ITALY GOES GLOBAL

The views and strategies of Italian companies

HSBC

Internationalisation: a key factor for Italian GDP growth

Italian companies conquering foreign markets
Internationalisation remains a key driver for sustaining the growth of large Italian companies. This, in turn, has a positive impact on domestic GDP. For this reason, and to better understand the views of Italian entrepreneurs, the challenges they face and the opportunities open to them, HSBC commissioned Padua University-CMR to carry out research with both medium and large Italian companies.

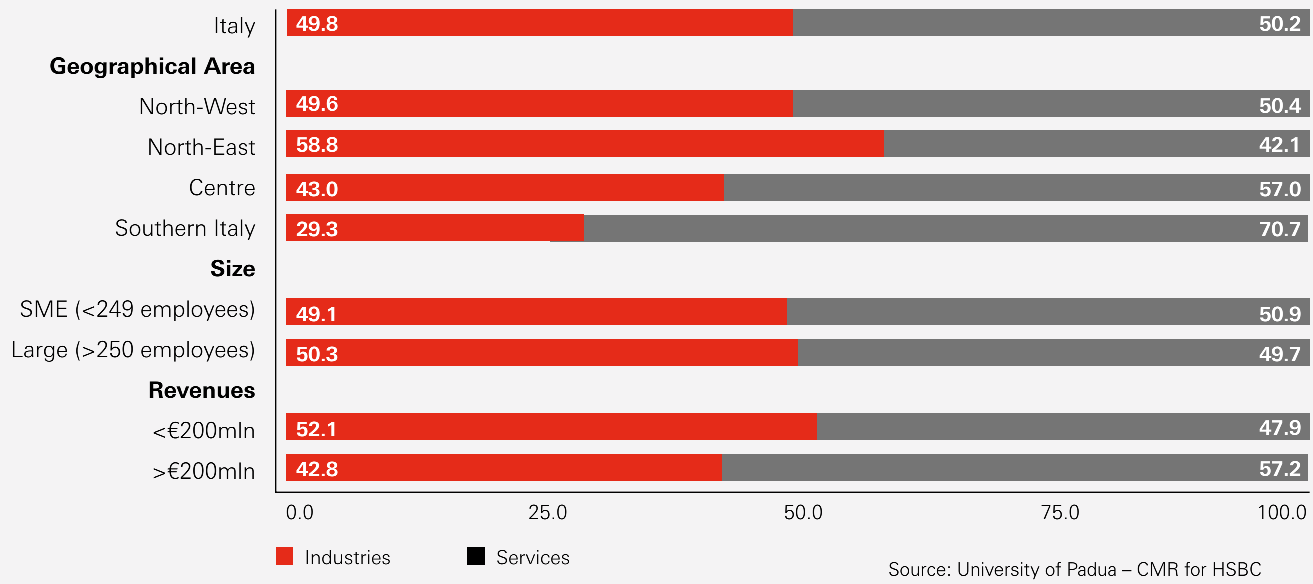
This research, one of the most comprehensive carried out in Italy, looks specifically at Italian multinational corporations with turnover above €200m and which either export internationally or invest directly in a foreign country.

The study covers a crucial topic for the Italian economy by analysing who these companies are, their general business strategies, their strategies for globalisation, their governance structure and their expectations. Alongside quantitative data, the research included interviews with 808 entrepreneurs and top managers, providing qualitative data for a more precise understanding of the internationalisation process.

The Italian large companies at a glance

- 1,276 Italian companies exceed €200m turnover.
- 424 are in the manufacturing sector.
- When holding companies are included and the analysis is extended to consolidated balance sheets, commerce and service companies make up 50.2% of the total and manufacturing and construction companies make up 49.8%.
- Most companies are located in the north-west of Italy (47.7%), followed by the north-east (29.4%), central Italy (15.7%) and the south (7.1%).
- Industrial and metalworking companies are mostly found in the north, especially in the north-east. Service companies are found mostly in the centre and south.

Company distribution (%)



Source: University of Padua – CMR for HSBC

The research uncovers a range of findings that can be used to better understand companies behaviours and needs. It also highlights key drivers of development for the growth of the country.

1 **Medium- and large-sized Italian companies are more hunter than prey.** They are active in acquisition transactions abroad. In fact, more than half have made an acquisition at least once, and 81% of these were abroad.

2 **Export is not the only solution for** companies looking to address productivity and profitability problems.

3 **Italian companies are innovative** in their products and processes and their internationalisation journey further boosts these innovation strategies.

4 **The main export sector is manufacturing**, followed by services.

