Università degli Studi
di Macerata

Dipartimento di Studi
sullo Sviluppo Economico

Working paper n. 33

March/2011

Italian FDI integration with Southeast Europe: country and firm-level evidence

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ISSN: 1971-890X

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Abstract

Southeast European countries have experienced significant economic integration into the world economy since 2000, through international capital flows and especially foreign direct investment (FDI). The present work sheds light on recent trends in Italy-Western Balkans economic integration through FDI. The methodology is based on a country level analysis and on case studies, designed to ascertain Italian firms' underlying motives for investment in the area. Evidence suggests that the phenomenon is broader than official statistics would indicate: Italian firms often set up subsidiaries without formal or direct capital control. As integration in the area is a recent phenomenon, it is not surprising that the main determinants of Italian investments are cost reductions and new market opportunities, typical of initial stages of penetration in a foreign country. What is interesting in this context is that local entrepreneurs regard efficiency-seeking investments as profitable only if they are connected to market-seeking goals. We find evidence also of localized industrial development stimulated by the entry of Italian firms which is activating subcontracting relationships with existing firms in the host region.

JEL classification: F21, F23, P20
Keywords: foreign direct investment, Southeast Europe-Italy integration, case study

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1 Introduction

During the first decade of 2000, Southeast European (SEE) countries experienced significant economic integration into the world economy through international capital flows and especially foreign direct investment (FDI). This area of Europe is becoming an increasingly popular destination for FDI by EU member countries and overseas multinationals, and is benefiting from the world-wide surge in investment flows that characterized the period 2003-07. Several factors contribute to this recent trend: relatively low labour costs, increased institutional and political stability, and a general expectation that the more advanced countries in the region will join the EU.

Economic integration of the "Old Europe" mainly involved the Central and Eastern European (CEE) countries, but has broadened to include SEE. In the post-1990s period, Western Balkan countries became important as destination markets and areas for receiving temporary exports and managing re-imports connected to the outward processing trade, which paralleled the increased interest in these investment targets. The SEE countries are becoming relevant suppliers of both intermediate goods and finished products and acting as the Old Europe's new production platform. Their geographic location at the heart of the enlarged Europe is figuring increasingly in the logistic and commercial strategies of many multinationals.

Among the EU countries involved in the deeper economic integration with the New Europe, Germany and Italy are playing pivotal roles as investors; however, these two countries present significant differences in terms of the geographical and sectoral distribution of FDI. While German firms are investing mainly in Central Europe (Slovak Republic, Hungary, Czech Republic) Italian FDI is concentrated in the lower value added industries in the Balkans region (Bulgaria, Romania) with the West Balkans playing an increasingly prominent role (Giovannetti and Luchetti, 2007).

The present paper tries to shed light on recent trends in Italy-Western Balkans economic integration based on FDI. We focus mainly on the six countries of the Western Balkans[1] (SEE-6 countries), namely Albania, Bosnia-Herzegovina, Croatia, Macedonia, Serbia and Montenegro; however some of our analyses includes Bulgaria and Romania in order to enable a comprehensive comparative view.

The country-level analysis is complemented by a case study approach to investigate the underlying motives of Italian foreign investment in the area and predict the possible effects for host countries in terms of localized industrial development. We pay particular attention to the relationship between

[1]Throughout the paper we use SEE and the Western Balkans alternatively.

the Marche region (central Italy, Adriatic coast) and the Balkan countries, in terms of its relevance for commercial flows, outward processing flows and FDI in the Balkans area. Our focus on this region enables a deeper analysis and allows us to observe the behaviour of investors in the Balkans. This context serves as a "laboratory" for our research aims since it is representative of Italian regions with a high presence of industrial districts in traditional manufacturing sectors. Hence, analysis of its economic integration with the Western Balkans is important for understanding the possibilities related to transferring a specific form of territorial organization of production characterized by a dense network of local subcontractors.

Finally, political actions, such as the Adriatic-Ionian Initiative (AII), are promoting greater integration - even at the economic level - between the two areas. The AII involves three EU member countries (Italy, Slovenia and Greece) and five Western Balkans countries in the pre-accession stage (Serbia, Croatia, Montenegro, Bosnia-Herzegovina and Albania)[2]. At the inter governmental level, there is a proposal to set up an Adriatic-Ionian Macro Region, with the aim of developing strategic actions, using a cooperative approach, to encourage inclusion of the Balkans in the EU[3]. Other initiatives include the Adriatic Euro region[4] and the IPA Adriatic Cross-border Programme[5].

Our results suggest that, among the Western Balkan countries, Serbia,

[2]The AII was primarily aimed at strengthening regional cooperation among the Adriatic coastal countries, developing common solutions to common problems related mainly to security and stability, and environmental protection of the Adriatic and Ionian Seas. See: `http://www.esteri.it/MAE/EN/Politica_Estera/Aree_Geografiche/Europa/Balcani/IAI.htm?LANG=EN`.

[3]Italy, Greece and Slovenia are the EU member promoters of the Macro Region; the project is scheduled for completion in 2014. The Macro Region will provide a forum for the discussion of and solution to common problems related to the environment, transportation, fishing, coastal supervision, small and medium companies, tourism, culture, etc. The Italian regions involved in the project are: Friuli Venezia Giulia, Veneto, Emilia Romagna, Marche, Abruzzo, Molise, Basilicata, Calabria, Sicilia, Puglia. The Balkan countries involved are: Albania, Bosnia-Herzegovina, Croatia, Montenegro, Serbia.

[4]The Adriatic Euroregion was established in 2006. It aims at developing trans-national and inter-regional co-operation between Adriatic coastal regions. It has 23 members - regional and local governments from Italy, Slovenia, Croatia, Bosnia-Herzegovina, Montenegro and Albania. For further information see: `http://www.adriaticeuroregion.org`.

[5]The IPA Adriatic Cross-border Programme is a cross-border programme co-financed by the European Commission through the Instrument of Pre-accession Assistance (IPA), designed to assist both candidate countries (Croatia) and potential candidate countries (Albania, Bosnia and Herzegovina, Montenegro and Serbia). For further information see: `http://www.adriaticipacbc.org`.

Croatia and Albania have been the main destinations of Italian FDI in recent years, and that sector attracting most Italian FDI is manufacturing. The Marche region has been showing an increased propensity to invest in the area, driven mainly by local, light industry firms. The phenomenon is broader than shown by the official statistics since Italian firms (and especially those from the Marche Region) are often creating subsidiaries without any formal or direct capital control. Since greater FDI in the area is a quite recent trend, it is unsurprising that the main determinants of investment from firms in the Marche region are typical of an initial investment: the search for cost reductions and new market opportunities. However, what is interesting is that local entrepreneurs regard efficiency-seeking investments as profitable only if they are connected to market-seeking goals. Finally, we find some evidence of localized industrial development in the Western Balkans stimulated by the entry of Italian firms which is activating subcontracting relationships with existing firms in the region.

The paper is organized as follows. Section 2 reviews the literature; Section 3 describes the data and the methodology used. Section 4 provides an overview of the country-level analysis based on secondary data sources and Section 5 analyses the Marche region in terms of FDI towards the Balkans. Section 6 presents some case studies of Marche region companies that have invested in Balkan countries. Section 7 concludes and discusses some future developments of this research.

2 Literature review

The theoretical issues related to FDI and the international fragmentation of production have been discussed, extensively and separately, in the international economics literature, typically in relation to their macroeconomic effects (e.g. Markusen, 1995, Feenstra and Hanson, 1996, Feenstra, 1998, Markusen and Venables, 1999, Arndt and Kierzkowski, 2001, Deardorff, 2001, Hummels *et al.*, 2001, Baldone *et al.*, 2007). However, very few works have examined the interplay between fragmentation of production and FDI activity. Since the sourcing strategies of business firms have become more complex, some models consider heterogeneous firms in terms of either their internalization decisions (outsourcing versus integration) (Grossman and Helpman, 2002, 2003), or location choices related to outsourcing (home versus abroad) within the context of incomplete contracts (Grossman and Helpman, 2005). This body of work focuses on why some companies source inputs abroad primarily via FDI, while others use the strategy of outsourcing for the same purpose. Grossman and Helpman (2003) find that outsourcing is more preva-

lent in larger markets and that the availability of higher quality contracting institutions abroad and lower customization costs, increase the prevalence of outsourcing. Grossman and Helpman (2005) see the cost of customization as central for deciding about the acquisition of intermediate inputs at home or abroad. Therefore, differences across countries in terms of their legal systems and institutions related to contract enforcement, may explain the pattern of international outsourcing across countries.

There is also a large body of empirical macroeconomic work, but only a few provides evidence of the involvement of Western Balkan countries in international capital flows and their role in the global fragmentation of value chains (Brada *et al.*, 2004; Damijan *et al.*, 2006; Dragusha and Bejleri, 2008; Redzepagic and Richet, 2008). Studies focusing specifically on Italy-Western Balkans economic relationships are even more scarce (Coletti and De Panizza, 2007; Giovannetti and Luchetti, 2007; Simest, 2010).

The case study part of our work is related to two main lines of enquiry in the literature on international business and industrial organization. We focus mainly on the investor, referring to the Dunning's OLI (Ownership, Location, Internationalization) theory[6], although we also provide some evidence that can be interpreted in light of the main contributions on the governance of global value chains and the related prospects of economic development in industrial clusters in developing countries.

