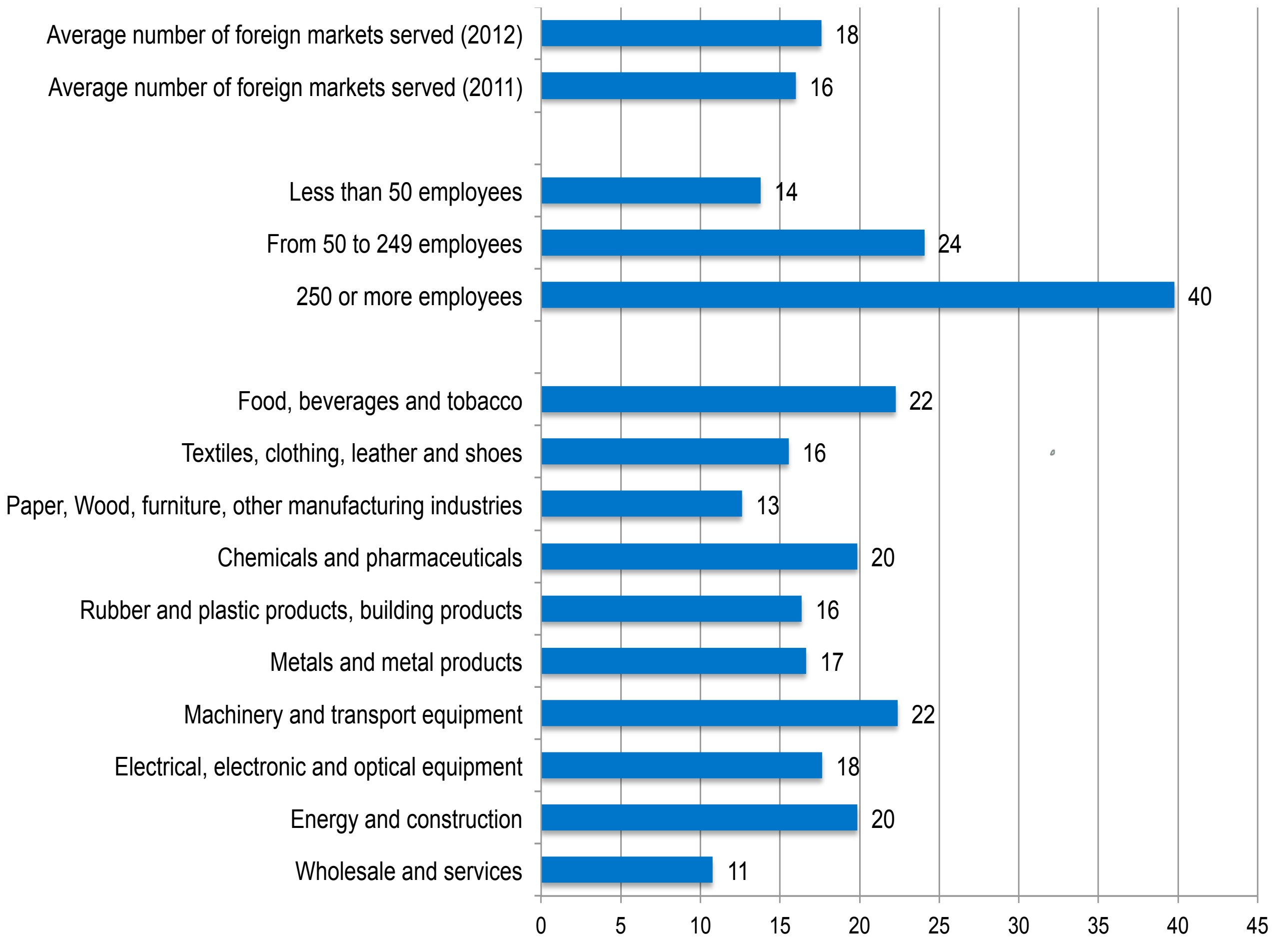
2.4 Diversification of foreign markets

On average, each firm in the sample exported to about 18 different countries (see Fig. 2.4). Compared with last year's figure, the mean number of foreign markets catered for rose by about two.

This is significantly different from the national mean: half of all Italian exporters still concentrate on selling to just one foreign country, and the national average number of foreign markets served is between 5 and 6[1].

[1] *L'Italia nell'Economia Internazionale*, Rapporto ICE 2011-2012, Chap . 8. ICE, Rome , 2012.

Figure 2.4
Average number of export markets, 2012

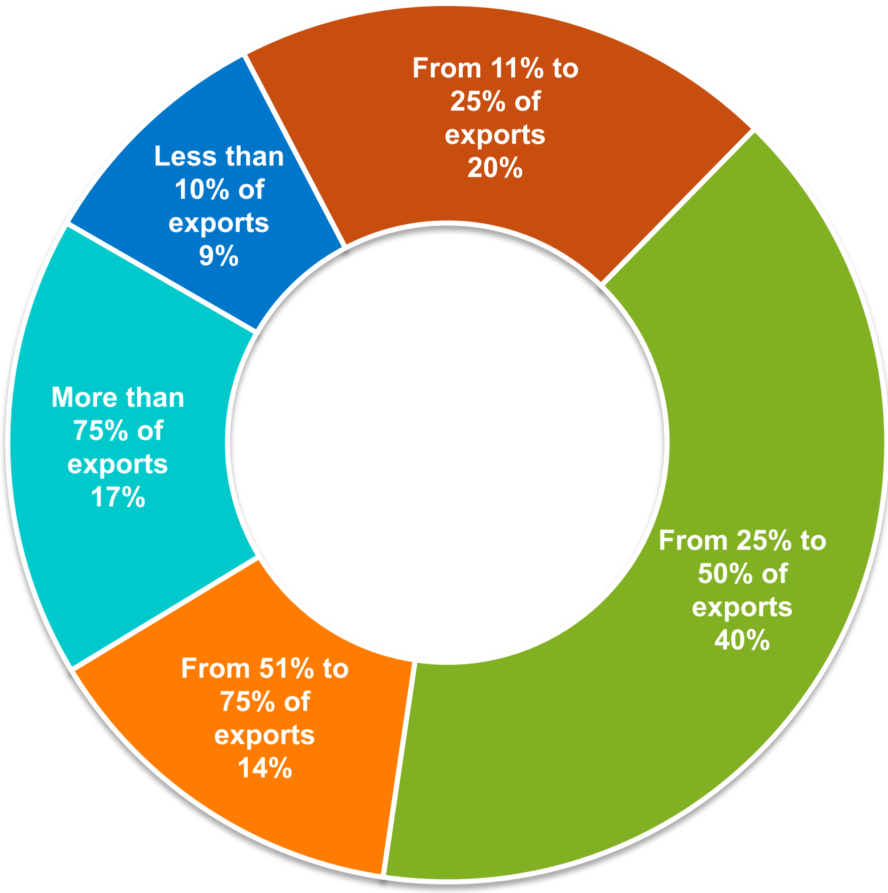


Member firms were also asked to say what proportion of their total exports was accounted for by their biggest single foreign market.

The distribution of the responses gives confirmation of the strong tendency to diversify export markets geographically: only 7% of respondents said that they exported to just one market abroad, while nearly two thirds of exporting firms market their products or services in at least six different foreign countries (see Fig. 2.5).

In greater detail, 43% of the firms said they export to at least eleven different countries (39% last year); 18% to at least 26 different countries and 7% to no fewer than 50 countries.

Figure 2.5
% of exports going to the firm's primary foreign market, 2012



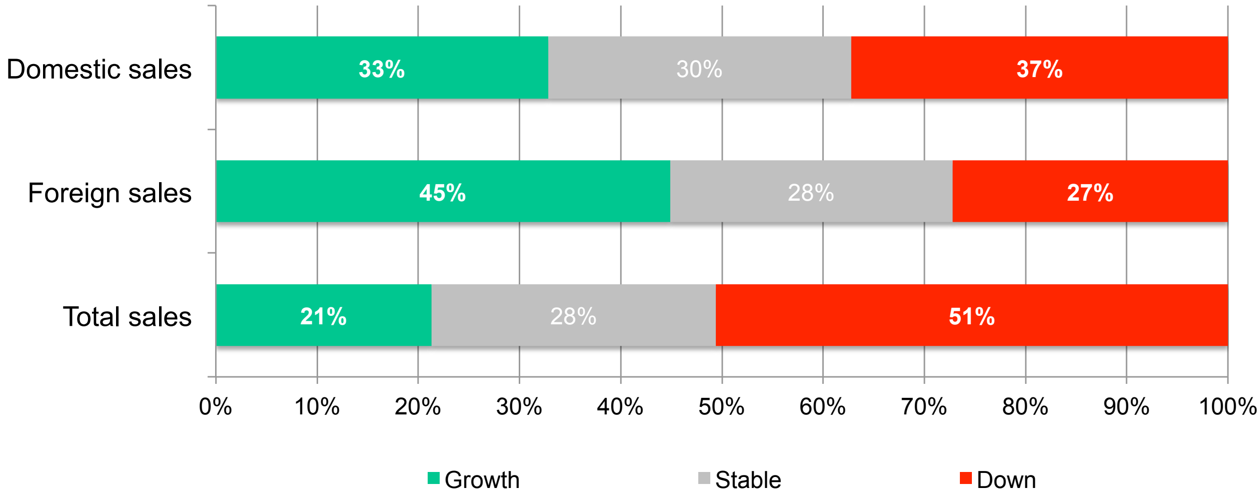
2.5 Exports and economic performance

The extremely difficult conditions in the home market meant that export growth was a real panacea for many firms in 2012. Only a third of firms in the whole sample ended 2012 with a higher turnover than in 2012; the annual Financial Statement closed with figures comparable to last year's for 30% of them, but sadly the trend was downwards for the remaining 37% (Fig. 2.6).

So far as sales in Italy were concerned, the final figures for 2012 were lower than the year before for more than half our respondents; only 21% of the sample recorded an increase, and for 28% home sales were roughly the same.

Foreign markets' performance was very different: here a relative majority (45%) of firms recorded an increase, while "only" 27% of the sample ("only" in view of the circumstances!) failed to do at least as well as last year.

Figure 2.6
Changes in sales, Italian and export markets, 2012 – 2011
(% of firms in the sample)



It should be noted that due to this rise in exports more than a hundred firms in the sample were able to report higher turnover in 2012 despite steady or falling sales in the home market, while another 150 managed, again thanks to export growth, to keep overall turnover steady despite a distinct decline in home sales.

3. Target areas for expansion abroad

3.1 Today's main target markets

Figure 3.1 shows where Lombardy-based companies are putting their main efforts for expansion abroad. Each country is coloured according to the number of firms which either reported having a direct presence there (company office, subsidiary or joint venture) or said it was one of the firm's five biggest export markets: the darker a country's blue, the more respondent firms reported a presence or major exports there; countries not mentioned by any firm are shown in grey.

The greatest density is found in Europe and the United States; next come the four BRIC countries (Russia, China, India and Brazil) and the Mediterranean area, while fewer of the respondent firms report a presence or significant exports in the other geographical areas.