5 **Italian companies are more interested in being close to their customers and the availability of key customers** than in lower production costs or the availability of qualified local partners.

6 **Local legislation, bureaucracy and tax regulations** are the main difficulties encountered by Italian companies when working in other countries.

7 **Two out of three companies do *not* use the «Made in Italy» brand** in their international business.

Globalisation: organisations and strategies

Today more than ever, companies of all sizes and in all sectors are taking steps in what is termed ***the economy of inter-dependencies:*** a real global village, in which natural and social phenomena spread rapidly across the globe.

For companies, there are two important consequences of this. The first is that no company can say *"globalisation has nothing to do with me".* The second is that companies need a new way of understanding globalisation and their place in it.

International trade *is not equal for everyone.* Companies take different strategic approaches – there are those who are active, those who act when required and those for whom the move to operating or trading internationally is involuntary.

International strategies cannot ignore the fact that the nature of the economy is evolving ever more quickly. For this reason, strategies for international operations can be interpreted in terms of *reversibility*. There are approaches that are *more easily reversible* (i.e. which allow for a change in tack without incurring excessive costs), such as direct exports, direct sales, or other forms of commercial distribution. On the other hand, there are approaches that are *more difficult to reverse* (i.e., those which incur greater costs if changes need to be made), such as joint ventures and direct investments abroad.

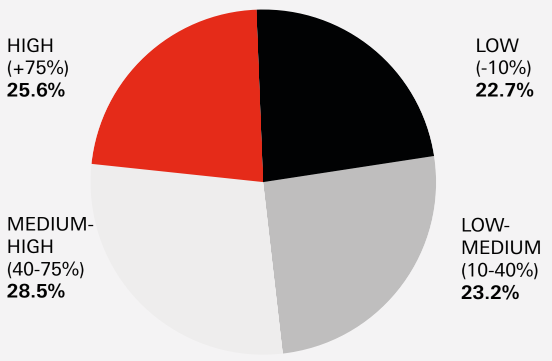
In recent years, there has been a great deal of talk regarding a sort of reverse *internationalisation*, called back-shoring or re-shoring. How can this strategic behaviour be interpreted? It is not a phenomenon that is juxtaposed *against* globalisation, but is grounded in the concepts of institutional structure, comparative advantage, complementarity and arbitrage. This means the decisions for global operations are less and less driven by a short-term (and recurring) search for the least expensive options and are increasingly steered by the search for locations where institutions work well; where they are effective and efficient.

Manufacturing companies: the effect of exporting on performance

Based on the financial statements of 424 Italian manufacturing companies with a turnover of more than €200m, the study investigated the relationship between the tendency to export and companies' profitability and productivity.

- More than a quarter (25.6%) of companies earned more than 75% of their revenues abroad.
- More than one-fifth (22.7%) do not export at all or export less than 10% of their total turnover.
- The companies that export larger proportions report a higher vertical integration index.

Propensity to export of Italian companies (export/revenues)