The OLI paradigm developed by Dunning addresses three main research questions: (1) the reasons why firms go abroad (O); (2) the location of the investment (L); (3) the mode of entry used by firms uses to enter foreign markets (I). The locations chosen for firms' investment abroad is based on a combination of the ownership-specific advantages of the firm (Dunning, 2002*a*, pp. 134–135) and the location-specific advantages of the host country (Dunning, 2002*a*, pp. 135–136), that the firm wants to exploit through internationalization (through intra-firm rather than arm's-length transactions). Based on the UNCTAD (1998, pp. xxvi-xxviii) model, there are three main factors that influence the decision about where to invest. First, there are the specific FDI policies adopted by the host countries, in terms of attracting or protecting against foreign investment. From a broader perspective, the elements typical of the "ESP paradigm" can be used to take account of the economic and institutional factors characterizing the host country (Dunning, 1982)[7]. In addition, the proactive policies/incentives developed by the home

[6]For a complete review of the theoretical literature on FDI determinants, see Faeth (2009).

[7]As described in Dunning (1982), the attractiveness of a country could be analysed in terms of (E), system (S) and policies. Environment is related to human and natural

country to help domestic firms to invest abroad also need to be considered. Finally, there are some economic factors involved which mirror the initial motives for investing abroad: resource seeking, market seeking, efficiency seeking and strategic asset seeking (Dunning, 1977, 1993). Resource seeking investment is aimed at accessing natural, physical or human resources; market-seeking investment is driven by the search for domestic, adjacent or regional markets. Efficiency-seeking investment is aimed at rationalizing production to exploit economies of specialization and scope across or along value chains, i.e. product or process specialization; strategic-asset-seeking investment is aimed at advancing the company's regional or global strategy or linking into foreign networks of created assets, such as technology, organizational capabilities and markets. In this respect, Dunning (1980, 1996) distinguishes between the main motives for initial investment—namely (natural) resource-seeking and market-seeking—and the main motives for sequential investment—efficiency-seeking and strategic-(created-)asset-seeking.

The host country market has a strong influence on FDI location choice. The larger the market size and the greater its potential in terms of expected economic growth, the more attractive it is as an investment location.

In the search for greater efficiency, companies may look for lower costs of labour or other production inputs. They could gain economies of specialization and scope, through a product specialization, across the value chain, or through a process specialization, along the value chain (Dunning, 1993, p. 233). FDI may allow firms to acquire strategic assets that will compensate for competitive weakness or increase their competitive advantage, based on technology, organizational capabilities, knowledge, brands.

Of course, the importance of the drivers of investment and the related location choices will differ depending on the type of investment, the industry involved, and the size and strategy of the investor.

While the OLI paradigm is useful to understand the determinants of FDI from the investor's standpoint, the Global Value Chains (GVC) approach and the related literature on industrial clusters in developing countries (Schmitz, 1995;Altenburg and Meyer-Stamer, 1999;Humphrey and Schmitz, 2002;Cassiolato *et al.*, 2003;Giuliani *et al.*, 2005;Schmitz, 2005;Scott and Garofoli , 2007; among many others) is more useful for providing clues about the con-

resources, to technology and other strategic assets available in the country. It is influenced by the stage of its economic development and cultural/historical background. System refers to the organizational framework for the use of the resources and assets: role of government (socialist/capitalist/mixed), nationalism, international links, etc. Policies refer to the (macro or micro economic level, or FDI related) measures taken by government to achieve strategic economic and political goals.

solidation and upgrading capabilities of local firms in the host region based on their subordinate position in international productive networks. Basically, extensive case study research—mainly in Latin America, Southeast Asia and Sub-Saharan Africa—demonstrates that, among the different governance structures in GVCs (from pure hierarchy to market-based relationships), *quasi-hierarchy* is the predominant mode and results in a functional lock-in of the clusters in the GVC. This research shows also that clusters in developing countries are usually organized as a simple collection of independent, small-scale firms, which may be dominated by a few "Fordist giants" (Schmitz, 1995). The predominance of large-scale production plants undertaking production delocalized by European firms has been demonstrated by work on Mediterranean Africa (especially Morocco) (Courlet, 2006; El Kadiri and Lapèze, 2007). There is little evidence of the emergence of local division of labour in host regions following the insertion of local firms in international chains of production[8]. Instead, the entry of foreign firms has been found to produce some destructuring effects in the existing national filières (Courlet, 2006).

3 Data and methodology

This analysis is based on a mixed-method approach. First, in order to ascertain the magnitude of the phenomenon under study at both national and regional level, we analysed the available secondary data sources before collecting primary data through interviews.

For our country-level overview, we rely on two statistical sources: (1) a database produced by the External Trade Statistical Division of the Bank of Italy (for the period 2007–2009); and (2) the Reprint database produced by Politecnico di Milano-ICE.

The Bank of Italy database is based on Italian balance of payments statistics and provides detailed information on Italy's FDI outflows, disaggregated by industry and destination country. The main advantage of this dataset is that it covers a wide range of equity-type internationalization of production, including greenfield investments and foreign takeovers. It encompasses both investments (acquisition of foreign activities by Italian residents) and disinvestments (selling of foreign activities by Italian residents). As pointed out in the literature, use of balance of payments statistics entails some problems related to omissions of some FDI operations. For example, Italian FDI in financial and insurance activities in the area is underestimated because

[8]We refer to the division of labour through subcontracting relations with local firms as the "district effect".

most acquisitions by banks traditionally are achieved by means of financial holdings located in third countries, operations that FDI data do not include since they report only the first transaction (from the Italian company to the third country holding). This matters in the case of Croatia where financial triangulation is widespread especially in the banking sector. The Reprint database is based on information (from 1986) from a survey of Italian initiatives abroad; it is updated annually by the National Institute for Foreign Trade (ICE).

Our main sources of secondary data were complemented by and cross-checked with two more sources of information: the ICE country reports and the Simest (2010) report.

In the analysis of the Marche region, we integrate national statistics sources with the Fondazione Merloni database (FMDB). On the basis of firms' financial statements, FMDB collects information on more than 200 medium-sized and large companies (the biggest in terms of turnover) located in the Marche region. The FMDB gives information on the number and location of foreign companies over which the parent company has direct control. It focuses on companies with turnovers of more than €30m. and some other companies that joined the database on a voluntary basis. The FMDB is generally statistical representative of the set of local companies with turnovers ranging from €10–30m. No statistical significance is assigned to companies with turnovers of between €5m. and €10m.

The second step in the regional level analysis, is based on direct sources. Following Yin's methodology (Di Minina *et al.*, 2010) we consider that "how" or "why" questions can have significant explanatory power in case studies because «such questions deal with operational links needing to be traced over time, rather than mere frequencies or incidence» (Yin, 1994, p. 6). "Explanatory" case studies use deductive logic to test propositions and establish causal relationships (Yin, 2009). They are suited to the verification and not just discovery of new theory (Welch *et al.*, 2010).

We rely on information from entrepreneurs and managers of medium-sized and large firms involved in FDI in Balkan countries, derived from interviews based on a semi-structured questionnaire. We chose a multi-case study approach to perform case analysis replication and cross-case comparison. This allows us to distinguish among the findings from a simple case study that are unique, or applicable to the other cases (Eisenhardt, 1989; Chiesa and Frattini, 2007; Eisenhardt and Graebner, 2007). We used the direct interview method which allows researchers to develop deeper relationships with interviewees (Daniels and Cannice, 2004). Interviews were conducted between February and July 2010.

In selecting our cases, we followed the logic of theoretical sampling and

pre-selected cases that varied by industry, host location, unit size and set-up time, in order to ensure that each case constituted a "distinct experiment" and provides evidence from various perspectives (Eisenhardt, 1989; Creswell, 1998).

The case study approach is used to investigate the specific motivations of companies' investment strategies, the strengths and weaknesses of different Balkans territories, the problems and opportunities encountered in the investment and the advantages or barriers related to managing the foreign unit. Although the main focus was qualitative information, quantitative data are also analysed. Some basic quantitative indicators collected through interviews with entrepreneurs (turnover, numbers of employees, share of export in turnover) helped to construct a general profile of the firms (see Section 4.2).