Figure 3.1
Countries named as site of firm's presence or in its top 5 export markets, 2012

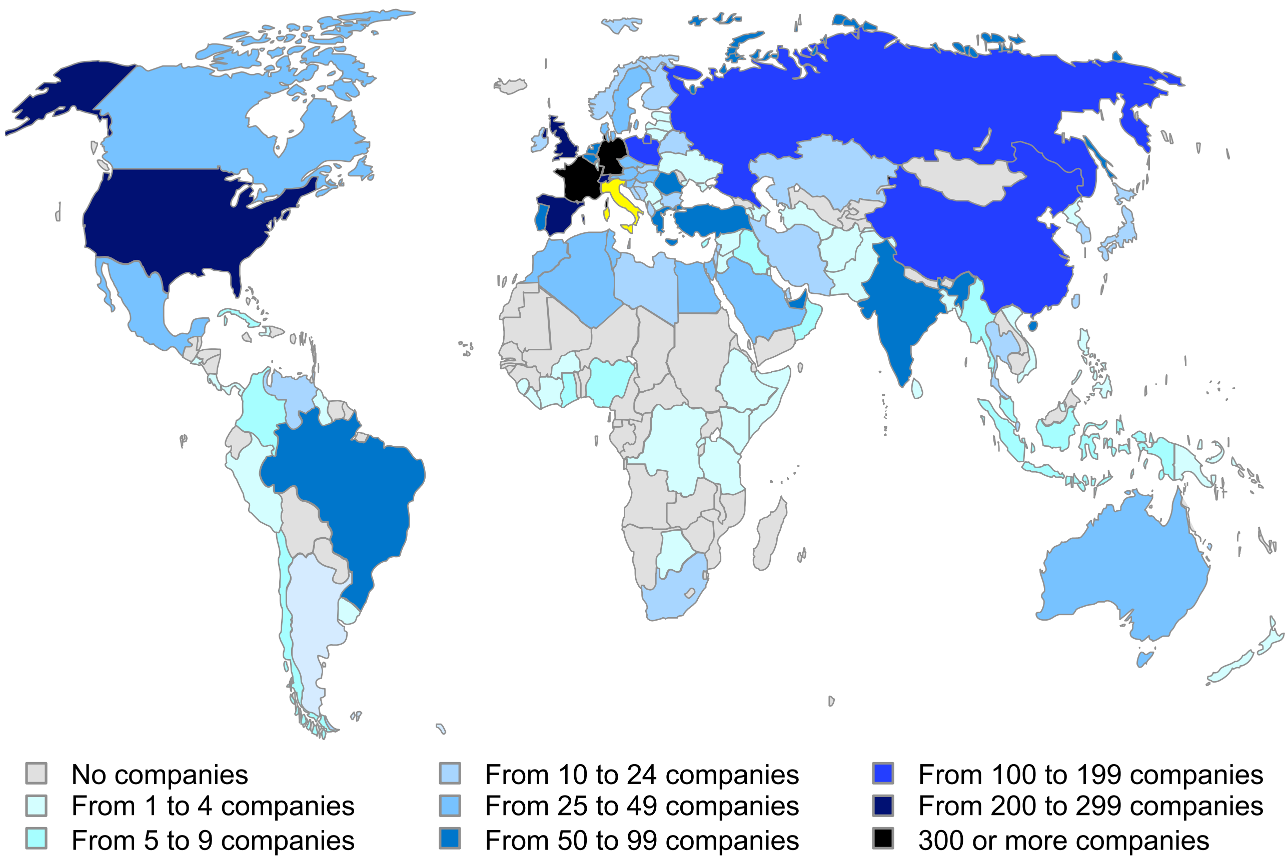


Figure 3.2 shows the percentages of firms active in the various geographical regions[2], broken down by company size. It will be seen, among other things, that the percentage of firms active in each region increases, by and large, with company size, though the Mediterranean area and the Middle East are exceptions: here even SMEs are clearly managing to win themselves a sizeable presence in the market.

Figure 3.2
Regions where Lombard companies are active abroad, by company size, 2012
(countries named as site of firm's presence or in its top 5 export markets)

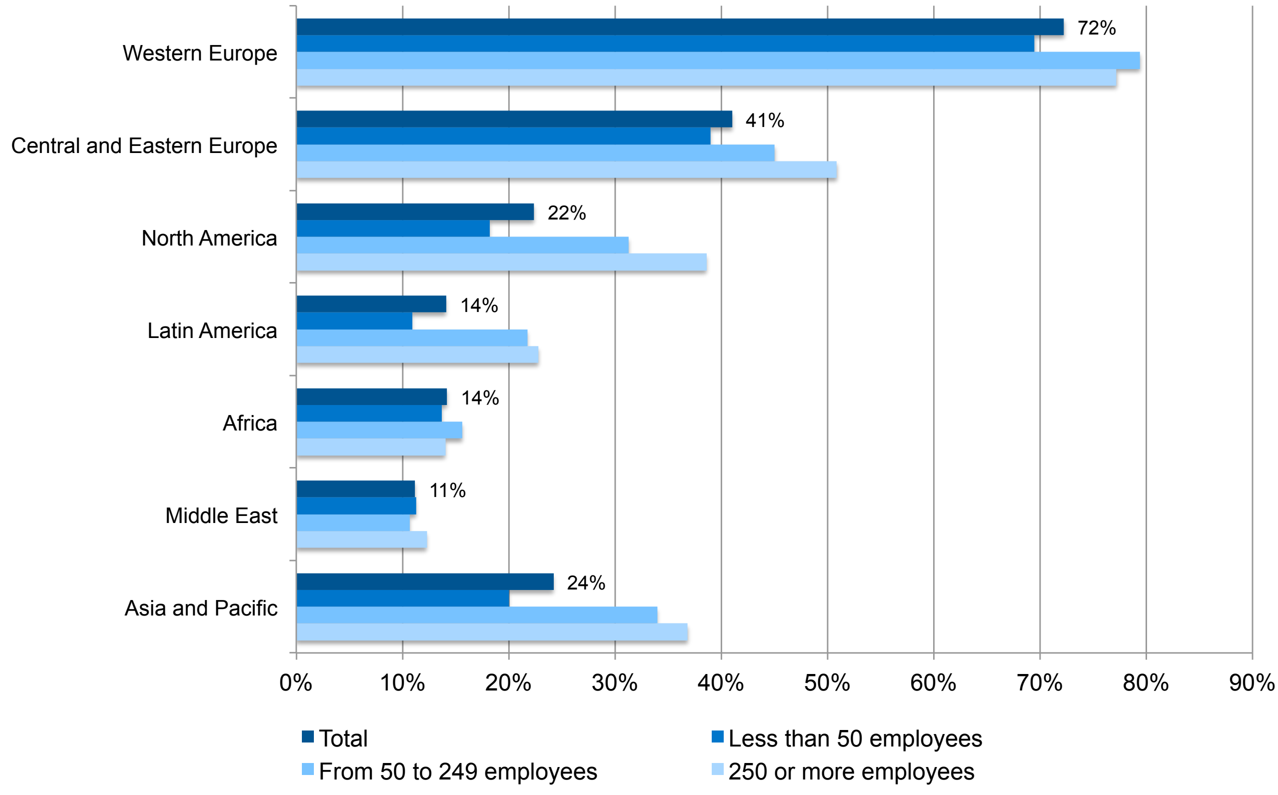


Table 3.1 gives details, for each of the thirty countries most often named, of the number of these firms active in them, and of the various forms taken by their export activity or presence. A colour coding is again used for ease of analysis, with different colours for the various regions.

2 Firms are regarded as "active" in a given region if they have named at least one country in that region as one of their five biggest export markets and/or as one where they have a direct presence.

Table 3.1
30 countries most often named by firms in the sample as among their top 5 export markets or as sites of a direct presence, 2012

Rank	Country	Total companies	Top 5 export markets	Representative offices	Subsidiaries or sales joint ventures	Subsidiaries or manufact. joint ventures
1	France	449	439	33	32	12
2	Germany	430	417	37	25	5
3	Spain	271	258	27	18	5
4	USA	224	203	40	29	14
5	United Kingdom	222	211	17	22	5
6	Switzerland	210	207	13	6	2
7	Russian Federation	154	144	23	5	3
8	China	144	121	28	18	20
9	Poland	118	108	9	8	3
10	Brazil	93	77	19	11	7
11	Austria	90	88	2	3	2
12	Turkey	86	77	16	2	4
13	Netherlands	84	81	2	3	2
14	Belgium	77	75	3	2	1
15	India	64	47	9	11	11
16	Greece	59	55	7	3	2
17	United Arab Emirates	56	52	8	2	1
18	Portugal	55	50	4	5	1
19	Romania	54	49	3	3	3
20	Egypt	48	43	5	2	1
21	Japan	47	43	7	0	1
22	Czech Republic	46	41	2	2	3
23	Sweden	44	41	2	1	0
24	Australia	39	37	1	2	0
25	Tunisia	36	31	1	4	2
26	Slovenia	35	35	1	0	0
27	Saudi Arabia	33	33	3	1	0
28	Canada	32	27	5	1	1
29	Algeria	32	31	2	2	0
30	Hungary	30	27	2	1	2

Legenda:

Western Europe	Central and Eastern Europe	America	Asia and Pacific	Africa and Middle East

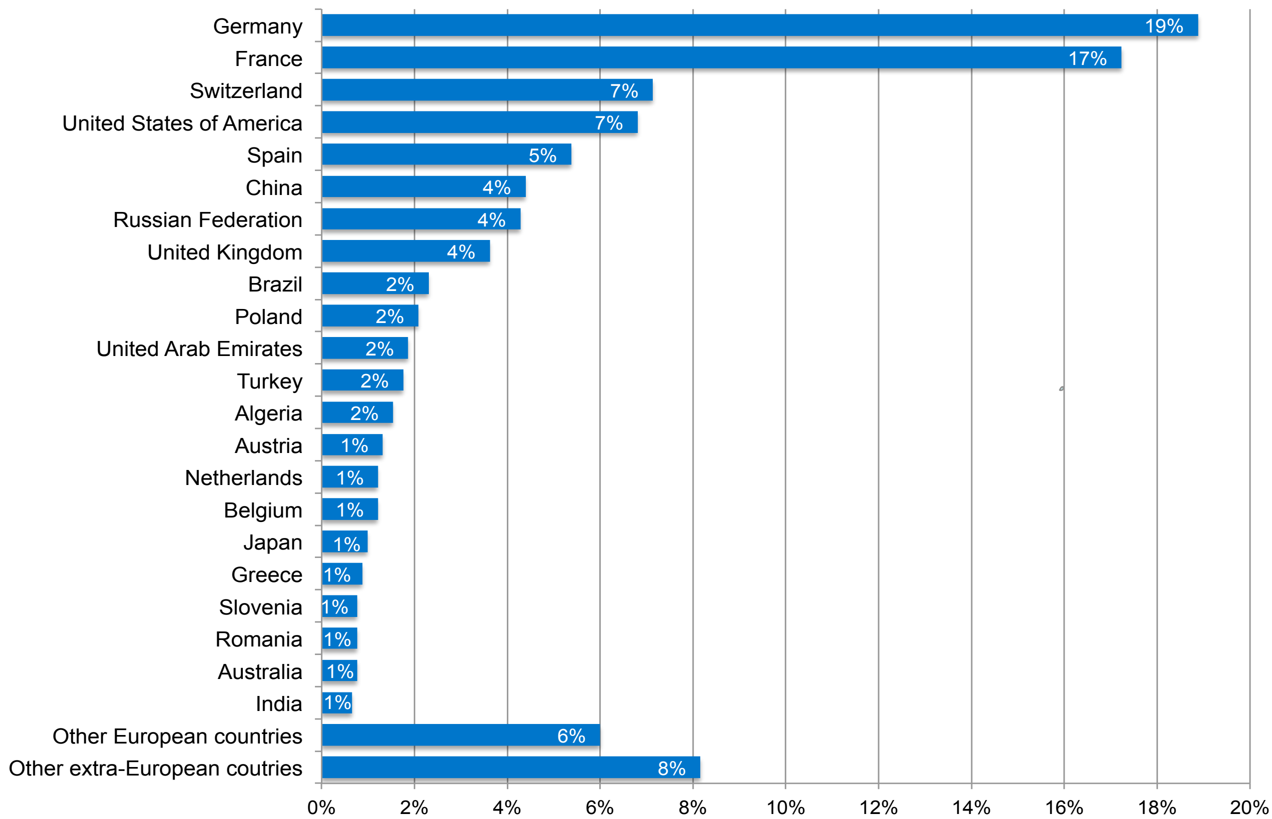
The predominance of green throughout this ranking is immediately obvious (11 Western European countries among the top 23 places), and especially in its upper portion, with no fewer than five countries out of the top six: France, Germany, Spain, the United Kingdom and Switzerland.