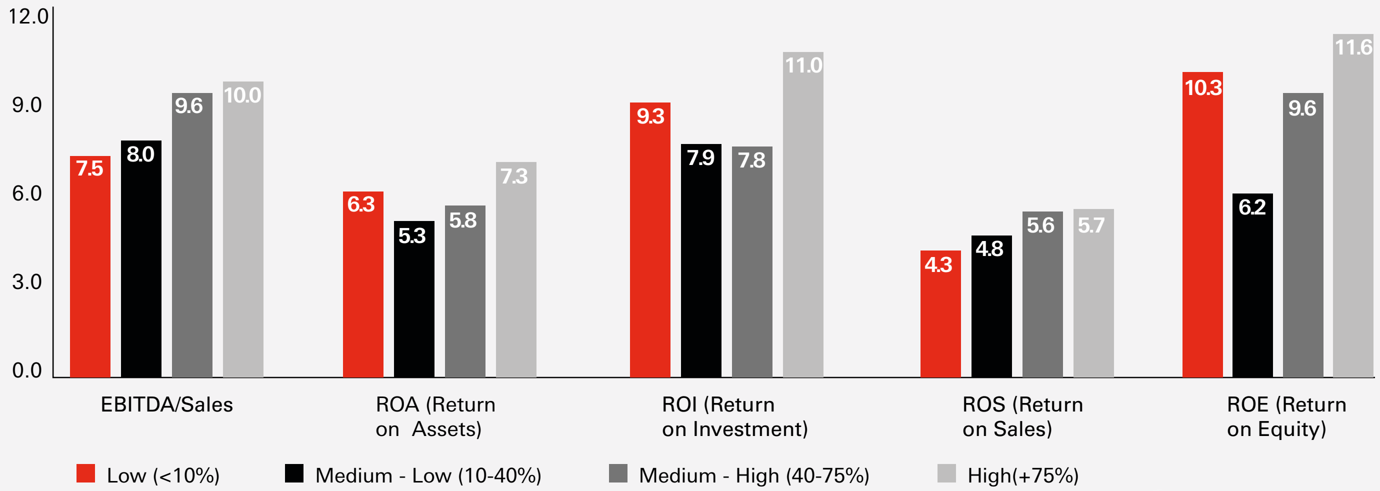


Source: University of Padua – CMR for HSBC

Profitability

To highlight the profitability of the four groups of companies, we applied the five most commonly used indicators: the ratio of EBITDA/sales, return on assets (ROA), return on investment (ROI), return on sales (RoOS) and return on equity (ROE). These indicators improve as exports rise. **Companies that export more are more profitable than others.** This applies to all profitability indicators analysed, even where there are some minor differences.

The relationship between export and profitability



Source: University of Padua – CMR for HSBC

Productivity

To measure productivity, we used the ratio of added value and the cost of labour for the 424 analysed companies. The highest productivity was for companies with a low propensity to export. Those with a medium propensity to export show the lowest productivity, but these figures are still very close to the average

These figures clearly show that there is no relation between profitability, productivity and export revenue. In other words, exporting is not a way to increase profitability and productivity. According to the economics literature[1], what characterises export companies is their productivity *before* they begin global trade, which allows them to bewtter absorb costs related to their internationalisation.

The results of the hypothesis that there are learning processes during the globalisation process (**learning by exporting**) are somewhat less clear.

Italian exporters have room for growth. Some of the companies with a low level of exports show characteristics (above average productivity and profitability) that are prerequisites for growth in international markets. These companies, therefore, appear to have the capability to drive an increase in Italian exports through intensive margin growth (average exports per company).

[1] For example: Costa, S., Pappalardo, C., & Vicarelli, C. (2017), *Internationalization choices and Italian firm performance during the crisis,* in *"Small Business Economics",* 48(3), 753-769; Fryges, H., & Wagner, J. (2010), *Exports and profitability: first evidence for German manufacturing firms*, in *"The World Economy",* 33(3), 399-423; Iacobucci, D., & Spigarelli, F. (2007), *I processi di internazionalizzazione delle medie imprese italiane*, in *"L'industria, rivista di economia e politica industriale",* 28(4), 625; Mayer, T., & Ottaviano, G. (2008); Wagner, J. (2012), *International trade and firm performance: a survey of empirical studies since 2006*, in *"Review of World Economics"*, 148(2), 235-267.

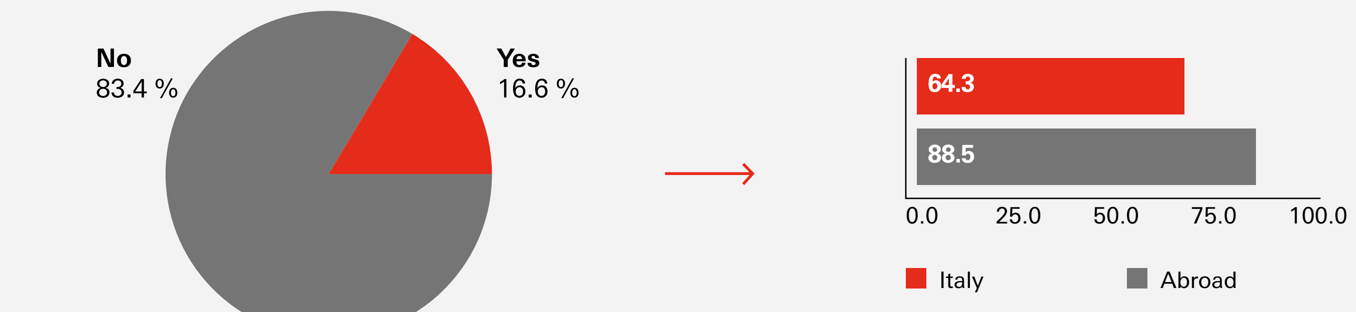
The internationalisation processes of Italian companies

Acquisitions

Only 16.6% of major Italian companies have been bought by other firms, whilst a considerably larger portion (51.8%) have made acquisitions over the years.