4 Country-level evidence

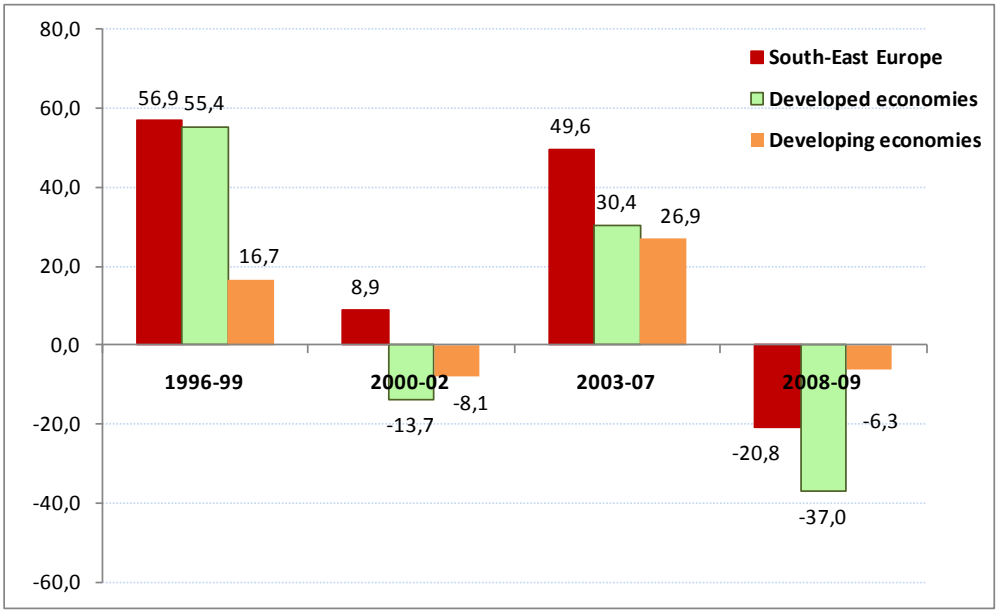
4.1 An overview of Balkan countries' FDI inflows

FDI inflows to the Western Balkans were $188m; in 1995, in 2007 this figure was $13bn. Investments increased substantially in the post-1990s period and especially in 2003–07. During the most recent worldwide economic expansion the average growth rate of inflows to SEE was 50%, much higher than the rise experienced by the developing (25%) and developed countries (30%) (Figure 1). It is believed that the prospect of EU membership and the Stabilization and Association Agreements in force or being negotiated for most countries in the region contributed significantly to the considerable increase in inward FDI in recent years since foreign investors anticipate completion of reforms in a more stable political and economic environment (Bevan *et al.*, 2001).

Geographically, total inflows are unevenly distributed across countries, with two large countries- Croatia and Serbia and Montenegro—accounting for 77% of total investment in the Western Balkans in the period 2003–07. Bosnia-Herzegovina attracted 13% of cumulative FDI inflows in the period and the remaining 10% was shared equally by Macedonia and Albania (Figure 2[9]). The role of Croatia and Serbia and Montenegro is still comparatively smaller than the roles of other main Balkan countries—namely Romania and Bulgaria. FDI cumulative inflows in these latter were twice those received by Croatia and Serbia and Montenegro, but since Croatia and Serbia and

[9]Since 3 June 2006, following the referendum of 21 May 2006, Montenegro has been an independent state. In Figure 2 we refer to Serbia and Montenegro as a single unit of analysis because of the longer period being evaluated.

Figure 1: Average annual growth rate (%) of FDI inflows, by period



Source: UNCTAD (2010)

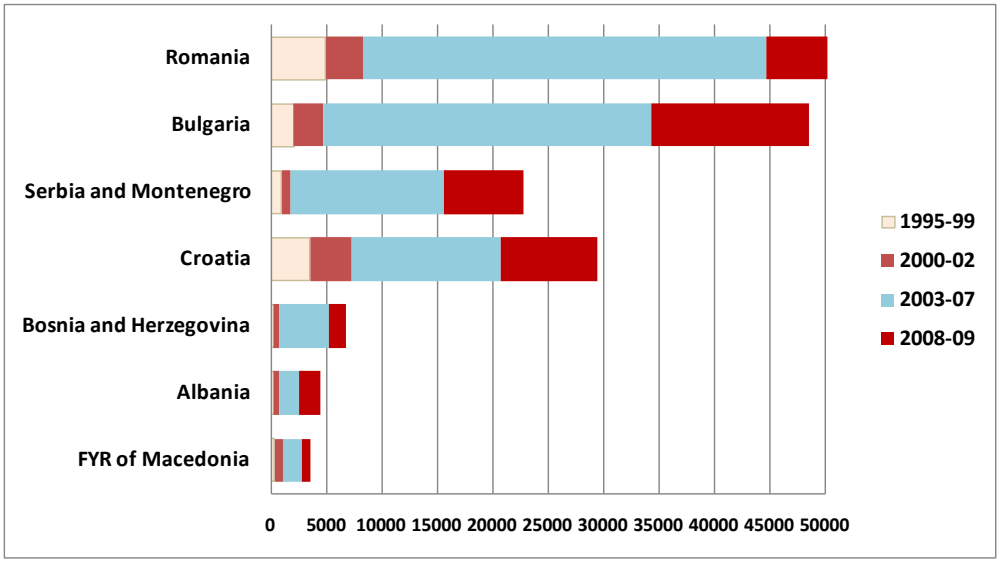
Montenegro are demonstrating resilience to the global financial crisis (GFC), their importance is likely to increase. In fact, in 2009, while FDI inflows into the Western Balkans as a whole decreased by 40%, Bulgaria and Romania experienced a decline of 54%[10].

The main sources of FDI are the developed countries, which are mostly EU members. In the past, European FDI has accounted for more than 80% of total inward flows to the area (Redzepagic and Richet, 2008) and in 2008, EU members continued to account for the bulk of FDI into the region (UNCTAD, 2009).

Italy ranks among the ten major investors in most of the Balkan countries: Italy is the most prolific investor in Albania, where roughly 48% of FDI is from Italy and 34% from Greece (Redzepagic and Richet, 2008). It is ranked fourth among investors in Montenegro, after Greece, Slovenia and Russia, and fifth for Serbia, after Austria, Greece, Norway and Germany (Simest, 2010; ICE country reports, various years).

[10]The reasons underlying the recent trends in inward FDI-particularly in 2008 and 2009- are related to both external (basically the GFC) and internal factors (stage in the privatization process). For more details on the impact of the GFC in the Balkan countries, see Cutrini *et al.* (2010).

Figure 2: Inward FDI, cumulative flows (millions of dollars) by period



Source: UNCTAD (2010)

Table 1: Italian FDI in the Balkans area (€million)

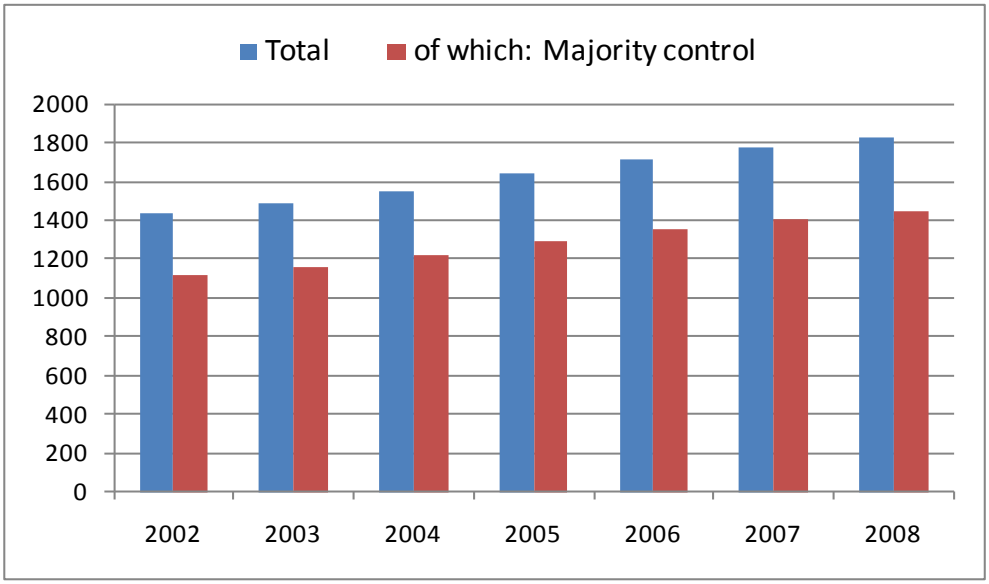
	2007	2008	2009
Western Balkans	162	108	181
Bulgaria	38	23	7
Romania	337	970	109

Source: External Trade Statistical Division, Bank of Italy

In 2007–2009, we can see the increasing importance of SEE as a destination for Italian FDI, in the context of the Balkan area as a whole (Table 1). Italian investments in the Western Balkans have remained fairly stable despite the worldwide economic downturn, while Italian FDI in Bulgaria and Romania decreased by 88% (from €993m. to €116m). In 2009, Italian FDI to the Western Balkans accounted for almost two-thirds of total flows to the whole Balkans area[11] (Figure 2). Serbia, Croatia and Albania are the main Western Balkans recipient countries, and attract substantial shares of Italian

[11]Recall that Italian investment in Balkan countries was exceptionally high in 2008 due to the huge Italian investments in manufacturing in Romania related to "coke, refined petroleum".

Figure 3: Firms in Balkan countries part-owned by Italian firms



Source: Reprint database, Politecnico di Milano and ICE

FDI to the area—46%, 28% and 19% respectively during the most recent period (2007–2009) (Figure 3).

4.2 Italian-Balkan countries' FDI

The firm-level analysis completes the picture emerging from the country-level analysis developed so far. Reprint data suggest that firms located in the Balkan countries with part ownership by Italian firms, grew continuously during the post-1990s period, increasing by 400 units between 2002 and 2008 (an increase of 28%).

Not only are Italian firms keen to have a presence in the Balkan countries, they are gaining increasing control over investee firms. The increased share of units controlled by Italian firms, from 77.8% in 2002 to 79.2% in 2008, can be related to the longer investment perspective being adopted by Italian firms (Figure 3).