There is also a numerous detachment of Central and Eastern European countries: no fewer than seven in this top thirty. Highest-ranking of the non-European countries is the USA in fourth position, followed by the BRICs (Russia seventh, ahead of China in eighth place, Brazil in tenth and India in fifteenth).

France is the country named by most firms (439) as one of their top five export destinations, followed quite closely by Germany (417) and then, at longer intervals, by Spain (258), the UK (211), Switzerland (207) and the USA (203). The USA is however the country with the highest number of representative offices (40) and the second highest number of Lombard companies' sales and service affiliates or/JVs (29: France has 32). China is the country with the most manufacturing affiliates/JVs (20), followed by the USA (14), France (12) and India (11).

Figure 3.3 shows the countries named by exporting firms as their main foreign market. Germany and France, named by 19% and 17% of the firms in the sample respectively, again stand out as the two most important markets, though they have changed places since previous surveys. Next come Switzerland and the USA (named by 7%), Spain (5%), China, the Russian Federation and the United Kingdom (4%).

Figure 3.3
Firms' biggest foreign export markets, 2012
(% of exporting firms)



29% of the firms in the sample named a non-European country as their main export market, which shows the importance of emerging markets to many Lombardy-based companies even today; but that importance is going to grow considerably over the medium term, as we shall see.

3.2 Target areas for expansion over the next three years

The firms in the sample were also asked in which countries they intended to expand their presence over the next three years (2013-2015); they were invited to name up to five countries, and include all possible options (exports, representative offices, trading subsidiaries or joint ventures, manufacturing subsidiaries or joint ventures, R&D centres).

Figure 3.4 summarizes the answers on geographical expansion of exports, and Table 3.2 gives details of the various options for development indicated by respondents in the case of the top thirty Countries.

Figure 3.4
Target countries for Lombardy-based companies' export growth in the next three years (2013-2015)

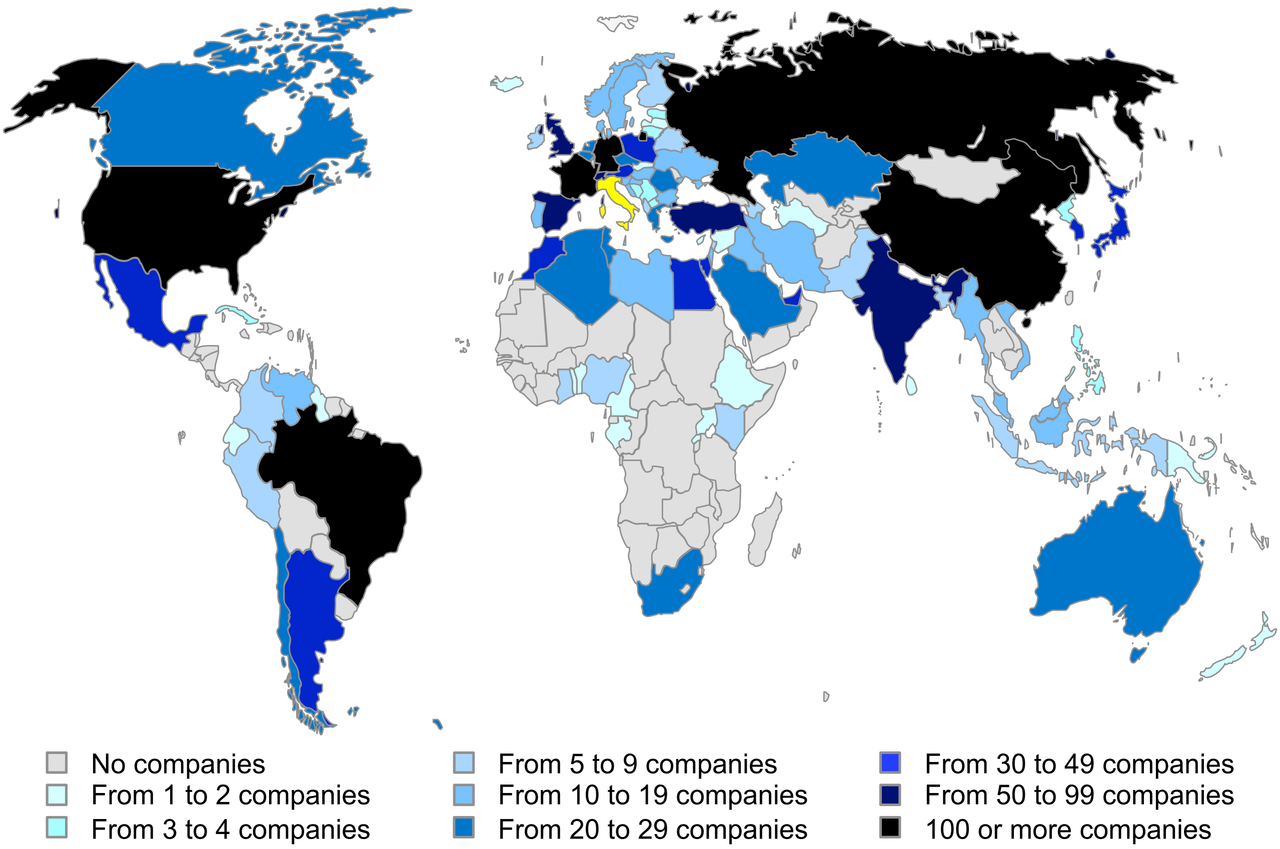


Table 3.2
Top 30 target countries for firms' export growth or direct presence in the next three years (2013-2015)

Rank	Country	Total companies	Top 5 export markets	Representative offices	Subsidiaries or sales joint ventures	Subsidiaries or manufact. joint ventures
1	Russian Federation	177	170	10	11	0
2	Brazil	163	148	23	16	20
3	USA	157	146	23	18	9
4	Germany	156	148	16	9	3
5	China	147	129	18	18	14
6	France	120	112	8	9	3
7	India	98	81	8	10	11
8	United Kingdom	64	62	6	0	1
9	Turkey	60	53	5	6	4
10	Spain	58	54	4	5	2
11	Switzerland	54	53	2	2	0
12	United Arab Emirates	50	46	3	4	0
13	Poland	42	40	3	1	1
14	South Korea	29	27	3	2	1
15	Egypt	26	25	1	1	0
16	Japan	25	23	2	1	1
17	Mexico	24	23	2	0	2
18	Austria	23	23	0	0	0
19	Morocco	23	21	3	2	2
20	Romania	21	18	2	2	0
21	Saudi Arabia	20	19	2	2	0
22	Argentina	20	20	0	0	0
23	Netherlands	19	18	0	1	0
24	Belgium	18	18	0	0	0
25	Australia	17	17	1	0	0
26	Algeria	16	15	1	2	2
27	Libya	16	12	2	3	1
28	Sud Africa	16	14	1	1	0
29	Tunisia	15	14	0	0	1
30	Canada	15	14	1	2	0

Legenda:

Western Europe	Central and Eastern Europe	America	Asia and Pacific	Africa and Middle East

As in Table 3.1 above, the various lines have been colour-coded to indicate regions. A simple visual comparison between Figures 3.1 and 3.4, or Tables 3.1 and 3.2, shows the rapid changes now taking place so far as target areas for Lombardy-based companies' expansion abroad is concerned.

Though much attention is still paid to the major developed countries of Europe and America which are the main export markets for their products and services at present (France, Germany, Spain, UK and USA), it is immediately clear that the focus of Italian companies' international expansion is shifting towards the emerging countries in general and the BRICs in particular: all are shown darker in Figure 3.4 than in Figure 3.1, as also is Turkey.

The figures in Table 3.2 tell the story just as clearly. The four BRICs have moved up the ranking of preferred destinations and are now firmly established in the lead rather than the second echelon. Russia is unmistakeably the country named most often (177 firms say they intend to grow their business there in the next three years), followed by Brazil (163); China comes fifth (147) and India seventh (98). It should also be noted that Brazil is the country named by the highest number of firms as a potential destination for manufacturing investment (20 firms, against 14 for China and 11 for India), while China and the USA are the countries most often named as possible sites for a trading subsidiary or JV (18 firms each; 16 firms named Brazil, 11 the Russian Federation and 10 India).