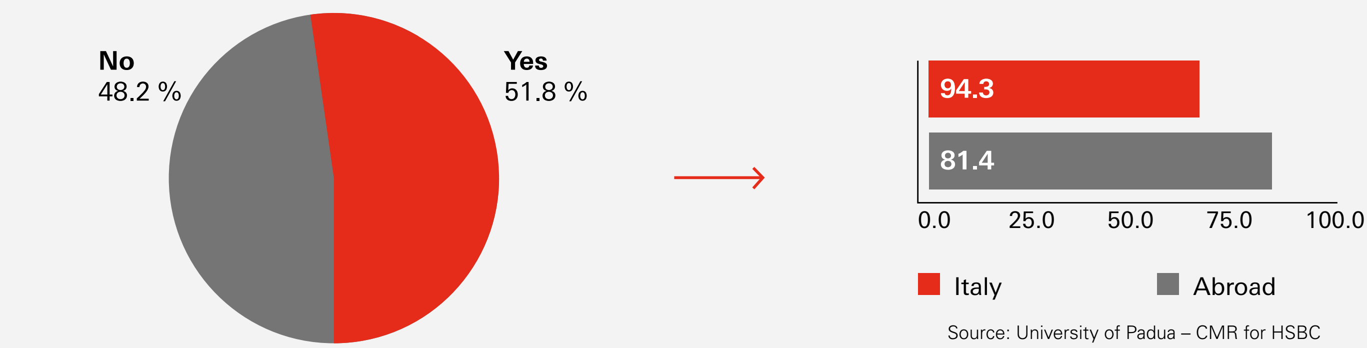
The biggest players in company acquisition are manufacturing companies (43%) and service companies (37%). 21.1% of manufacturing companies, however, have been bought by other companies. The most dynamic corporates in terms of acquisitions are located in the north-east (41.8%) and centre (45.7%).

Italian companies acquired... by businesses based in... (%)



Source: University of Padua – CMR for HSBC

Italian companies acquire... enterprises based in... (%)



Source: University of Padua – CMR for HSBC

Manufacturing and service sectors

With regard to manufacturing companies, two-thirds of their production (66.1%) is for the end-user, a quarter (24.9%) is developed for other companies as part of a chain and, 9% is machinery.

For commercial and service sectors, 56.7% work within a production chain for other companies; 15.6% have commercial relations with the public sector, and 27.7% deal directly with consumers.

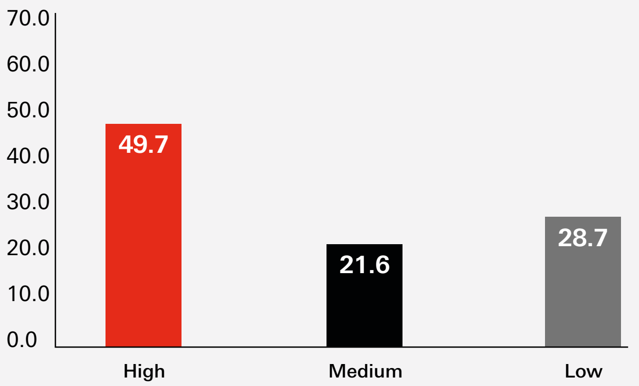
Innovation

The vast majority of companies studied said they had invested in innovation linked to products and processes. More specifically, 61% had innovated in products and 62.8%, in the production process.

Three innovation profiles can be drawn from this data – high innovators (49.7%), which have invested in both areas (product and process); low innovators (28.7%), which have made no investments in the last three years, and medium innovators (21.6%), which have invested either in innovating processed or products.

The propensity to open up relations with other markets depends on the degree of innovation introduced.

Company innovation index (%)
(Combination of product and process innovations)



Source: University of Padua – CMR for HSBC

Opening up to international trade

79.8% of companies said they had established commercial and productive relationships with foreign markets, and a further 1% reported that they would soon be launching relations with non-domestic companies. 17.2% had never worked internationally and had no intention of doing so. Just 2% had worked internationally but had stopped doing so.

Manufacturing (at 94.5%) is the sector most involved in internationalisation, while the service sector stands at 65.4%. The companies of the north-west (84.5%) and north-east (83.6%) of Italy were more involved in international trade than those in the centre (65.4%) and south (67.2%).