The main economic activities attracting Italian FDI in the 2000s were privatization-related sectors and manufacturing, and were motivated by the financial intermediation and insurance sectors of the host countries. It should be noted that the major Italian bank holding companies (Unicredit and Intesa San Paolo) control large shares of the national credit markets in the Western

Table 2: Main Italian investments in public utilities and other privatization-related sectors

Countries	Main sectors	Some companies
Bosnia-Herzegovina	Financial intermediation	Unicredit and Intesa San Paolo
	Gas distribution	Liquigas
	Financial intermediation	Unicredit and Intesa San Paolo, Gruppo Veneto Banca, Banca Popolare Verona e Novara
Croatia	Insurance	Assicurazioni Generali
	Gas distribution	Italcogim
	Large-scale retail trade	Oviesse, Upim, Coop
	Tourism	
	Financial intermediation	Unicredit and Intesa San Paolo
Serbia	Insurance	Assicurazioni Generali, Fondiaria Sai
	Transport infrastructure (railway)	
	Electricity and gas	
	Financial intermediation	Intesa San Paolo, Gruppo Veneto Banca

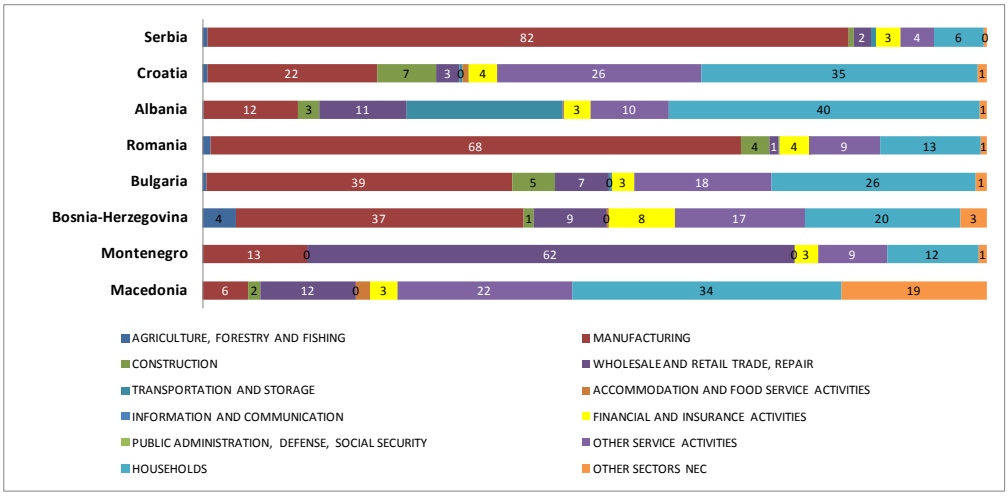
Source: Simest (2010), ICE country reports

Balkan countries: 50% in Croatia, 30% in Bosnia-Herzegovina, 25% in Serbia. The second most important privatization-related investment is public utilities (mainly gas distribution, electricity) (Table 2).

Acquisition of manufacturing companies or the establishment of cooperation agreements related to the outward processing mode of production, mirrors the Italian pattern of specialization with Italian FDI concentrated mainly in the traditional industries of textiles, clothing, footwear and furniture. In addition to Bulgaria and Romania, investment was particularly important in Albania, Bosnia-Herzegovina, Croatia, Serbia and Macedonia.

In the three years 2007-09, the sector attracting the most Italian FDI has been manufacturing, particularly for the main destinations of Serbia, Albania, Croatia, Bulgaria and Romania (Figure 4). This result is related

Figure 4: Sectoral composition of Italian FDI, by receiving country 2007–09 (%)



Source: External Trade Statistical Division, Bank of Italy

to the outward processing mode of production, which has underpinned economic relations between Italy and Romania since the early 1990s. It is now (since 2000) becoming important for economic relations between Italy and the Western Balkans[12].

Detailed analysis of the industry composition in the manufacturing sector allows us to identify two main patterns of economic integration through FDI: basic integration related to delocalization of labour-intensive tasks (*first tier*) and more complex integration (*second tier*). The former type of integration is typical of the economic relationships between Italy and the Western Balkan countries—such as Serbia, Bosnia-Herzegovina, Albania, Macedonia—and involve mostly traditional industries such as textiles, clothing, footwear and furniture. Second tier integration involves predominantly Croatia, Romania and Bulgaria which seem to have embarked on a second level of integration that includes traditional and high-tech industries (Figure A1, Table A1 in the Appendix).

The evidence related to Italian FDI to Croatia is consistent with the pattern that emerged for previous years, with involvement of both traditional and high-tech industry (see Figure A1 in the Appendix).

[12]Note that the share of Italian FDI in financial and insurance activities is underestimated because most bank acquisitions are managed by means of third financial institutions located in foreign countries.

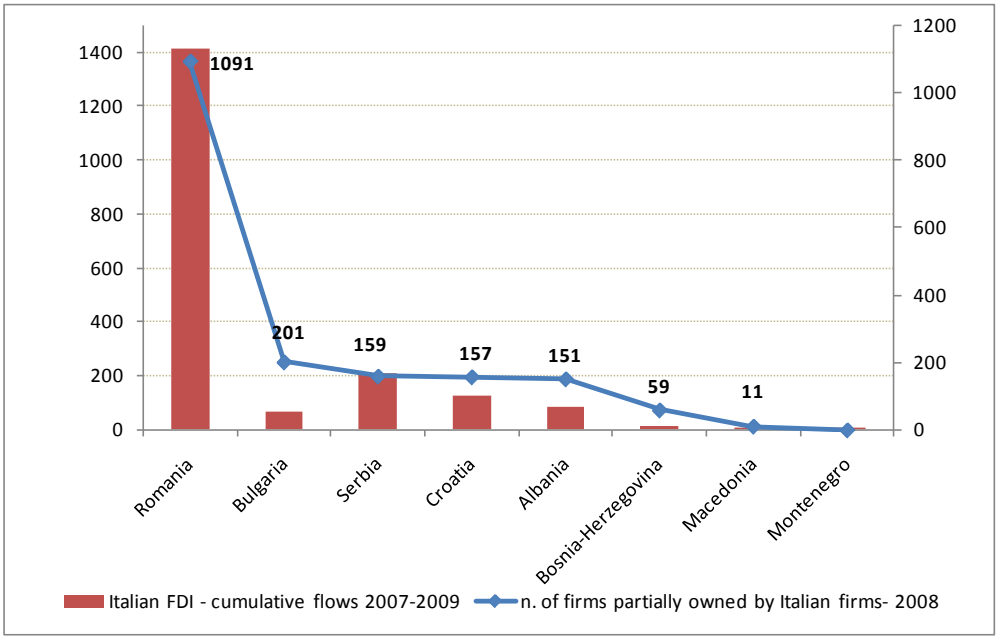
Bosnia-Herzegovina mainly attracted investment in the traditional light industries; in 2007–09 more than half (54%) of Italian manufacturing FDI in this country was directed to the textiles, clothing and footwear industries (Figure A1 in the Appendix). The Brčko Industrial Park, specialized in production and distribution, is devoted to the localization of Italian companies specialized in mechanical engineering, food, wood and construction (ICE country reports, Simest, 2010). There is growing interest in investing in the wood-processing sector, with both local and foreign companies (including Italian firms) implementing successful investment projects (see `www.fipa.gov.ba`).

In Serbia, in the past Italian investment was mainly due to the operations of Italian small and medium sized enterprises (SME) in the context of privatization; however this picture is changing with increasing involvement of large companies. Note that, in September 2008, Fiat negotiated the largest foreign investment in Serbia since the beginning of the transition process. The exceptionally high value of Italian manufacturing FDI in Serbia (€170m. in 2007–09) is due mainly to Fiat's investment in the country in partnership with the Serbian government; to a lesser extent, it is based on the textiles, clothing and footwear industries (Figure A1 in the Appendix).

Similar to world inflows, Romania is important in Italian FDI to the area. Recall that both data sources underestimate this phenomenon, for two main reasons. First, the database includes only acquisitions reported in the balance sheets of Italian. Second, only medium-sized firms are included, overlooking the increasing investment activity of Italian smaller firms which, in the 2000s, started to be involved in delocalization processes, particularly in the traditional industries in which Italy is specialized (textiles, clothing, furniture, footwear). As an example of these discrepancies in the available data, it is estimated that there are 400 Italian firms in Albania, 150 in Macedonia, 200 in Serbia and 70 in Bosnia-Herzegovina (see ICE country reports, various years, Ministero Affari Esteri, 2010, and Figure 5).

On the basis of additional regional data, analysis of the Marche region-Balkan countries' economic integration helps to quantify this phenomenon and, more importantly, accounts for some qualitative characteristics. After examining investments flows between these areas, we conducted a case-study analysis, the results of which are reported in the next section.