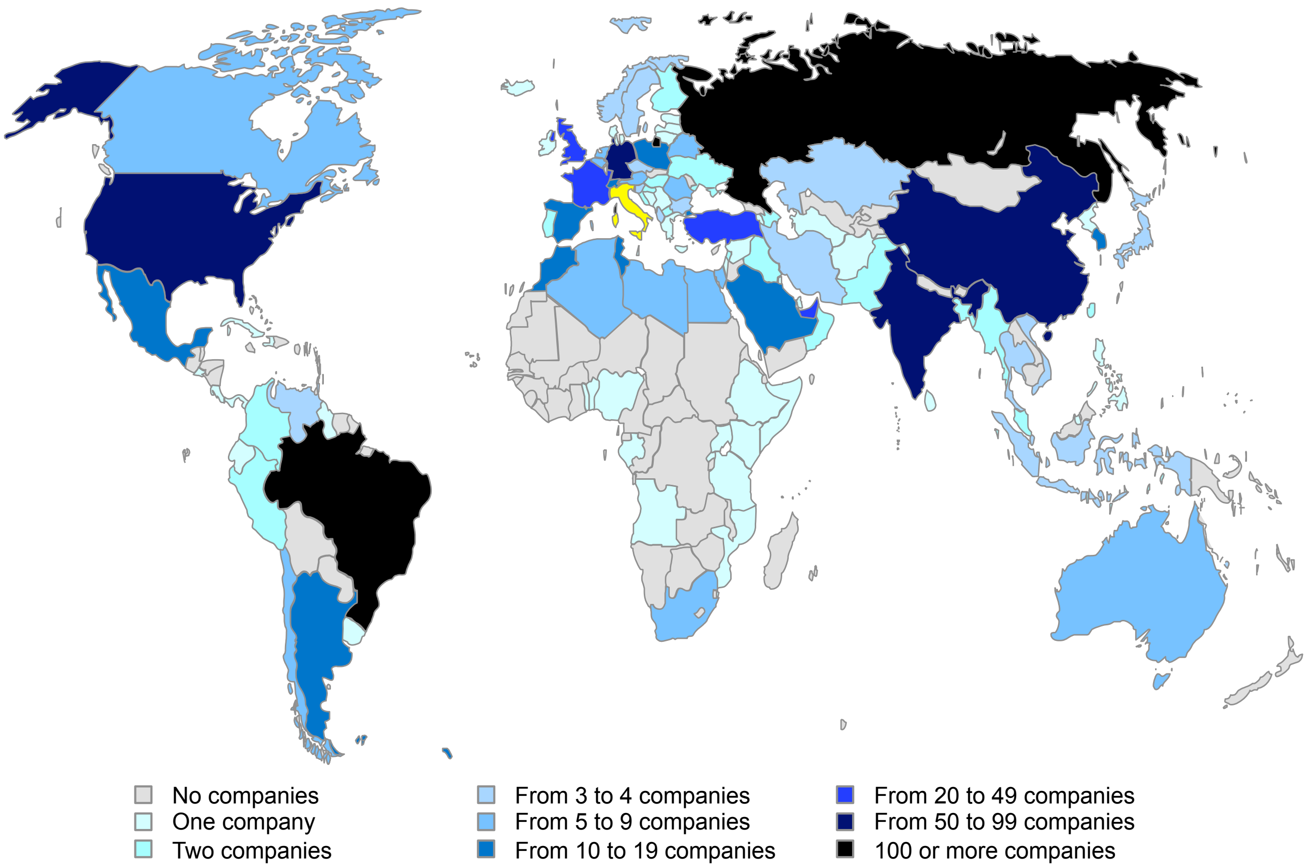
It is clear from a glance at the next few places that Lombardy-based companies are also paying more attention to markets in Latin America (Chile, Mexico and Argentina as well as Brazil) and to the Arab countries (UAE, Saudi Arabia and North Africa). Among the developed countries, too, the traditional European trading partners are increasingly being overtaken, so far as the interest shown by Lombardy-based companies is concerned, by non-European countries such as Australia, South Korea, South Africa, Canada and even Japan, where companies from Lombardy – and from Italy generally – have only a modest presence so far and there are truly worthwhile growth opportunities to be seized by deploying adequate strategies and investing serious amounts.

The first Western European country does not appear in Table 3.2 above fourth place (Germany), while the current leader (France) falls to sixth, the United Kingdom to eighth and Spain to tenth (it will be recalled that in today's ranking (see Table 3.1) the European countries take no fewer than five of the top six places. In general all the European countries, west or east, have slipped down the ranking: only twelve remain in the top thirty destinations, against today's eighteen. The only European country (European at least in economic terms) which appears to buck the trend is Turkey, which has risen to ninth place and is named by no fewer than 60 firms as a country where they intend to develop their business over the next three years.

Some regions, though they offer interesting development prospects, are relatively neglected in the medium-term international growth strategies of the firms in our sample. We refer in particular to the whole of south-east Asia apart from India and China, to Africa south of the Sahara – now growing at a considerable pace, and a market which could be quite worthwhile, especially for manufacturers of machine tools – and to the Balkans region, which as well as being a useful manufacturing base for serving Russia and all of south-east Europe could also be a market whose own growth potential should not be neglected, especially as it is right next door to Italy.

The shift of focus in Lombardy-based companies' international growth plans beyond Europe is clear from Figure 3.5, which only considers a firm's intention to develop business in a particular country in the next three years if that country is not at present one of the firm's five main export markets and the firm does not yet have an established presence there. In other words, Figure 3.5 shows those countries where individual firms in our sample for which they are "new" markets intend to start doing business there in the next three years.

Figure 3.5
New markets where Lombardy-based companies intend to do business in the next three years (2013-2015)



Europe generally shows "lighter" in colour than in Figures 3.1 and 3.4, and it is not hard to see the great interest in the BRICs, the Mediterranean area, the Arabian peninsula and Latin America.

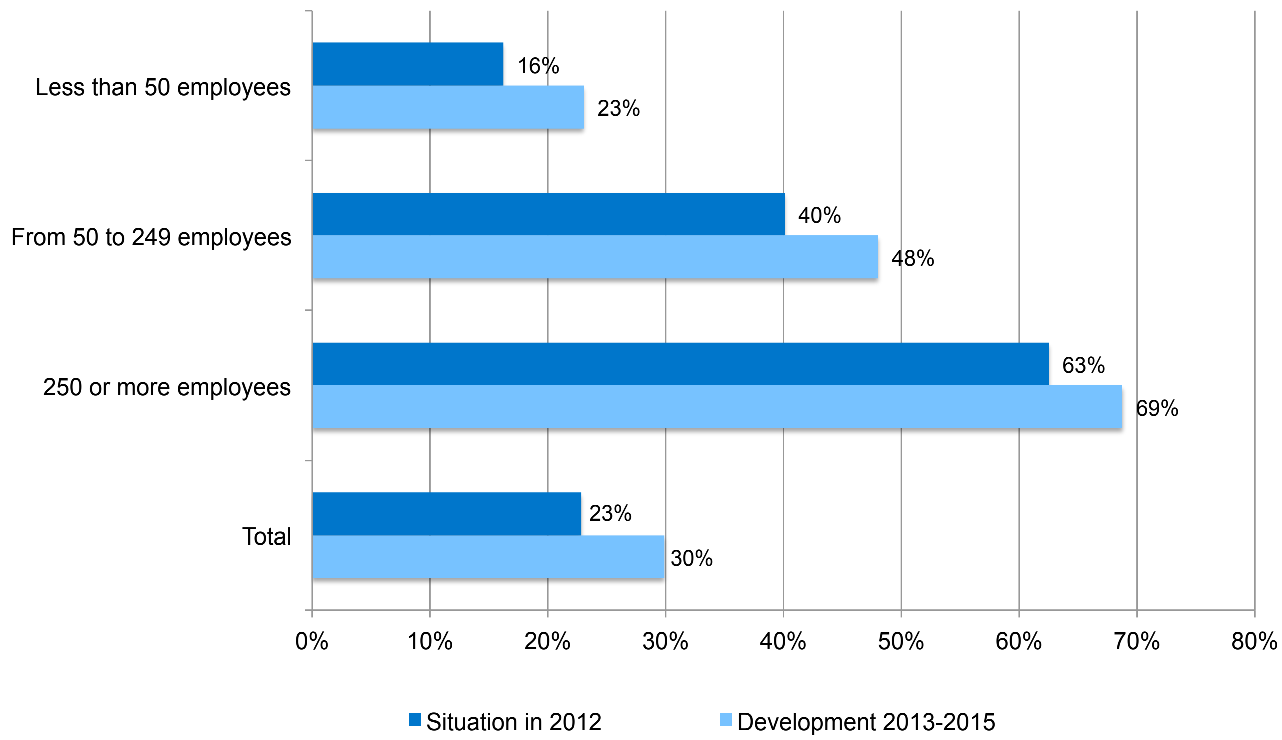
3.3 Possible effects of developments in the next three years

Figures 3.6, 3.7 and 3.8 give us a measure of the possible effects of the present international growth strategies of the firms in the sample. They portray a scenario dependent on the fairly "heroic" assumption that all the projects indicated by these companies are actually implemented and fulfilled: i.e. that the countries where each of these firms intends to develop exports will join its main export markets, and that all potential projects to set up established presences abroad (representative offices, subsidiaries and joint ventures) come to fruition.

That scenario is hardly likely, nor would it be wise to set too much store by the picture painted by simply adding all the corresponding figures. Some interesting clues (unquantified) may nonetheless be extracted, and will help in the understanding of current trends.

In particular, if all the firms which have mentioned the possibility of establishing a direct presence in one or more foreign markets were actually to carry out such plans, then the proportion of firms with establishments or subsidiaries abroad would rise by seven percentage points from 23% to 30%, though the breakdown by company size would not change appreciably (see Fig. 3.6).

Figure 3.6
Possible effects of international growth plans for 2013-2015 on the percentage of Lombard companies with establishments or affiliates abroad, by company size



One of the consequences would be quite a significant increase in the extent of international activity engaged in by firms with fewer than 50 employees: the proportion of SMEs with foreign establishments would rise from 16% to 23% – almost half as many again. In the case of firms with 250+ employees, on the other hand, that proportion would only rise by a tenth.

Of the various sectors, it is services which stand out: here the percentage of firms with foreign establishments could actually double (from 19% to 38%, see Fig. 3.7), putting this sector among those with the highest degree of international activity, just behind engineering and vehicle manufacture (where the percentage of firms with foreign establishments could rise from 30% to 40%). Within services, it appears to be logistics, consultancy and technical services firms which are particularly oriented towards growth abroad, and “Made in Italy” firms, along with manufacturers of electrical, electronic and optical products, which are least dynamic from this point of view: here the percentage of firms with foreign establishments might grow from 23% to 24% and from 28% to 30% respectively.

Figure 3.7
Possible effects of international growth plans for 2013-2015 on the percentage of Lombard companies with establishments or affiliates abroad, by sector