Opening up to foreign markets (%)

Total	79.8%
Sector	
Manufacturing	94.5%
Services	65.4%
Area	
North-West	84.5%
North-East	83.6%
Centre	65.4%
South and Islands	67.2%
Innovation index	
High	88.9%
Medium	85.6%
Low	57.3%

Source: University of Padua – CMR for HSBC

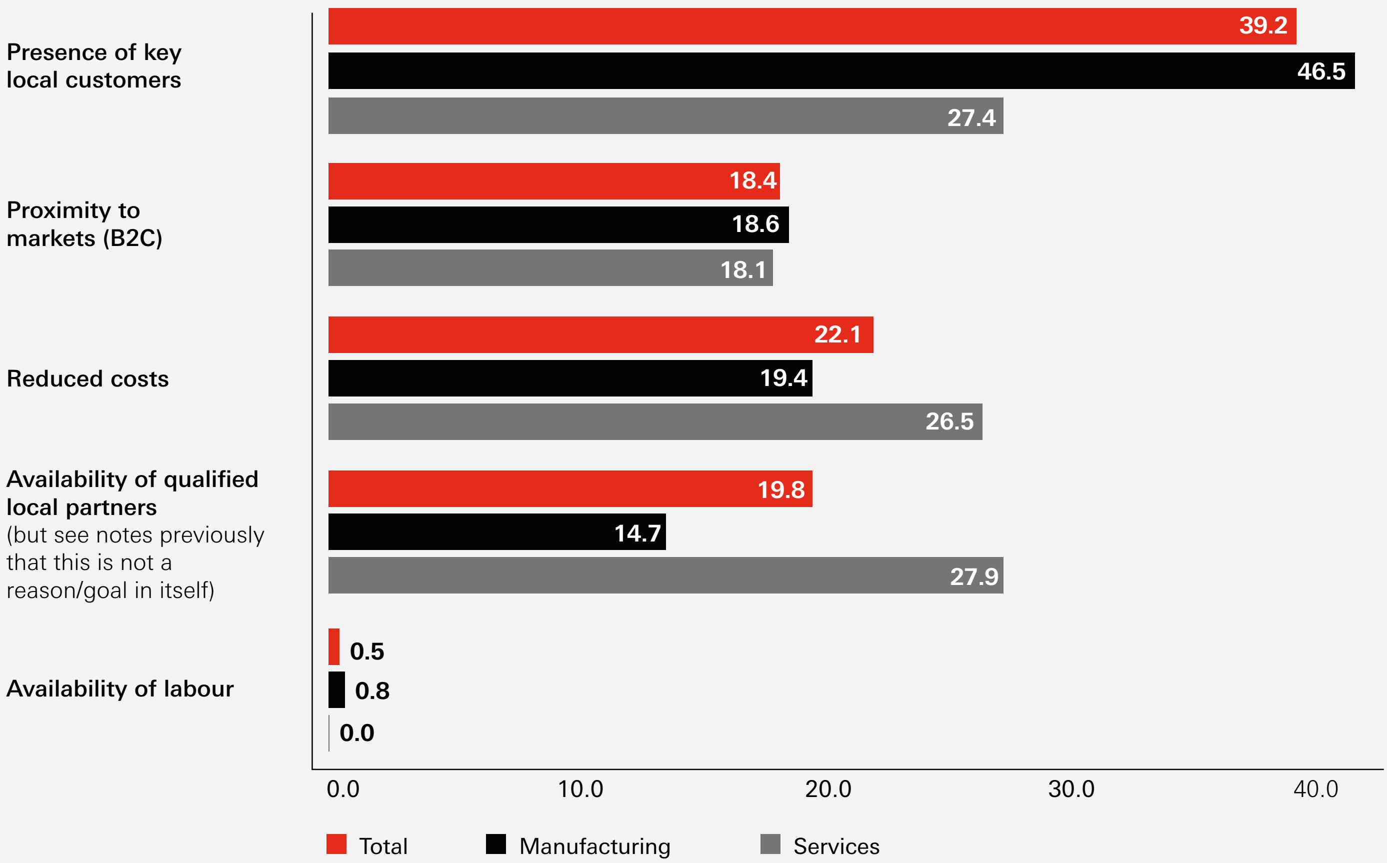
What form do these non-domestic relationships take? Firstly, we have the purchase of products or services from foreign suppliers (92%). In addition, we have the sales of their own products and services (90.1%). Commissioning the development of products or services abroad is far less common – fewer than half of those questioned (46.8%) opted for this type of initiative.

Motives for international relations

There are various reasons for extending networks beyond national borders, including some specific to sectors.

The presence of suppliers and customers is the most important factor (39.2%). 22.1% are looking to limit costs, 19.8% are looking for qualified foreign partners with whom to go into the local market, and 18.4% want to be as close as possible to their end customers. Virtually none are driven by the need or idea of finding labour (0.5%).