Figure 5: Italian FDI and firms in Balkan countries: Geographic distribution



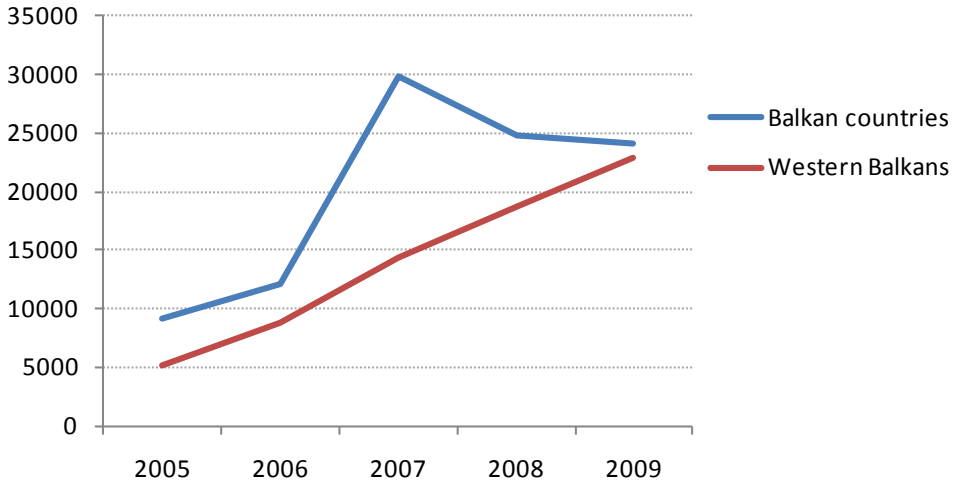
Source: Italian flows, Bank of Italy (External Trade Statistics Division); number of firms are taken from the Reprint database, ICE

5 Italian investments in Balkan countries: the case of the Marche region

The Marche region has exhibited a recent and increasing propensity to invest in the area, and especially in the Western Balkans. Since 2005, the Marche region FDI in SEE has increased continuously at an average annual growth rate of 46%. This trend is particularly significant in relation to regional FDI to the whole Balkans area which experienced a substantial upward trend in 2005–07 followed by a sharp decline in 2008–10 (-19%) (see Figure 6). The Marche region accounts for almost 12% of total Italian FDI in the Western Balkan countries, with a particular concentration in Serbia, Croatia and Albania.

In terms of Italian manufacturing FDI (and the usual focus on *nearshoring*) to the area, we note that the Marche region is an important investor, particularly in some of the most important traditional Italian specialization industries. Table 3 reports the industry composition of manufacturing FDI from the Marche region to the Balkans in the period 2007–09. It shows that it accounts for almost half of overall Italian manufacturing FDI in these industries

Figure 6: Recent trends in FDI from the Marche region, €'000



Source: External Trade Statistical Division, Bank of Italy

Table 3: Outward FDI towards Balkans countries, by manufacturing industries, cumulative flows 2007–09 (€'000)

	Marche	Italy	%
Textiles, wearing apparel, leather and footwear	50,577	78,550	64.4
Of which:			
Serbia	*48,225*	*62,066*	*77.7*
Romania	*2,152*	*11,468*	*18.8*
Bosnia-Herzegovina	*200*	*3,117*	*6.4*
Electrical equipment	7,000	16,536	42.3
Food, beverages, tobacco	6,470	16,487	39.2
Other non-metallic mineral products	440	13,084	3.4
Chemicals and chemical products	100	9,246	1.1
	64,587	133,903	48.2

Source: External Trade Statistics Division, Bank of Italy

and that the Marche region accounts for significant shares of the national FDI in textiles, wearing apparel and footwear (64%), electrical equipment (42%) and food products (39%).

The main destination countries for manufacturing FDI from the Marche region are Romania, Serbia and Albania. International capital flows in the textile, clothing and footwear industries are mainly directed to Serbia and Romania . Within the traditional light industry sectors, the Marche region is an important source of Italian FDI flows to Serbia, accounting for 77.7% of the total FDI flows in this sector. These results may be due to international outsourcing of lower value added tasks by firms in the footwear district of the Marche region (Cutrini, 2010).

Investments in the food industry involve Albania and Romania. Romania is also the only country attracting investment from the Marche region in electrical equipment during the observed period Finally, investments in chemical products and other non-metallic mineral products are directed only to Albania.

5.1 Main FDI to the Balkans: Analysis of Fondazione Merloni microdata

Analysis of FMDB data gives us information on the number and locations of subsidiaries, from which some main trends emerge.

First, it can be seen that there is increasing interest in Balkans although it might be seen as marginal in the context of the overall internationalization of local firms. The relevance of Marche region investments in the Balkans increased in the period 1999-2008. In 1999 subsidiaries in the Balkans accounted for just 9% of total units controlled outside the EU; in 2008 this had risen to 16%, a faster acceleration than in other areas. Between 1999 and 2008 there was a substantial increase in internationalization activity among local companies abroad, and the number of foreign subsidiaries more than doubled, although, investment in the Balkans area did not increase by as much as investment in East Asia and especially China, which hosed 25% foreign units in 2008 (Table 4).

From a geographical perspective, it seem that only the more economically advanced Balkan countries (Croatia, Bulgaria, Romania, Serbia) are targeted by local firms. Figure 7 shows the geographical distribution of foreign investment. Romania retains its dominant position within the group of destination countries from the beginning of the period. There was investment in all the sectors considered in at least one year in the period 1999–2008. However, note that while Romania attracts the most investment, in some cases it is short term. Serbia and Croatia attracted much lower numbers (1 or 2) of investment projects but investors seem to be taking a long term perspective in these cases. Bulgaria attracted increased attention in 2007 and 2008.

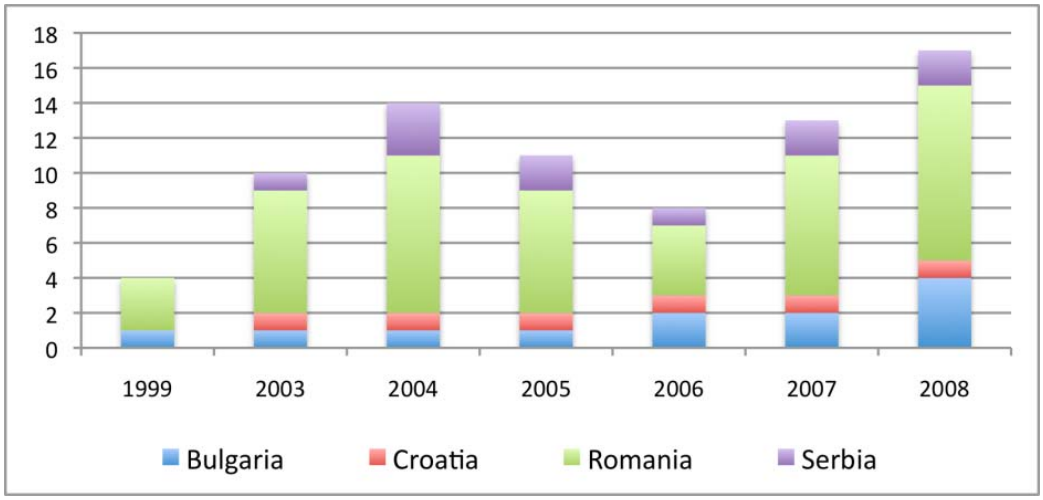
If we focus on sectors, firms from the footwear industry are the main

Table 4: Subsidiaries in non EU countries: n. of controlled companies

	1999	2003	2004	2005	2006	2007	2008
Africa	0	1	4	3	2	1	3
South and Central America	8	11	11	11	8	7	11
North America	18	21	23	25	19	16	21
East Asia	10	15	31	34	39	37	38
of which Cina	*3*	*8*	*17*	*20*	*22*	*23*	*24*
Middle East	1	1	1	1	1	1	1
Oceania	0	4	4	3	3	2	2
Eastern European and non EU countries	9	29	30	28	21	23	29
of which Balkan countries	*4*	*10*	*14*	*11*	*8*	*13*	*17*
Total	46	82	104	105	93	87	105

Source: FMDB database

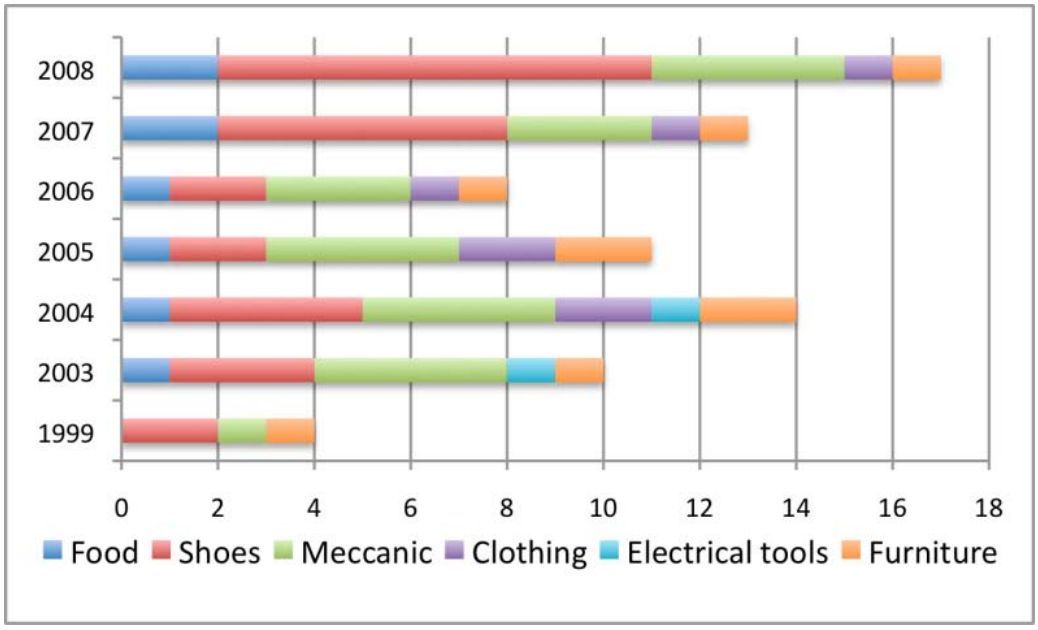
Figure 7: Italian-owned enterprises in the Balkans: The Case of The Marche region (n. of companies) in 1999; 2003–2008. Geographical focus



Source: FMDB

investors in the area in terms of both business to consumer and business to business FDI. The volatility of investment, especially in the past, can be interpreted perhaps as a symptom of the short term perspective of entrepreneurs,

Figure 8: Italian-owned enterprises in the Balkans: The Case of The Marche region (n. of companies) in 1999; 2003–2008. Sectoral focus—change spelling of meccanic to mechanical



Source: FMDB

but further research would be needed to confirm this proposition.