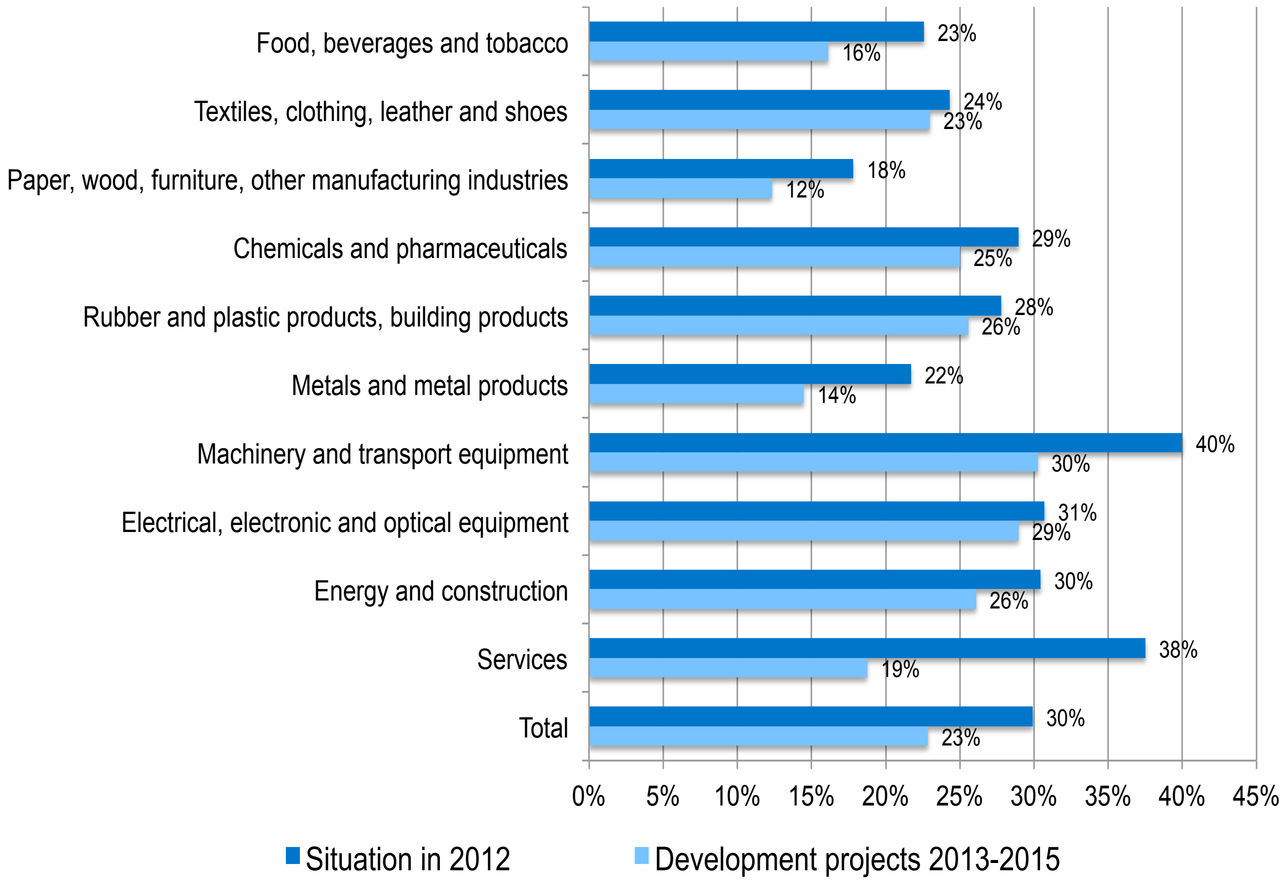
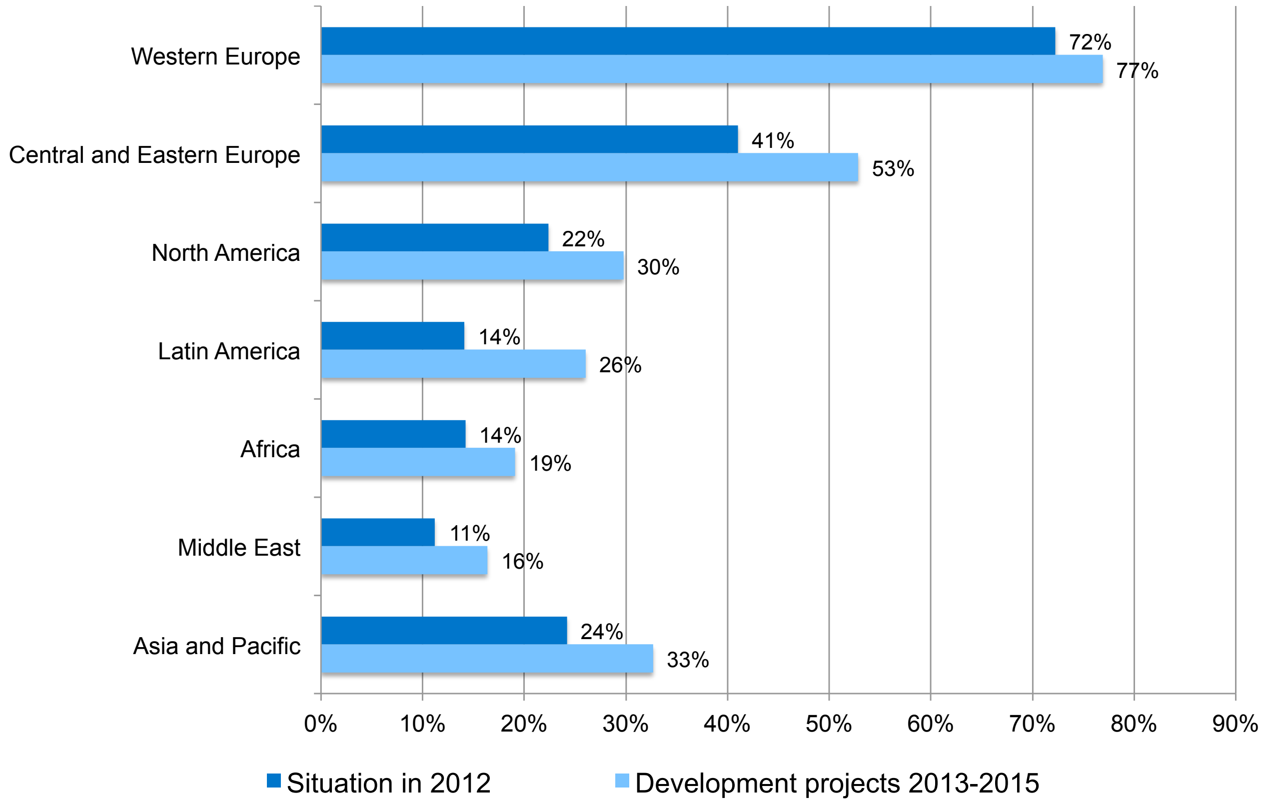


Figure 3.8
Possible effects of international growth plans for 2013-2015 on Lombard companies' activity, by economic region



Lastly, Figure 3.8 shows the possible effects of these firms' international growth plans on their business activity in the various economic regions. The most significant development would be in Central/Eastern Europe and in Latin America, mainly due to the strong interest in Russia, Turkey and Brazil currently shown by the firms in the sample.

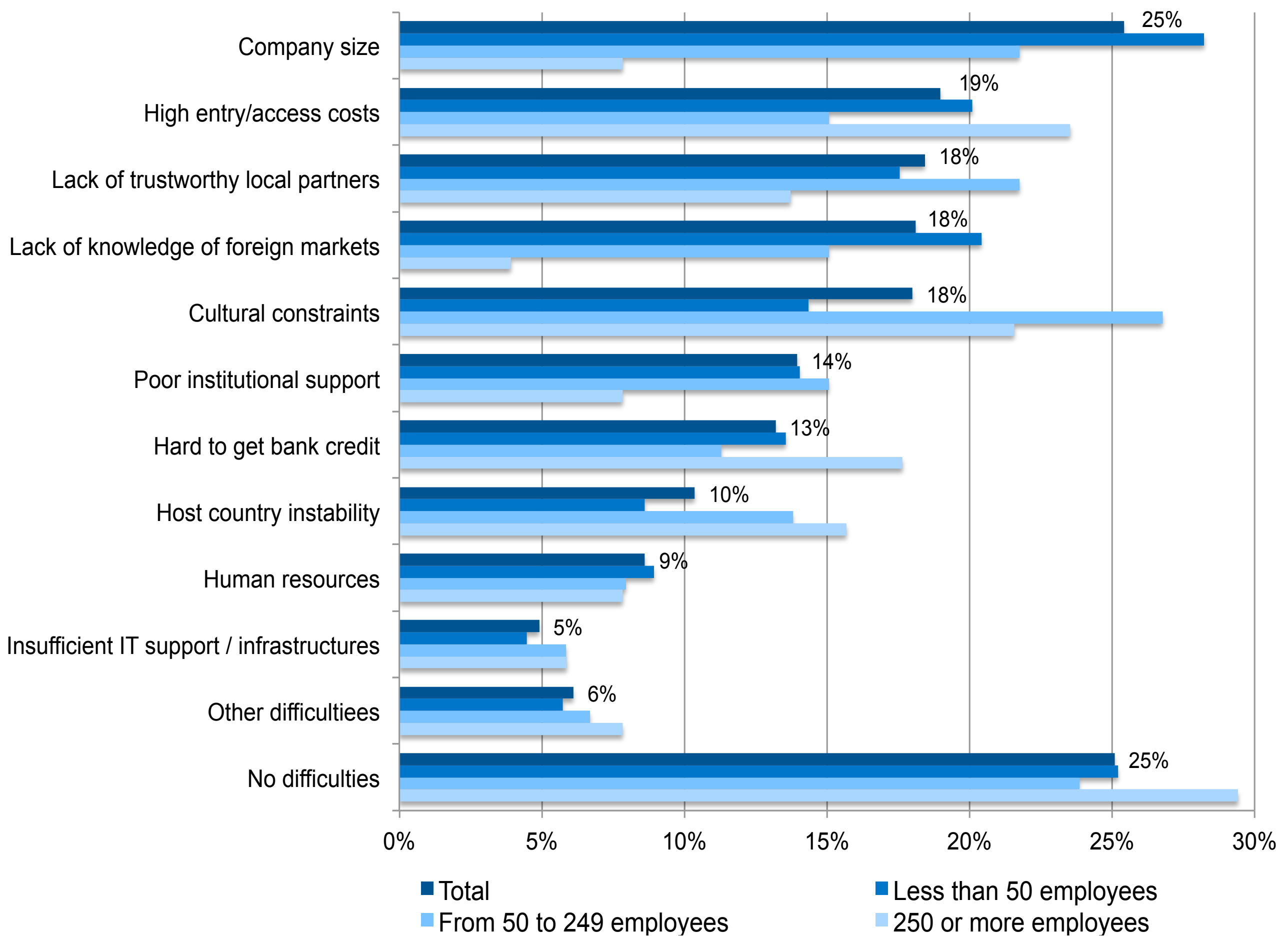
One final consideration, already emphasized in previous Reports, deserves repetition in our view. The analysis of the countries where the firms in the sample have a presence today and intend to invest in the next few years tells us that the main thrust of Lombardy-based companies' efforts to invest directly abroad is still in the direction of penetrating markets and getting closer to their main customers: initiatives undertaken in order to cut production costs through offshoring to low-wage countries are far more sporadic, and mainly concentrated in the Balkans and the countries of the southern Mediterranean shore; however, even in these areas, access to national or regional markets with attractive growth prospects is often one key objective of the investment, for these firms understand that the benefits of merely offshoring production work to countries with low labour costs can prove short-lived unless they pursue other – considerably more important –

4. Difficulties encountered and the demand for services

4.1 Difficoltà encountere in expanding abroad

About three quarters of Lombardy-based companies which engaged in any way in foreign business dealings reported some kind of difficulty in the process of developing abroad (see Fig. 4.1).