What drives companies to look to foreign markets? (%)



Source: University of Padua – CMR for HSBC

The proportion of companies that have opened a new plant or office beyond national borders is limited, but not negligible (35.4%). Fewer companies have moved part of their production abroad (25.7%). Fewer still have bought an existing company or production base abroad to use for their own business needs (22.1%).

The most frequent method adopted is also the simplest: using a network of local agents assigned the task of proposing products and services (42.8%). In the second place, we find those with a contractual agreement with a foreign local partner (33.9%). In third place are those that have chosen to autonomously open branches abroad without local partnerships (26.6%). Finally, a few have established a corporate joint venture with a foreign local partner (17.9%) or purchased a portion of an office/establishment abroad (14.9%).

A third (35.7%) of companies with relations abroad apply none of these methods. 28.5% opt for just one method and a 35.8% use at least two operating systems simultaneously.

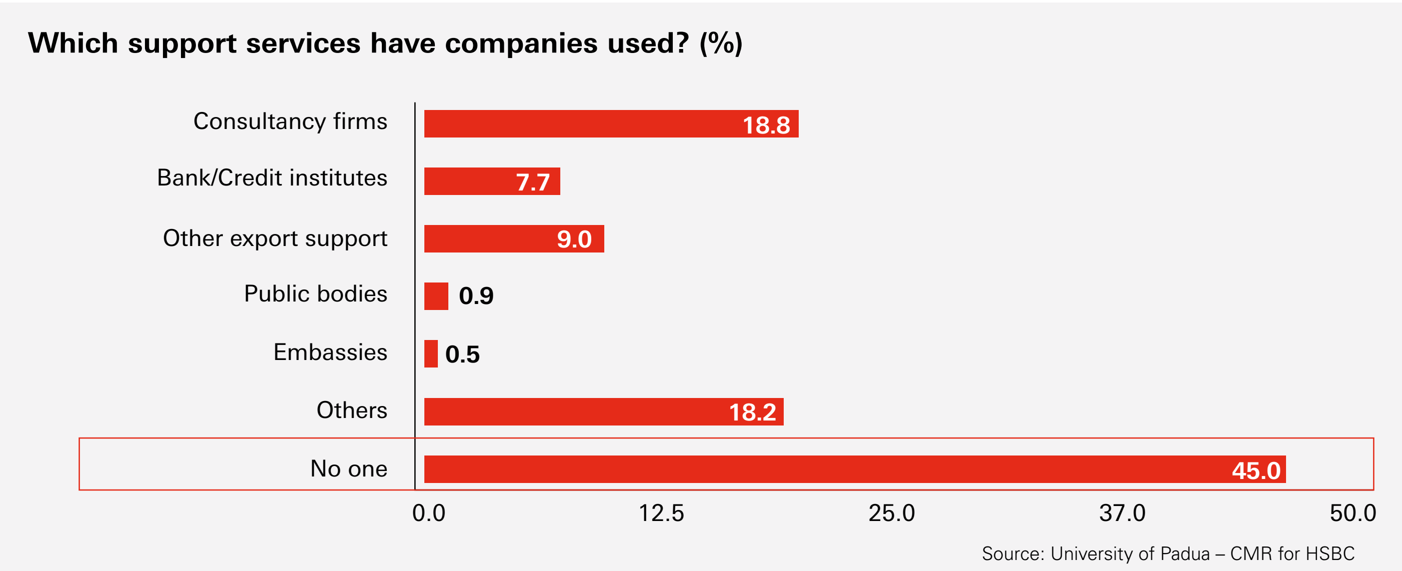
What are the main obstacles to international trade?

According to the companies we interviewed, there are problems and difficulties in international trade and operations. For 61.8% of medium- and large-sized companies, local regulations and bureaucracy are a real barrier towards internationalisation, and tax regulations are a barrier for 53.2% of Italian companies.

One-third of companies (36.5%) note low levels of difficulty in the globalisation process. By contrast, 17.3% experience considerable difficulty. 46.2% have encountered some difficulties that are not enough to hinder the process but do mean it is not as smooth as it could be.

Getting support

What support do companies turn to decide their investments abroad and to organise their globalisation processes? 45% of companies said they had worked alone, opting for DIY solutions without contacting any specific entity. 55% had contacted an entity of some kind that could help them with the planning, search for a partner and so on.



Which countries do Italian companies choose?

Most companies have a domestic market (60.8%) selling their products and services in Italy. The other 39.2% is divided between those with an outlet in the European Union (22.6%) and those able to go beyond the continental boundaries (16.6%).