It would seem that firms from the mechanics industry are becoming more interested in investing in the Balkans; only a few subsidiaries are related to clothing, electrical tools, furniture and food (Figure 8). Compared to Banca d'Italia data on FDI, there are evident differences, related specifically to the clothing industry, where investment flows show a dominant share of FDI from the Marche region to the Balkans. This could be related to the fact that even small companies—generally excluded from the FMDB—are involved in internationalization through direct investment.

The most recent data provide a similar picture. In 2008, the number of Marche parent companies of units located in the Balkans was 17 accounting for about 1% of Italian companies in the area[13]. Nine units are in from the footwear sector and four belong to the Mechanics industry; ten units are located in Romania, compared to 1,091 Italian units in total in this country,

[13]We compared the FMDB and Reprint database since both refer to medium and large firms and therefore are comparable.

and four are in Bulgaria, compared to a total 201 Italian units.

These subsidiaries have several common features. They are mostly greenfield initiatives, with high control over invested capital (more than 50%, and most close to 100%). Where information was available, we checked for the role and specific functions of the subsidiary in the group. We find that subsidiaries most often are the production units of parent companies, which implies that the motivation for investment is probably efficiency seeking.

6 Strengths and weaknesses of some Balkans countries: case study analysis

The five case studies provide interesting information on the recent internationalization process of Marche region firms focused on the Balkans, in terms of the reasons for going abroad and the firms' expectations. We summarize the results of the case study analysis and then discuss the motivations for and characteristics of their investment in the Balkans in more detail.

The set of companies interviewed belong to the main sector of Italian specialization, namely textiles, clothing and footwear industries, and the mechanics industry. They are medium-sized and large companies: turnovers are between €9m. and €60m., the average being €37m. for firms in the mechanics industry and €43m. for firms in the textiles, clothing and footwear industries. Average firm size is 55 and 88 employees, respectively. The firms interviewed are quite heterogeneous in terms of their export orientation; generally, firms in the mechanics industries export less than firms in the traditional industries, with export shares in turnover of 23% and 43% respectively.

Table 5 presents the main characteristics of the nine investments in the Balkan countries. The recipient countries are Romania, Serbia, Croatia, Albania and Moldavia. Some of our results are consistent with the literature surveyed in Section 2 and especially in terms of availability of low labour cost, presence of an experienced workforce and the potential of domestic or neighbouring markets, which are shown to the main attractants of these countries.

6.1 Case study 1

Case 1 is a study of investment in Serbia. The parent company is in the footwear industry, and is specialized in the design and production of shoes. It has production plants in Italy, China and Serbia.

The company made two non-greenfield investments in Serbia: a production plant (100% owned), with 1,000 employees, and a tannery, owned 66%

Table 5a: A summary of the case-study analysis

Sector	Case Study 1 Shoes industry		Case Study 2 Mechanics industry	
	I_1	I_2	I_3	I_4
Host country	Serbia	Serbia	Croatia	Romania
Year of investment	2004	2006	1995	1999
Main reason	Efficiency-seeking	Efficiency-seeking	Market-seeking	Efficiency-seeking/Market-seeking
Mode of entry	Non greenfield	Non greenfield	Greenfield	Greenfield
Stage outsourced	Production plant	Tannery	Commercial office	Production plant/Commercial office
Ownership structure	100% ownership	66% ownership, Partnership with a Serbian entrepreneur	80% capital control	100% capital control
Governance of the value chain	Hierarchy	Quasi-Hierarchy	Quasi-Hierarchy	Hierarchy
N. of employees	1000	150	7	46
District effect	Yes			Yes

Note: non greenfield investments refer to acquisitions of existing companies

Table 5b: A summary of the case-study analysis

Sector	Case Study 3 Clothing industry
	I_5
Host country	Romania
Year of investment	1997
Main reason	Efficiency-seeking
Mode of entry	
Stage outsourced	Production plant
Ownership structure	No capital control
Governance of the value chain	Market-based
N. of employees	200
District effect	Yes

Note: non greenfield investments refer to acquisitions of existing companies

Table 5c: A summary of the case-study analysis

Sector	Case Study 4 Mechanics industry		Case Study 5 Textile industry	
	I_6	I_7	I_8	I_9
Host country	Moldavia	Romania	Romania	Albania
Year of investment	2004	2008	2001	2010
Main reason	Efficiency-seeking	Efficiency-seeking/Market-seeking	Efficiency-seeking/Natural resource-seeking	Efficiency-seeking/Market-seeking
Mode of entry		Greenfield	Non greenfield	Non greenfield
Stage outsourced				
Ownership structure	70% ownership, Partnership with an Italian entrepreneur	80% ownership, Partnership with a Romanian entrepreneur		Joint venture with majority control
Governance of the value chain	Quasi-Hierarchy	Quasi-Hierarchy		Quasi-Hierarchy
N. of employees	12	12	35	
District effect	Yes	Yes	No	Not yet

Note: non greenfield investments refer to acquisitions of existing companies

in partnership with a Serbian entrepreneur, with 150 employees. The two companies are located in different areas of Serbia, 300 km apart.

The approach adopted to investment in Serbia has been gradual, part of a strategy that might be defined as "explorative". Serbia was selected after investigating various countries for the outsourcing of phases of production. Romania and Poland were considered not sufficiently competitive in terms of labour cost advantages, due to their EU accession; Serbia on the other hands has comparatively low labour costs and advantages in terms of an experienced available work force. Many local firms in the footwear industry have acted as international subcontractors for Western companies, especially German and US firms.

In the 1990s discussions began about the possibility of outsourcing some production phases to Serbian subcontractors. Initially, some small and marginal production tasks were outsourced. After a period of "testing", the privatization of state owned enterprises in Serbia allowed the case company to consolidate its presence in the country.

There is currently a complex structure that has been set up to manage the entire production process, with the result that for some footwear lines the finished shoes are made entirely by the Serbian unit. The two companies located in Serbia are managed by Italians and production activities are supervised by Italian technicians. It is interesting that the production plant is linked to other small subcontractors located nearby to which specific phases of production are outsourced, giving rise to a local division of labour typical of an industrial district.

The reasons driving the investment in Serbia in this case can be "classified" as efficiency seeking. The low labour costs and availability of skilled and trained workers were fundamental to the delocalization strategy. However, the area was also seen as a strategic location to reach Eastern European countries as well as the CIS and Russia. The Serbian unit acts as logistic pole in the group, which indicates an asset seeking strand to the investment strategy.

Despite the savings in labour costs, the case study reveals a persistence in the characteristics of employees working for local branches, that are typical of their state-owned heritage. Poor management control techniques and managerial skills imply additional costs, beyond the coordination and monitoring costs. The interviewees did not see corruption, relations with local public institutions, or political instability as critical, and were of the opinion that they were not much different from conditions in Italy. However, it was acknowledged that relationships with local banks are difficult since credit is not competitive. Financial needs are resolved by intra-group flows.

6.2 Case study 2

The second case study deals with a mechanics industry firm which made two investments, in Croatia and Romania. The company produces pipes, evacuation and water treatment systems, complete sewerage systems, waterworks, gas pipelines and drainage systems.

The Croatian company was created, as a greenfield initiative, in 1995, with 80% of capital control. It comprises a commercial office, located in Split, with 7 employees: 2 in sales, 1 in administration, 1 in logistics. The Croatia investment was driven by market seeking motivations. The company wanted access to what it saw as becoming a new and promising market, once post-war reconstruction was completed. This relatively small investment gave the opportunity to explore actual interest in the Croatian market prior to more intense investment in the form of a production plant or warehouse.

The parent company decided to invest in the country since, in the mid-1990s, Croatia was a growing market with prospects of significantly increased domestic demand. It was also geographically well placed near to areas with potential high demand for primary infrastructure works, such as other former Yugoslavia countries and the CIS. Finally, Croatia has a good transportation system which enables the movement of goods.

At the time of writing, and perhaps as a result of the GFC, demand for infrastructure works is declining in Croatia (but increasing in neighbouring countries) and there are delays in payments due to freezing of public funds. The same firm's investment in Romania shows slightly different characteristics and underlying motives. The Romanian subsidiary was created in 1999, with 100% capital control. The unit acts as both a production plant and a commercial office. It is located in Suceava and has 46 employees. Romania was considered important in terms of providing access to a new market and in being a geographically strategic location. The local administration and the EU were providing investment facilities which, at the time, reduced the cost of the greenfield investment. All efficiency-seeking advantages were associated with reduced labour costs which promoted efficiency gains. Romania did not seem to suffer from any particular critical aspects apart from the persistence of informal institutions and workforce habits which hindered communication with the Italian employees. The Romanian subsidiary activated collaborations with local suppliers of accessories for the installation of pipes, and with local subcontractors willing to undertake parts of the production process, evidence again of a district effect.