Figure 4.1
Main difficulties encountered in expanding abroad

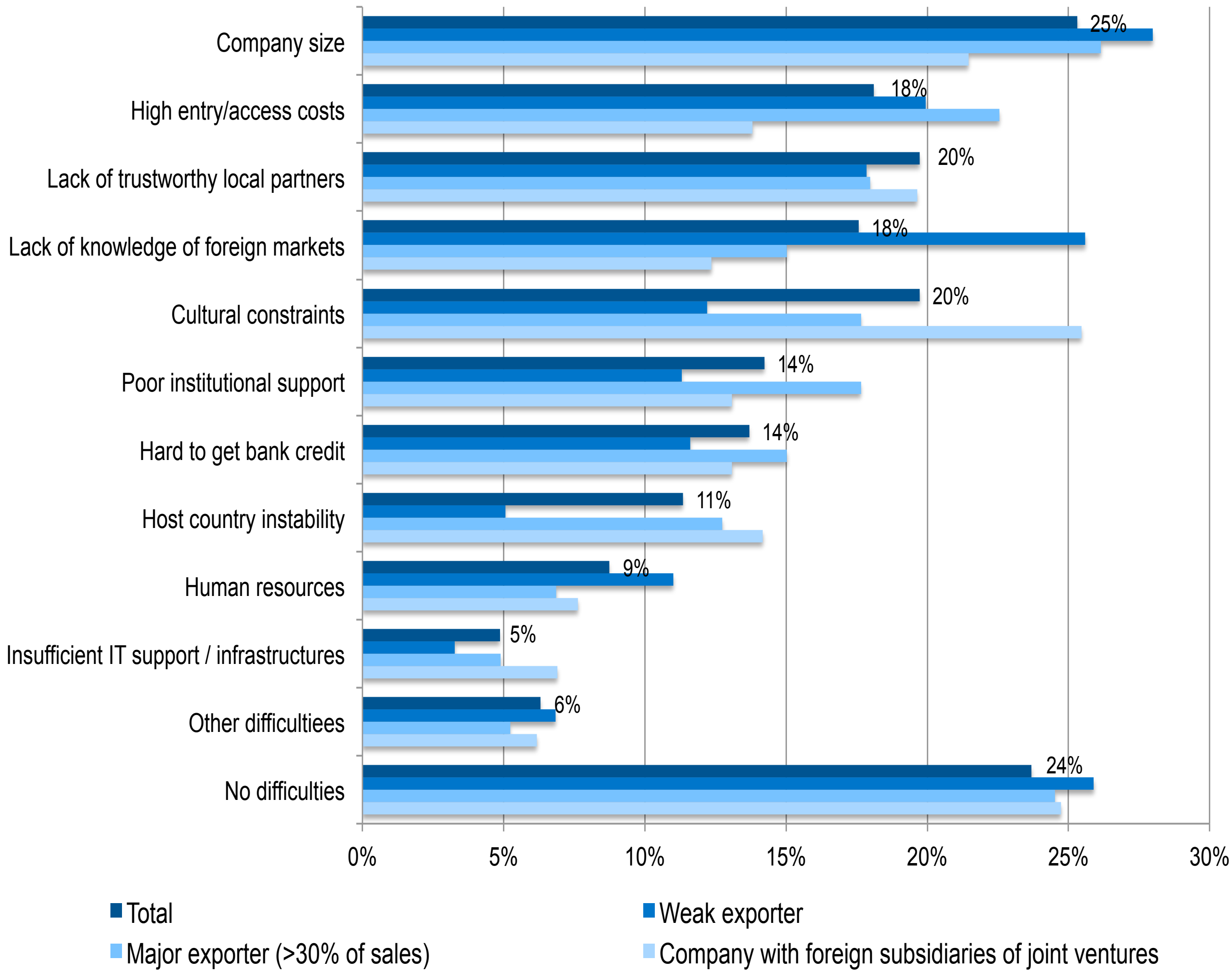


The biggest obstacles, reported by 25% of the respondent firms (or one third of firms reporting some kind of difficulty) are those which can be summarized as stemming from small company size: limitations on managerial and/or financial resources to invest in the work of expanding abroad, high fixed costs, lack of a culture of doing business abroad, &c.; it should be emphasized that these difficulties are not encountered by the smallest firms only, but often also by medium-sized firms (50-249 employees), which in many cases lack the resources needed to deal adequately with the efforts required by expansion abroad, where they often face competition from bigger companies – sometimes much bigger.

19% of respondent firms focus more precisely on the high costs which have to be undertaken to start and sustain the process of extending their business internationally.

A fairly similar proportion (18% of the total) are aware of how often cultural differences hinder their growth abroad. This is a factor whose importance grows significantly as the scale of the firm's international activities increases (see Fig. 4.2) and as its international expansion diversifies into new geographical areas. In particular, this factor becomes increasingly important the more the firm addresses countries further from Europe either geographically or culturally.

Figure 4.2
Biggest difficulties encountered in expanding abroad, as a function of the firm's degree of international activity



Another two factors, somewhat linked both to cultural factors and insufficient company size, were cited (by some 18% of respondents in either case) as significant obstacles to Lombardy-based firms' expansion abroad: lack of knowledge about foreign markets (such knowledge calls for adequate investments of money and, even more importantly, managers' valuable time; smaller firms simply cannot allocate enough of these), and the inability to find a trustworthy local partner (itself linked both to the cultural differences between Italy and the target countries, and to the scale of the resources firms can put into minimizing those differences through the use of special means of legal protection).

In the face of these difficulties (which, as we have said, grow with the geographical and cultural remoteness of the target markets), 14% of respondent firms complained that they did not get enough support from the official organizations and institutions whose job it is to provide such support to firms expanding abroad.

That job includes precisely those tasks of filling in the knowledge gaps which hamper small firms, and helping them cope with the other constraints they encounter when seeking international growth. It appears that the firms classified as "major exporters" suffer most from this: those firms which are not themselves multinational and have no establishments abroad, but still make over 30% of their sales in foreign markets.

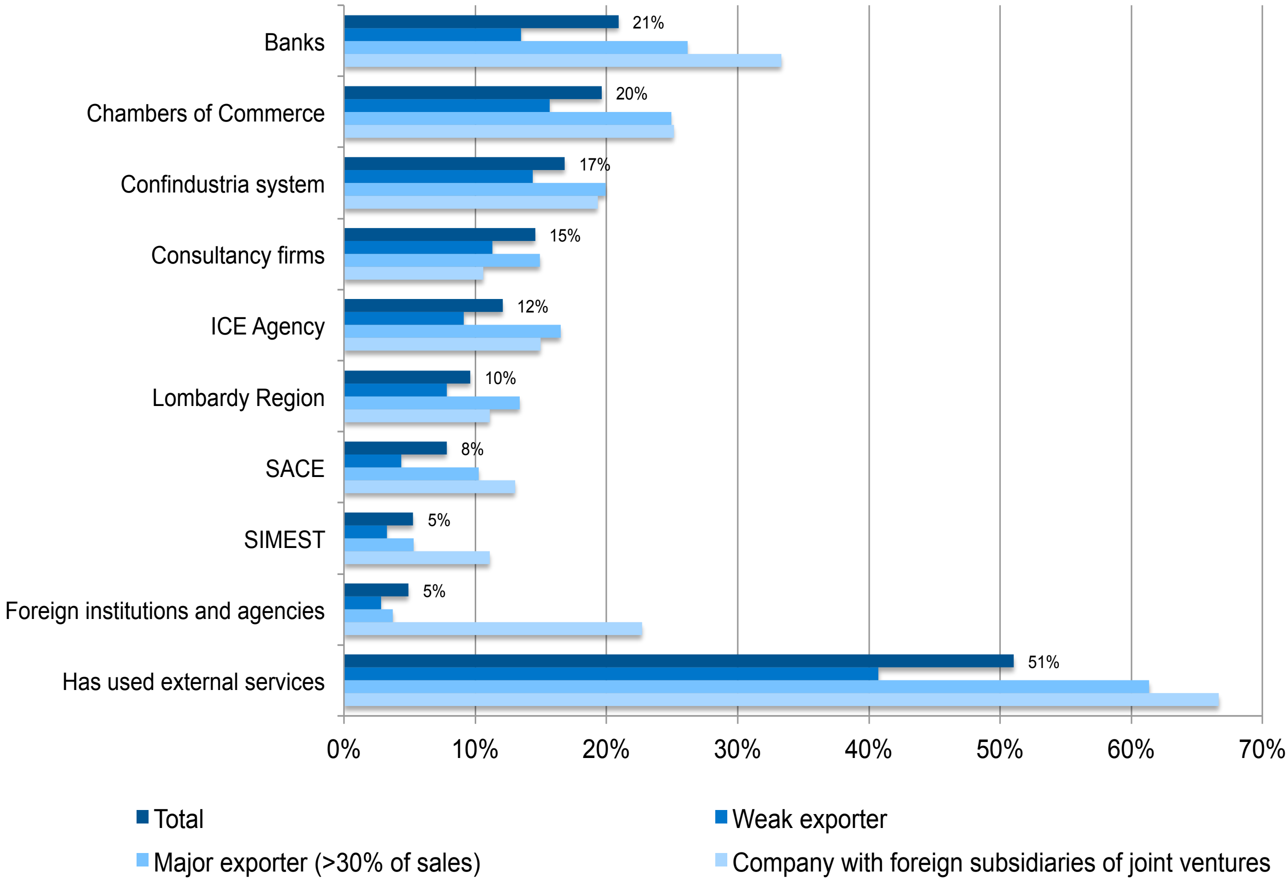
This is an observation which, though not so big as to be worrying, should nevertheless be duly borne in mind, not least because reports of this problem appear to be more frequent (in last year's the survey only 12% of the respondent firms complained of this); as in the past, this theme was investigated in greater depth: see the next paragraph.

4.2 Services supporting expansion abroad

Over half of the firms replying said they had used international business support services (see Fig. 4.3). That figure is ten percentage points higher than last year's; and although due weight should be given to the difficulties of direct comparison between the surveys, the difference does very probably show a growing tendency by companies to make use of outside services to support their choices on international expansion. The change is no doubt due to the greater range and geographical diversification of companies' business activities.

The responses make it clear that none of the various official organizations offering international business support services can be described as the favourite among Lombardy's companies (if only because the various services they offer to business show a significant degree of complementarity). On the contrary, firms tend to seek help from more than one source at a time (60% of those using outside services do so), in order to maximize the benefit by exploiting the specific skills of each.

Figure 4.3
Recourse to official bodies supporting international business expansion, by firm's degree of international activity



21% of respondent firms had used services provided by the banking system in connection with their international expansion; slightly fewer (20%) had had recourse to their Chamber of Commerce, or to the regional association of such chambers, Unioncamere Lombardia, or Promos, etc.

Firms had also turned to their trade associations (17%), consultancies (15%), the Italian Trade Commission (ICE) (12%), or the Lombardy Regional Government (10%). Other organizations called on less frequently were the Italian export credit agency SACE (8%) and SIMEST (5%): this was partly due to the specialized nature of the support these two agencies offer. Lastly, 5% of firms used services provided by foreign institutions or agencies.

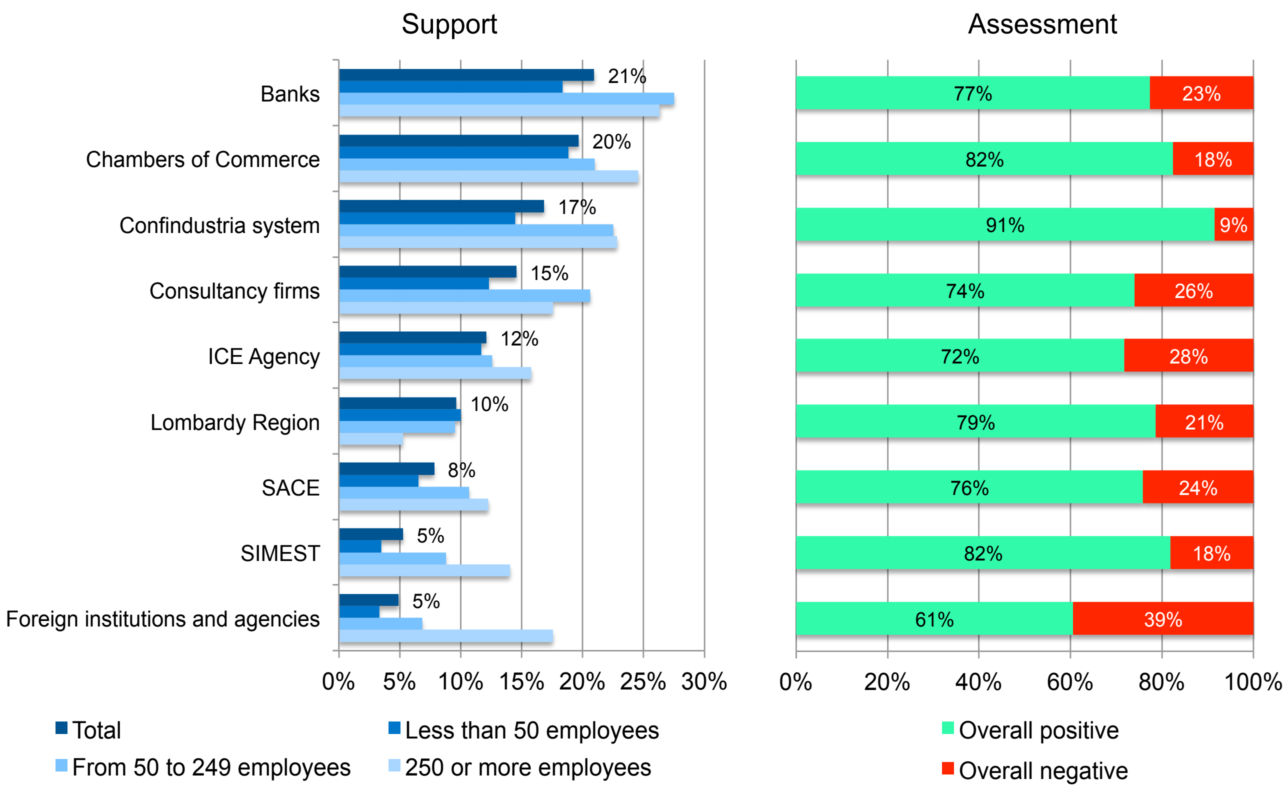
Some interesting differences were found concerning the demand for support services as a function of the kind of business which the firm carried on abroad.