Working with China

It is worth noting that 42.9% of those interviewed said they would consider production and commercial relations with China, and a further 4.2% said they would be launching there in the near future. 47.3%, however, said they did not trade with China and 5.7% had ceased trade there.

Most of those interviewed (54.8%) who had relations with China said they had encountered some (47%) or many (7.8%) obstacles along the way. The main problems were:

- Legislation, regulations, and bureaucracy (37.7%)
- Finding different types of partner – from local, industrial, commercial or financial (22.1%)
- Culture and language (20.6%)

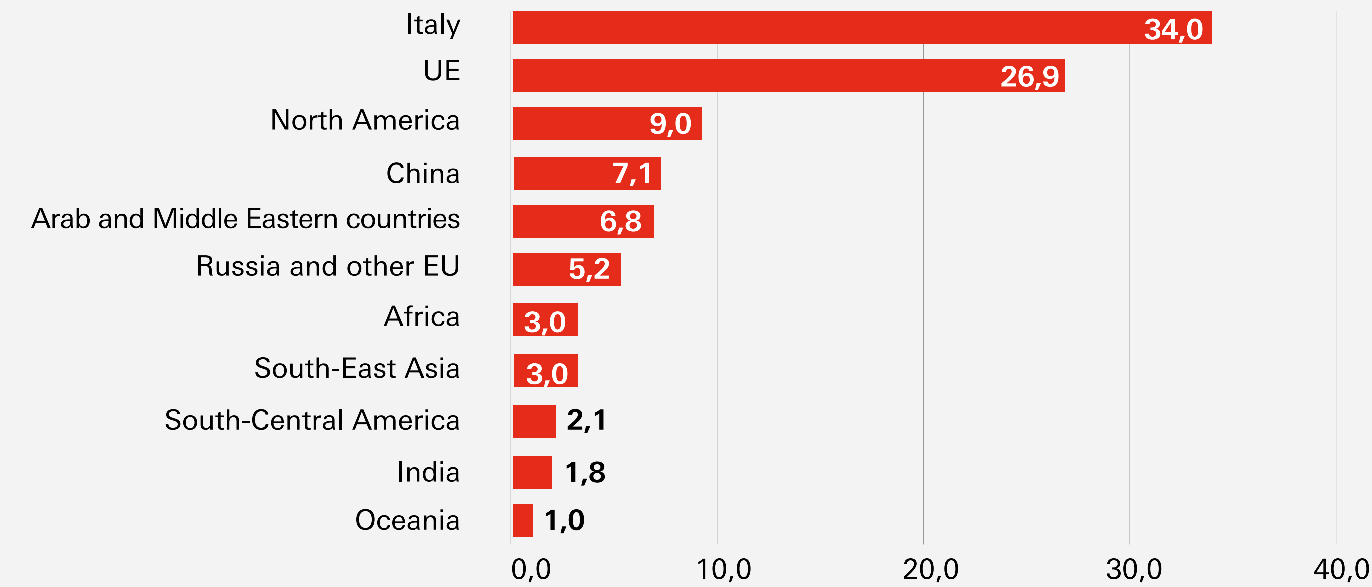
The main directions taken by Italian companies exporting outside the EU are North America (26.3%), followed by Russia and the other continental countries which are not part of the EU (22.8%), trailed by Arab and Middle Eastern countries (15.3%), Africa (9.5%) and China (9.6%).

2018-2021: Is the future for Italian companies an international one?

The domestic market is considered the most promising market over the next three years for 60.9% of companies. This is made up of Italy (34%) and the European Union (26.9%).

Beyond the EU, the preferred markets are North America (9%), China (7.1%) and Arab and Middle Eastern countries (6.8 %).

Promising markets in the next 3 years (%)