6.3 Case study 3

The third case study is a clothing company, that designs and produces to order under customers own brands. Exports represent 75% of production. In 1997, the entrepreneur made the decision to invest in Romania and, currently, 40% of production is located there, the remaining 60% being in Italy. The Romanian subsidiary is located in Alba Julia and employs about 200. It is run by an Italian managing director and production activities are supervised by Italian technicians.

There is no formal capital control over the Romanian unit, which acts as a unique supplier to the Italian parent company. It is specialized in the production of trousers: the raw materials are supplied by the Italian company and the semi-finished trousers are re-imported into Italy for final finishing. The Romanian company relies on a number of local subcontractors. Similar to case study 1, it is a hub in the territory, around which a local division of labour typical of industrial districts has emerged.

The quality of production is considered good; there are no language difficulties and, more importantly, employee turnover is low. It should be noted that the advantages of this location, mainly the labour cost differential, which drove the original investment are no longer available in Romania. Currently, delays in production timing—the major disadvantage—are no longer balanced by efficiency savings. The company continues just because of the problems involved in disinvesting. The infrastructures and services in Romania did not evolve as expected and EU accession in 2007 has not enhanced the quality of the business environment.

6.4 Case study 4

The fourth case study is a company in the mechanics industry. Its activity is related to moulding of ferrous materials, and production and co-design assistance in various sectors (white goods, automotives, furniture, weapons, etc. ...). The company has made two investments in the Balkans—the first in Moldavia and the second in Romania.

The Moldavian company was created in 2004, in a 70%:30% partnership with an Italian entrepreneur living in Moldova. It is located in Chisinau and has 12 employees. The subsidiary carries out assembly operations for the automotive sector using spare parts produced by the parent company in Italy. It undertakes production to order in welding, manual and mechanical assembly, and also moulding.

The Moldavian company relies on local subcontractors for particular paint procedures, and has emerged as a hub of the district that has developed in the

area, with a local organization of production similar to those in case studies 1 and 3. Initially, the company found it very difficult to source even the simplest components and machinery/equipment. It had to get everything from Italy ("even wrenches"). When the first contact with a local subcontractor was established, getting reliable quotes was a problem. However, procedures and work flows have been standardized and commercial relations in the area are good.

The decision to invest in Moldavia was based on efficiency considerations: Moldavia offers low labour costs, economic and political stability and low risk for investors. Its national company law was inspired by the European model, especially in relation to property rights and intellectual property protection. The workers have good mastery of the Italian language and there are Italian banks in the area. Customs duties on good exported to the CIS are favourable making products/services sold to these markets through Moldavia more price competitive.

Despite these advantages, certain problems have emerged. Investment is required in workforce training to enable achievement of required quality standards. Logistics management is strategically important because transportation costs and the costs related to customs procedures are very high.

The second and more recent investment was in Romania in 2008. This was a greenfield initiative, in partnership (80%) with a Romanian entrepreneur (20%) who previously had worked in Italy. The company is located in Arad and has 12 employees: 3 in administration and 9 in production. It is run by the Romanian partner with production activities supervised by Italian technicians. It is specialized in powder coatings to order.

This investment in Romania was driven by market seeking and efficiency seeking motives. The country offered internal market opportunities based on increasing domestic demand. A subsidiary in Romania was seen as important to align with the internationalization processes of big customers that had delocalized in the country and to exploit a timing advantage compared to other European competitors. There were no similar companies in the area at the time of the investment.

The city of Arad was close to local mechanics firms that required painting services. Geographical proximity is crucial to reduce the costs and risks of damage to painted parts. The subsidiary's location was strategic in terms of its proximity to interesting and promising markets, such as Hungary, and Old Europe (there are good motorway connections). In addition, this Greenfield investment was made to transfer to Romania an Italian plant, which was inefficient due to the high labour costs in Italy.

There was already a vast net of local suppliers in the area since many Western industrial groups were already located there. Unfortunately, punc-

tuality, cost and quality of the service were unsatisfactory and not competitive. Relationships have been developed with the Romanian branch of an Italian supplier, which is providing important competitive advantage in terms of flexibility (time/mix of products available) and costs.

There are also some downsides to investing in Romania. These are related mainly to the quality of bureaucracy, the legal system and the financial institutions. Establishing a utility requires long and time-consuming procedures. The high costs of services/utilities and rentals tends to counterbalance the competitive costs of labour. There is a lot of time wasted on the requirements of the fiscal and labour agencies.

Relationships with the banks, even local branches of Italian financial institutions, are critical. Credit costs are high, even when backed by assets. There is no easy access to "traditional" and simple financing instruments.

Finally there is a lack of specific expertise in the use of techniques and instruments crucial for the management of relationships with suppliers and banks by employees responsible for administrative tasks. This is another example of the inconsistency between the new economic environment and the inherited social systems that include education systems that do not include training and qualification in economics or management.

6.5 Case study 5

The last case study involves two investments in the Balkans, in Romania and Albania, by a medium sized company in the textile sector engaged in special finishes to goods and fabrics related to dyes, wear and tear, etc.

The investment in Romania was made in 2001 to diversify the group's activities in the production and manufacture of wood for stripped wood and parquet flooring. It was a non-greenfield initiative: the entrepreneur and another private Italian investor, decided to acquire a Romanian company in order to take advantage of the good availability of high quality, solid oak and low labour costs. After the acquisition the company was completely renewed. All equipment was imported from Italy to build a new plant that conformed to EU rules and requirements. There are currently 35 persons working in the company, which is managed by locals. Negative aspects of location in Romania relate to microeconomic characteristics and the macroeconomic environment, namely lack shortage of entrepreneurial perspective, and lack of a potential domestic market.

The same parent company invested in Albania in 2010, through a joint venture with a group of Albanians who had worked for the company in Italy on the sandblasting process. The Italian company, which has majority control, transferred the knowhow and technical equipment; the Albanian partner

provided a skilled workforce, entrepreneurship and knowledge of the internal market. The specific advantages of Albania are related low labour costs and the fact that in the effort to anticipate the future investment strategies of other clothing industry companies, several important high-fashion groups have invested in the area. The company is planning to establish a production plant in Albania and become the leader for sandblasting. Fiscal facilities are available.

6.6 Some "lessons" from the case study analysis

We can draw some initial conclusions from the case study analysis so far.

The phenomenon of direct investment by companies in the Marche region in the Balkans is more widespread than represented in the official statistics. Some subsidiaries are created without formal or direct capital control. The companies interviewed reported the presence of many Italian (and particularly Marche region) small entrepreneurs who have invested in local companies or developed subcontracting relationships with local producers. Since it is small companies that are involved in this internationalization process, and they are not recorded in national databases, it is difficult to map the real scale of Italian investment in the area.

When investment in the Balkans is driven by efficiency seeking reasons exclusively, they seem to be less competitive and rewarding. Labour costs are increasing, and utilities and services are particularly expensive. If delocalization is driven by the search for cost competitiveness, other important areas—such as SouthEast Asia—could be a better solution and provide greater scope for simple reductions in production costs. The Balkan area, however, is well placed strategically and is also a potentially good market for Italian products, both business to consumer and industrial production. The interviewees suggested that when considered as a destination market or logistic hub for reaching other emerging/growing markets, investment in the Balkans is regarded as valuable and profitable. In this case, even the GFC has not changed firms' positive evaluations of investment in the Balkans, despite a small reduction in orders and production.

Another important finding is that Italian units in the Balkans support local subcontractors taking on specific phases of production. Usually, Italian investment creates a business culture in the area and a sort of "cluster" or district emerges. It would be interesting to develop the present analysis in order to get a deeper understanding of the scope of this "contagion" effect and its consequences in terms of the fragmentation of production processes and localized industrial development.

We can draw two lessons from our case-study analysis which have impor-

tant implications for local and regional policies in the area of origin and in the destination country.

First, that small companies do not use the support of public agencies and bodies to explore investment opportunities in the area. It seems there is a gap between companies and institutions which could be seen as wasted opportunity.

Second, companies underlined the need for training administration staff to meet Western business standards, methods and techniques. While they are satisfied with the production workforce, the administrative staff is less satisfactory.

From a policy perspective, what is needed to enhance and reinforce economic integration between Italy and the neighbouring Western Balkan countries are (1) better provision of information on the support for internationalization, and (2) improved management competences in the local workforce.

Finally, relationships with banks are difficult and expensive. There is no access to "traditional" and simple financing instruments—even asset backed one; there is no access to inexpensive credit. Italian companies try to overcome this problem with intra-group financial planning but more efforts at government level are needed to push Italian banks that have assumed a leadership position in the Balkans, to support the development of Italian business relationships in the area.

7 Concluding remarks and further developments

Despite the broad consensus that the involvement of Balkan countries in the context of the EU accession process is having an impact on their international economic integration, up to date evidence on inward FDI in the area is limited. This work tries to shed light on the magnitude of the phenomenon and unravel the main determinants and characteristics of FDI in the area. We relied on a mixed-method analysis referring to secondary sources of data and to original information collected through case-studies.

In the light of the specific political actions designed to strengthen political and economic integration between the two areas (e.g. the Adriatic-Ionian Initiative and previous initiatives such as the Adriatic Euro region and the IPA Adriatic Cross-border Programme), this article contributes to the knowledge on the state of economic integration so far within the two areas, with the aim of helping the formulation of appropriate policies in a multilayered perspective, encompassing EU, national and regional levels. A deeper understanding of the different forms of economic integration should help to support the most efficient use of existing EU instruments and funds at national and

regional levels, to enhance the governance and economic capabilities of the Western Balkan countries.