The requirements of those firms which had a foreign presence in the form of a subsidiary or joint venture were more expensive and more complicated than those of firms which merely export goods. In particular, a fast-growing proportion of firms with their own foreign presence were having recourse to the services provided by banks, by SIMEST and SACE and/or by foreign institutions and agencies (international agencies or, more often, host government agencies), because of the specific nature of the services offered by such bodies.

Concerning the role of Confindustria's trade associations, it is worth pointing out that in some markets they are far and away the favourite body for firms to approach on matters to do with international expansion, partly because of the agreements they have made with the other organizations working in the area. This enables firms to turn to an association they feel to be particularly local for access not only to its own services but also to those provided by others.

Respondents were also asked to give their opinion of the assistance they received from the various Italian organizations working in one way or another to support companies' international expansion. Overall, this drew a largely positive response from those using the services (see Fig. 4.4).

Figure 4.4
Assessments of official organizations providing support to international activities



By far the most complimentary opinions were those about the Confindustria system (approved by over 90%). SIMEST and the Chambers of Commerce organization also received good reports, on balance, from more than 80% of respondents.

Somewhat less flattering opinions were given of other Italian organizations working in this area – the Regional government, banks, SACE, the ICE agency and consultancy companies – which got an overall negative assessment from more than 20% of respondents, and almost as many as 30% in the case of ICE.

The lowest level of satisfaction – barely over 60% – was with foreign (international or local) institutions, governments and government agencies: smaller firms probably find such organizations difficult to approach and deal with.

It should however be emphasized that in general the assessments given by the bigger firms (50 or more employees) always tend to be more positive than those of the smaller ones; this was particularly evident in the assessments of SACE and SIMEST, whose services are in any case designed for companies which have considerable managerial resources (recourse to SIMEST, for instance, requires the preparation of a business plan).

4.3 Services provided by the Confindustria system

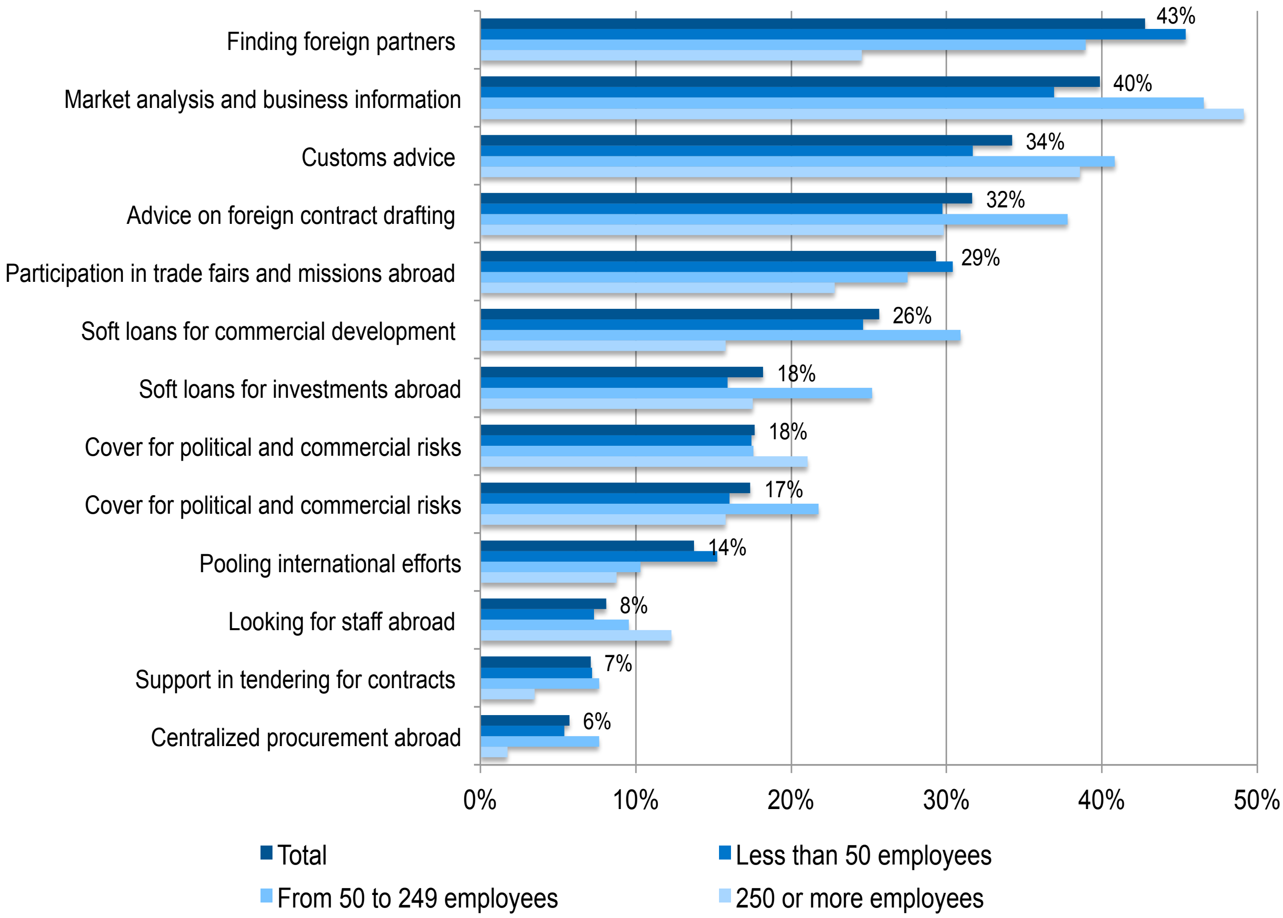
As pointed out above, the Confindustria system is, in many parts of Lombardy and especially those furthest from the regional capital, the favourite source of help for most firms on matters to do with expansion abroad.

This is partly because of its bilateral agreements with the other bodies working in the area, which mean that firms can turn to an association which they regard as particularly "local" for access not only to its own services but also, through it, to those of other organizations.

Above all, the respondent companies mention the need for support in finding foreign partners; and this need is further confirmed in the views expressed by member firms about the services provided by the Confindustria system: that form of support is considered important by 43% of respondents (see Fig. 4.5).[3]

[3] Companies were asked to say which five services, of all those provided by the Confindustria system to support international expansion, they considered most important.

Figure 4.5
Importance assigned to Confindustria services in support of international expansion



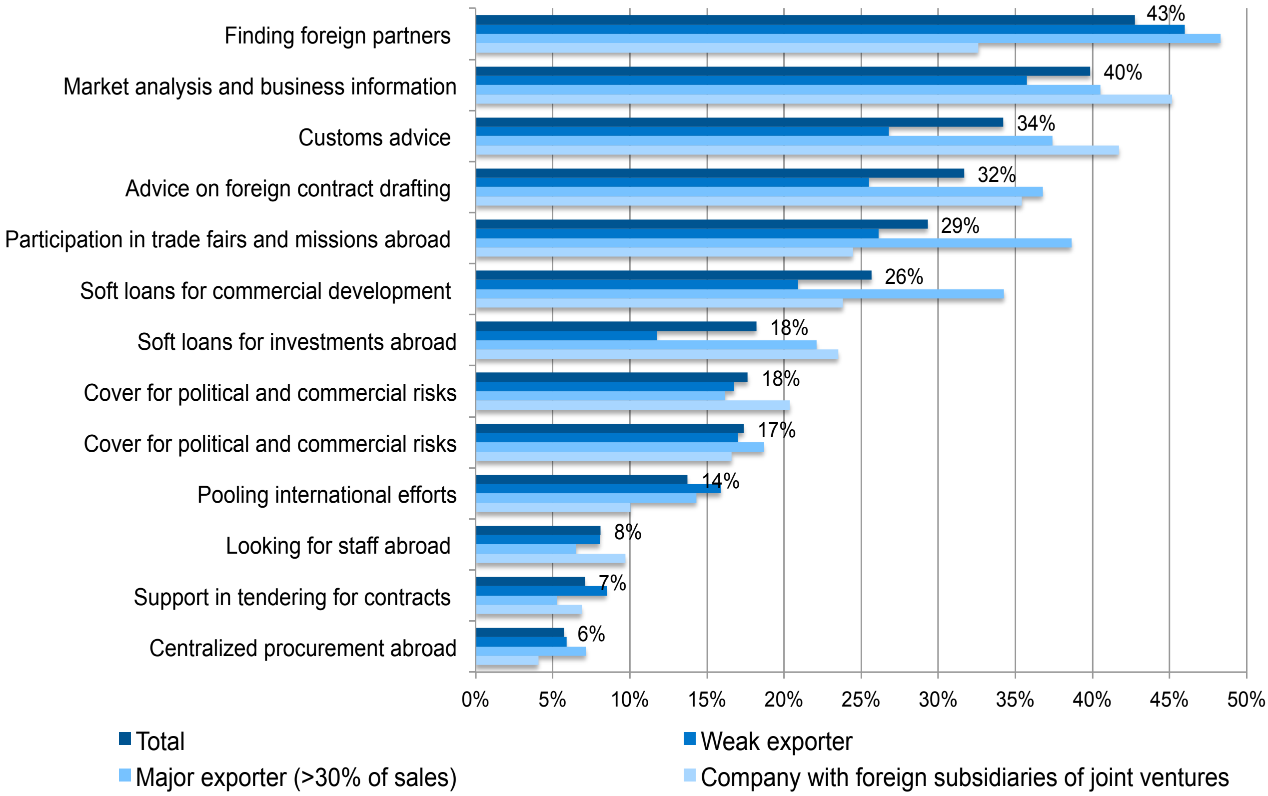
Next in order of importance come market analysis and economic information on individual foreign countries (40%), advice on customs issues (34%) and on foreign contracts (32%); then help with organizing participation in trade fairs and missions abroad (29%) and with finding business development loans on favourable terms (26%).

These results seem decidedly robust, in the sense that they are very similar to those found in last year's survey (with a different sample).

One undoubtedly useful finding was the difference among companies' opinions according to company size. Activities designed to find a partner for business-to-business meetings were by far the most highly appreciated service among smaller firms (named by more than 45% of respondents with under 50 employees); and help organizing participation in trade fairs and missions abroad was also appreciated by more of such firms than the overall average.