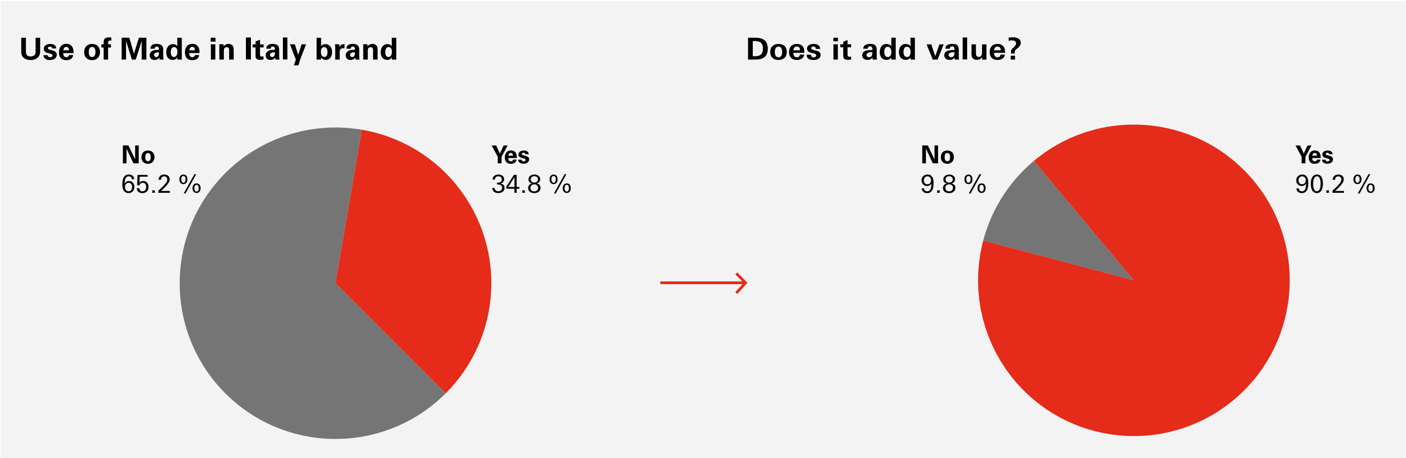


Source: University of Padua – CMR for HSBC

The research identified that the manufacturing sector will be more interested in looking beyond the EU in the next three years (52%). North America will represent a key destination for textiles companies (32.5%), food companies (16.6%) and metalworking companies (15.4%). China is considered as a prominent market for the textile (18.6%), chemical (10.5%), and metalworking sectors in the next three years.

Choices of where to trade or operate will be based mostly on the need to be close to the end customer (42%) and the market in which products are procured (30.1%).

Is the «Made in Italy» brand a real competitive advantage?
Only a third of the companies researched use the «Made in Italy» brand (34.7%). Of those, 90.2%, however, said that it generated high added value.



Source: University of Padua – CMR for HSBC

World trade prospects
Most of those interviewed (71%) believe the near future will see an increase in world trade. A quarter (27%) consider that the situation will remain stable, and just 2% foresee a decline.

These statistics reveal limited sensitivity to some threats to global trade. Most of the companies interviewed believe the hypothetical US duties (66.8%) and Brexit (76%) will have no effect on Italian exports to the US or the UK.

When asked about their use of the Chinese renminbi, 83.7% had never used the currency, and 5.8% had used it but only very rarely. The remaining 10.6% had used it sporadically. 89.1% said they saw no reason to use it. 97.5% of non-users said they didn't expect to use renminbi in the near future.

Use of Renminbi:	
Yes	10.6%
No	89.4%
They do not use it because:	
They see no reason to	89.1%
No-one has explained why they should	6.2%
Access difficulties	2.1%
They do not trust the currency	2.1%
Political uncertainty	0.5%

Methodological note

This research aims to provide a clear picture of the international business activities of 1,276 Italian companies.

The research, designed and carried out by Padua University-CMR and promoted by HSBC, included a survey of a sample of medium- and large-sized Italian companies identified through the AIDA database and broken down by geographical region (north-west, north-east, central and south/islands) and by manufacturing and services sector.

The research included qualitative interviews with a sample of more than 800 entrepreneurs and managers to fully understand the process of internationalisation. Interviews were carried out by computer-assisted telephone interviewing (CATI) and web interviewing (CAWI) between October 5 and November 17, 2017.

Distortions were balanced during processing through weighting procedures that took into account the sampling stratification variables.

The research also analysed the literature on the topics of the internationalisation of companies, the balance sheets of all Italian companies (over €200m turnover) and the survey of Italian companies.

Professor Daniele Marini, who set up, edited and directed the methodology and data processing of the research, also co-ordinated the research.

HSBC in Italy

HSBC Bank plc has operated in Italy since 1995. We offer a wide range of banking services through our branch in Milan and our office in Rome. Our clients are large domestic firms, medium-sized businesses with international operations, local branches of multinational companies, financial institutions, and the public sector. HSBC Italy's services include corporate credit and lending, trade and receivables financing, cash management, and interest rates and foreign exchange risk management. We also operate in capital markets (equity and debt), as well as in mergers and acquisitions (M&A). HSBC has a successful export finance business and plays a critical role in funding Italian exports via ECA-backed structures. HSBC provides a range of account services and electronic transactions via the home banking platform (HSBCnet), host-to-host connectivity (HSBC Connect), and the payment system SWIFT.

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