The evidence provided may provide a better understanding of the nature of the internationalization process of Italian firms in the Balkans area, although there are several issues that require further analysis at national and regional level.

The integration of trade between Italy (the Marche Region) and the Balkans should be analysed. The typology of import and export flows and the magnitude of outward processing trade need to be assessed in order to evaluate the role and importance of international outsourcing. At the same time, the role of the different forms of contractual links (e.g. cooperation agreements, non equity joint ventures, ...) between Italian and Balkan companies, particularly SME, requires further study. In this respect, more case studies are needed because official statistics are not available. More case study evidence as well as macroeconomic analysis are needed to understand another phenomenon. In analysing FDI trends in the Balkans, as well as investment from the Marche Region, we found that in some cases—particularly in Romania—investments are highly volatile. It is important to understand whether companies' behaviour is being driven by seeking a first exploration of the country with a view to successive investments or by a short term investment strategy. It would be interesting to know whether this phenomenon is typical or if it is due to poor definition of corporate strategy. It could be related to a specific sector, perhaps footwear. However, at this stage in our research, the case study approach has not enabled deeper exploration of this aspect. More cases are needed.

Different investment strategies and behaviours towards different Balkan countries might be related to the institutional environment (country's regime type, level of property rights protection, quality of education, government policies and incentives, etc.) or to the market/firm/industry characteristics (such as host market size, wage rates, transport costs, level of foreign competition, industrial disputes, etc.).

Finally, future analysis should focus on the potential effects of outward FDI in the Balkans on the Italian production systems in terms of local knowledge and economic development patterns.

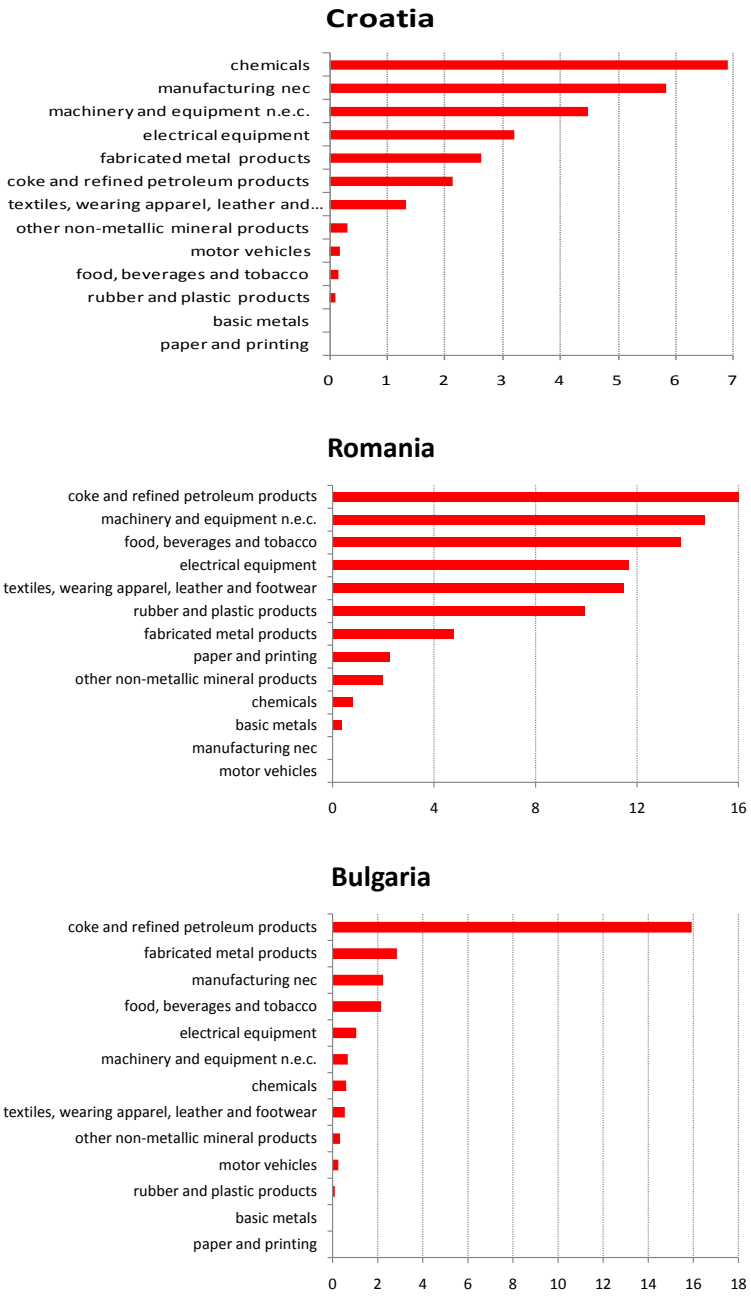
Appendix

Table A1: Main characteristics of Italian manufacturing FDI towards Balkan countries

Country	Main manufacturing industries in which Italian firms have been investing during the last decade
Croatia	• Food • Refined petroleum and gas production (Agip, Edison) • Textiles-clothing: Benetton (delocalization), Calzedonia (greenfield investment), extensive international subcontracting of Italian SMEs, particularly from the Veneto region • Furniture • Machinery • High-tech industries (electronics, high-tech glasses)
Bosnia-Herzegovina	• Textiles and Clothing (Golden Lady, Pompea) • Footwear (Olip Italia) • Furniture and wood processing (Top Sedia, Corà Spa) • Fabricated metal products • Industrial Park in Brčko (Veneto Region and entrepreneurs association)—2008
Serbia	• Clothing and footwear (outward processing trade) • Automotive industry: Fiat investment in 2008 in partnership with the Serbian government
Albania	• Clothing (International outsourcing, main source region: Lombardia) • Footwear (International outsourcing, main source region: Puglia)
Macedonia	• Footwear (outward processing mode of production, REGIA (upper-stitching production, 2000 workers) • Metal products (DUFERCO)
Romania	• High diversification of Italian manufacturing FDI, especially during the period 2007–09 • Not just traditional industries • Presence of both SME and large companies
Bulgaria	

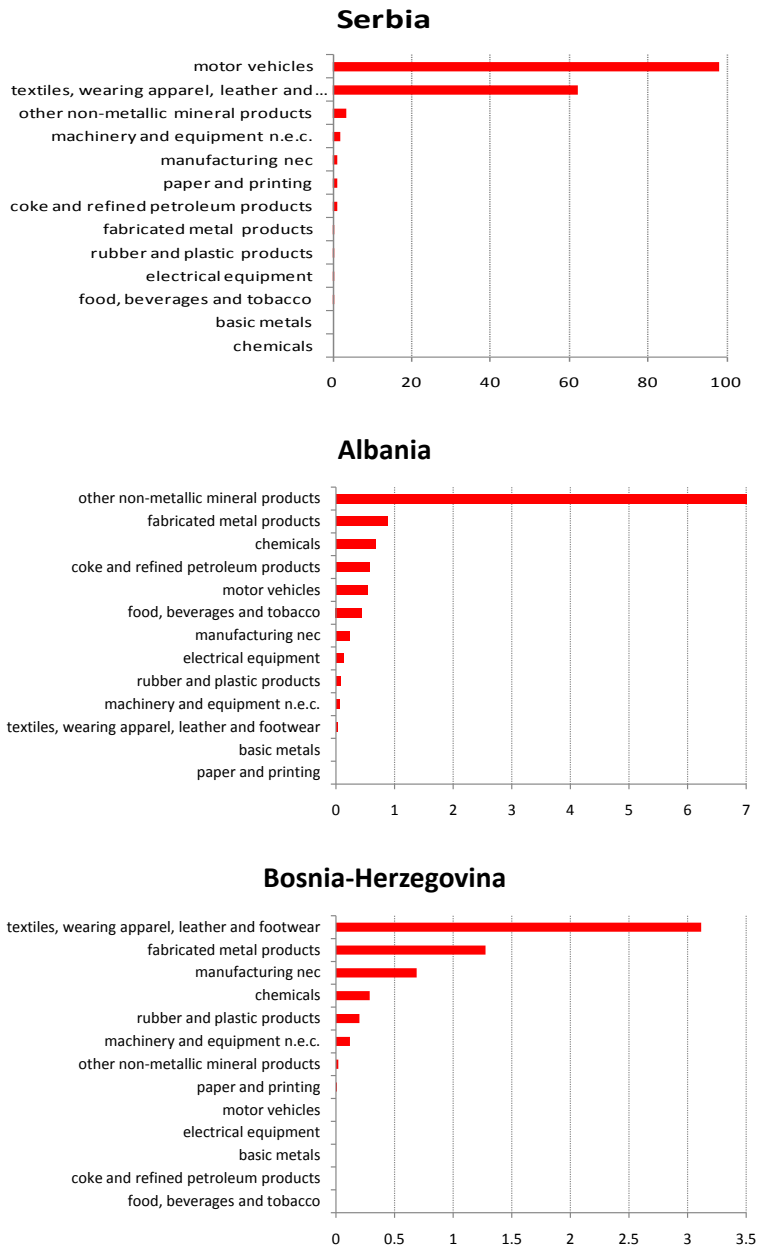
Source: ICE country reports, Simest (2010)

Figure A1: Italian manufacturing FDI towards selected Balkan countries, 2007–2009 (Millions of euro)



Source: External Trade Statistical Division, Bank of Italy

Figure A1: continued



Source: External Trade Statistical Division, Bank of Italy

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