The bigger firms, on the other hand, valued the more complex services designed for companies which already engage in international business to some extent (see also Figure 4.6). An especially high proportion appreciated market analyses and economic information about the various countries in which they were interested (mentioned by just under half of firms with 50+ employees); the medium-sized firms (50-249 employees) also showed great interest in advice on customs issues, foreign contracts and getting subsidized loans.

Figure 4.6
Importance assigned to Confindustria services in support of international expansion, by firm's degree of international activity



In terms of economic sector, companies in the B2B sectors (engineering, chemicals, rubber and plastics, metalworking and metal products, electrical and electronic products) appeared to be particularly interested in getting help to find partners abroad, as well as those in some sectors other than manufacturing (construction, energy & environment, services). On the other hand, more than average numbers of commercial firms and of consumer goods manufacturers (food, the world of fashion, and other manufacturing sectors) appeared interested in market analyses and economic information on the countries where they were planning international activities.

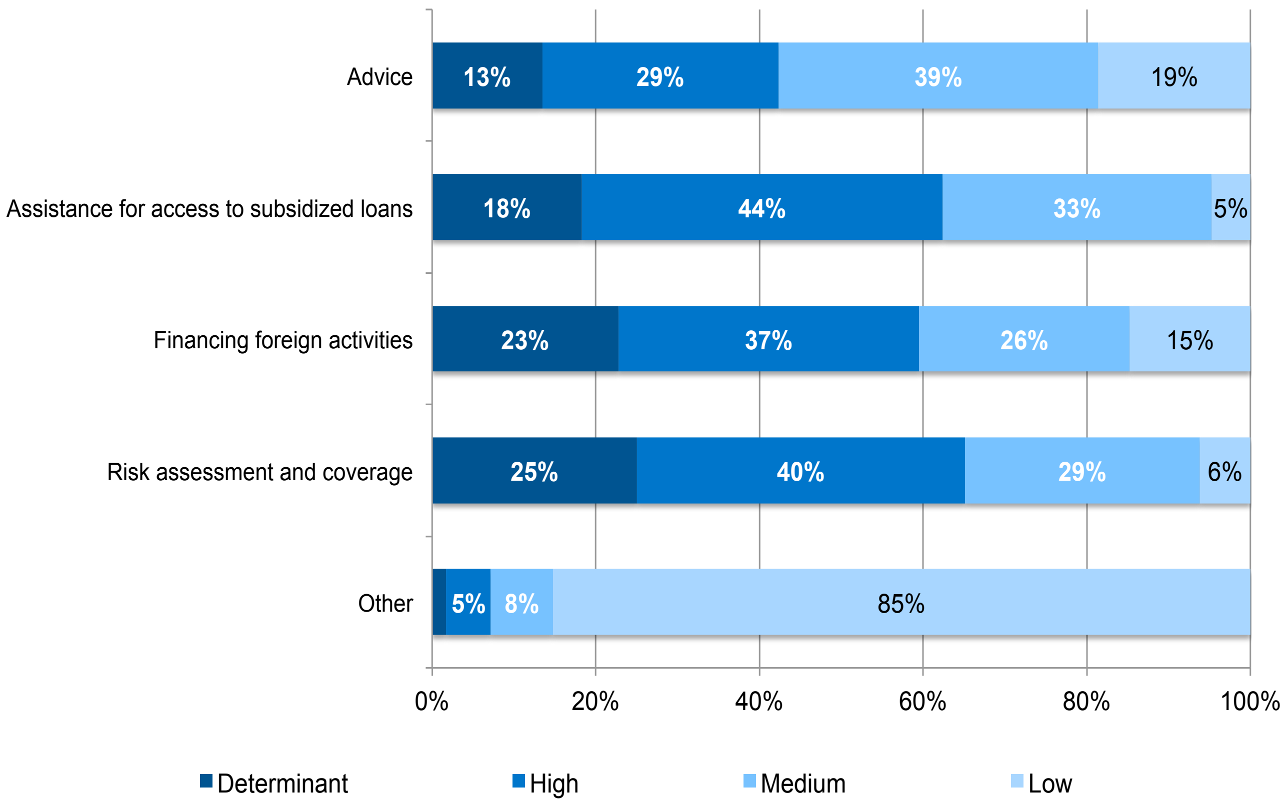
The survey findings confirm that companies' interest in international business support services is greater than it was; the Do-It-Yourself model widely used by small firms in the past – often with disappointing results – now definitely seems outmoded, especially when the foreign initiative involves taking an equity stake or putting in any sizeable resources.

4.4 The role of the banks

As discussed above, a significant proportion of firms, especially of those already engaged in international business, have recourse to the services of banks when expanding their activities abroad. As last year, respondent firms were asked a number of questions designed to bring out in greater detail their feelings about their relationship with the banking system, and in particular how support from that system features in their international expansion processes.

First, firms were asked what contribution they expect from the banks. Figure 4.7 summarizes their answers, which confirm last year's picture.

Figure 4.7
Importance assigned to having a bank/partner for various services of assistance abroad

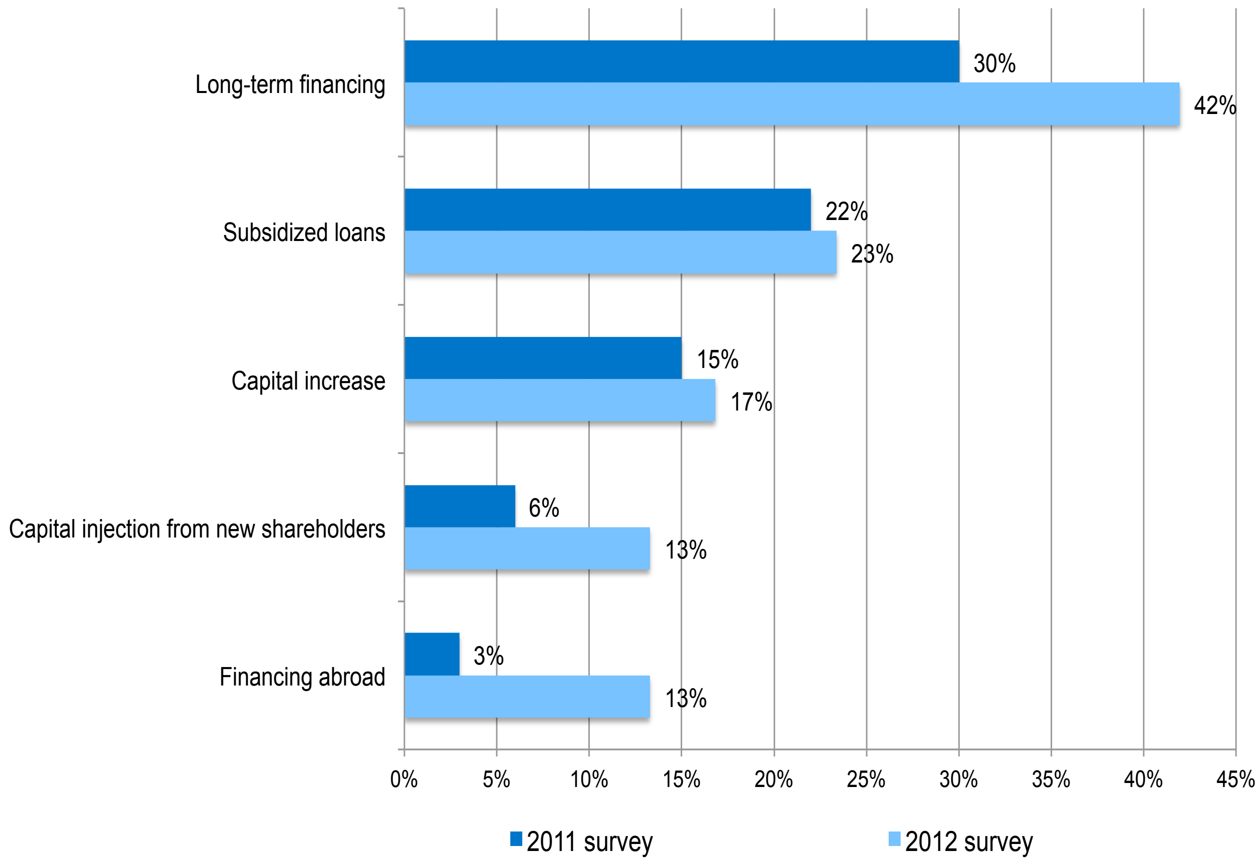


Companies most often regard it as essential to have a bank or partner at their side for support at the stage of assessing and hedging against risks (for which the support of a bank is judged “crucial” or “very important” by 65% of firms), for support in applying for subsidized loans to help with the capital investment (62%), and for funding their foreign activities (60%).

There is also an increasing tendency to ask the banks for more general advice in making decisions about the firm’s international expansion, especially among smaller firms which often regard their bank as a real partner to which they can turn for help with every aspect of a foreign venture. Expectations are moreover greater in the case of firms based outside Milan, which have a much more personalized relationship with their local bank.

There are big differences from last year’s findings, on the other hand, so far as concerns the sources of funding which firms use or intend to approach for their international development: all of the possible sources of external or additional finance are now being canvassed by many more firms – some by as many as ten percentage points more (see Fig. 4.8).

Figure 4.8
Forms of finance envisaged for developing activities abroad



This situation can be explained in part by the economic crisis, which has reduced the financial resources available to many firms; but it also undoubtedly indicates a greater awareness of the strategic importance of international activities, and of the fact that such activities call for adequate capital spending upfront and bold decisions to finance that spending.

By far the most widely-favoured choice was to take out medium- or long-term loans in Italy (41% of the respondent firms favoured this method, against 30% in 2011). 23% of companies had got or intended to apply for subsidized loans, and 17% used or contemplated capital increases.

The proportion of firms willing to open their equity to new shareholders in order to finance the firm's international expansion was double that of last year (from 6% to 13%), and no fewer than four times as many intended to raise finance outside Italy (from 3% to 13%): this last figure is an alarm bell which Italian banks would do well to notice.

4.5 International expansion through alliances

Comparison with past years' surveys clearly reveals a steady growth in companies' awareness of the practical potential of combining with other organizations to overcome the various kinds of constraint – in finance, managerial expertise and experience, etc. – which hinder their expansion in foreign markets.

Nearly 40% of the respondent firms said they were interested in some form of business combination for international projects; a quarter of those had already taken steps towards setting up such a combination. Compared with last year the proportion of firms interested in this was one percentage point higher (see Fig. 4.9).

It should also be pointed out that two years ago the proportion of firms interested in business combinations for international expansion was around 30% of the total, while actual experience of such combinations was rare. Then, an absolute majority of the sample had openly said they were opposed to any suggestion of joint activity; today, fewer than 40% of the total would say the same, the proportion having fallen by another 3.6 percentage points over the last year.

In our view this is an extremely significant figure, given Italian entrepreneurs' traditional mistrust of any form of inter-company collaboration: it means that the stakes are now so high as to overcome any reticence on that score.

The proportion of firms interested in some form of combination for purposes of international activity is almost 50% among the smallest firms, and above 40% among all companies with fewer than 50 employees; it is lower (19.2%) among those with 250+ employees, though it is among those larger companies that the highest proportion has already tried such measures in practice.

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Figure 4.9
Interest in business combinations for international projects