

Global Business Forum/Hannover Messe

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Italy: an attractive source for high technology subcontracting

Ladies and gentlemen, I want first of all to thank Global Business Forum and the Hannover Fair Authority for the opportunity they offered to me, to introduce the Italian subcontracting industry.

We are talking about subcontracting, which denotes a co-operation form in which “the buyer purchases from a supplier, the “subcontractor”, products or services which are part of or are specific for his finished products.

Considering the above, we can now state a principle that stays at the base of the entire subcontracting co-operation: all subcontractors contribute to the building-up of the competitiveness of their customers’ final product. (...*steering all choices*)

A first basic question arises: what reasons stay at the base of the thrust towards subcontracting, a thrust which industrial production has been going and still is going through?

Here are the answers:

- a lack of production capacity involving subcontracted items
- the need of reacting to a sharp increasing demand
- lack of know-how on subcontracted items or services

the second point has achieved top importance, as a mean to allow a manufacturer to produce more finished products than his available production capacity would allow.

This last point has also achieved more and more importance in connection with the many cases in which the buyer requires subcontracted items outside his production culture. Think of a manufacturer of mechanical machinery who needs plastic components. He knows nothing about plastics transformation: he better finds a subcontractor who

a) has a solid experience in working with plastic materials and

b) as a consequence thereof is in the position of offering competitive prices.

In this case, an extremely common one, the buyer, covering his requirements through an experienced supplier, can take advantage of the latter's experience and know how, as well as of his competitiveness, without undertaking a new investment which would carry him to an unknown production field, with all the connected risks. We are therefore in the presence of an example of a consistent rationalization of production, reached through subdividing work on the base of specific capabilities. In a case like this, the subcontractor is assuming the role of a strategical partner of the buyer, and is directly participating in his competitiveness.

Through this preliminary remarks, we can identify the three basic criteria through which a potential buyer is supposed to evaluate his potential suppliers:

- production capacity
- technological level
- know-how to share

and can start discussing whether and to which extent Italy can offer them

The title of this speech qualifies Italy as an attractive source of subcontracting: let me try to explain the bases of this statement.

The image of Italy as a subcontractor: let's start remarking that in the European context, Italy is generally seen more as a supply source of subcontracted goods rather than as a buyer.

A first visible proof of this, is that usually the Italian subcontractors are the largest group of exhibitors in most European subcontracting exhibitions, let it be the Hannover Fair, or MIDEST in Paris or ELMIA in Sweden or the other many more. In a subcontracting exhibition in Italy, a German exhibitor, or generally an exhibitor from outside Italy, is as rare as gold dust. Furthermore, Italy has no exhibition fairs faintly comparable to this one or to any other of the ones I just mentioned. Should somebody ask to me to recommend a fair with a good display of Italian subcontracting, I would probably address him here to Hannover. This doesn't mean that the international subcontracting world is denying Italy its attention: high level subcontractors have strongly established themselves in the Country. It is however a matter of fact that the Italian subcontracting industry relies on some competitive advantages, mostly deriving from the industrial tissue of the many different,

well defined production areas, which developed over the years their dedicated know-how in well defined production fields.

Steps of the Italian subcontracting industry's development

In any industrial area in the world, for understandable reasons, subcontracting starts and progresses in its development at the same time as all other industrial activities.

Its development progresses generally with the arising of the above basic reasons for which the manufacturers turn to subcontracting.

But let's do our best not to lose sight of the core subject.

In Italy as elsewhere, the development of any industrial production has favoured the establishment of productions and activities supporting it, which later evolved independently. In order to fully understand this point, we are not supposed to think macro, which in this case means at national or regional or even at district level, but within the limited horizon of a single production unit. Quite often we'll find out that after some time, the derived production can even show only a faint connection with the main one. A clear example of this is offered by the city where I live and work. In the nineteenth century, it saw the establishment of textile industries supported by Swiss investors. The development of it triggered the development of service for textile machines which, in turn, evolved into the production of spare parts for the same, which was followed by the production of complete textile machines, which is today a strong point of the economy of the city, while textile industry is long dead. In turn, the textile machines production fostered the development of the precision mechanics subcontracting industry which is at present one of the top assets of our region, and which supplies its products to a lot of production branches worldwide.

But to utterly schematize the development process of subcontracting anywhere, we should consider the two basic ages of industry: a first one, oriented towards a vertical organization of production - from the iron and coal mine to the nail - and a second one, the one in which we live, in which it is obvious for the manufacturers to get parts of their final products from external suppliers, the subcontractors. This last configuration can involve "some" parts, but even ALL OF the parts necessary for assembling the final product. I could mention to you some examples, but I'm sure that you also know some. By the way, this extreme sort of industrial production based on subcontracting was very helpful for the great production effort during World War Two. More generally speaking, the manufacturers have fully accepted the principle that in order to enhance their competitiveness, they must connect

with a network or a chain of proper subcontractors. Better to think of a chain, as it implies the synergy and integration of more partners.

Subcontracting in today's Italy

It is customary, discussing an economical reality, to put on the table the usual bunch of statistical information and numbers, which should give a clear picture of the size of it. This has proved to be close to impossible for subcontracting, for the many-sided characters of the subcontracting industries: most of them actually have also their own finished products, and it's beyond anybody's possibility to establish which share of the turnover or how many employees are involved with subcontracting.

A study carried on in the course of 2007 evaluated the size of subcontracting in Italy to about 56.000 units, with at least 640.000 employees and a total turnover of approximately 60 Billion Euros.

Several Italian Institutions are monitoring the subcontracting activity, mostly with the aim to evaluate its importance on a regional or provincial level (Italy is subdivided in 20 regions and around 100 provinces: we must also consider however, that some Italian regions have a population and an economy comparable to some entire European states or large German Länder, while others are much smaller) A basic point has been stated without discussion: most of the Italian subcontractors are small or very small enterprises. Less than 4 % have more than 100 employees.

The geographical distribution is by itself interesting: we could affirm that the geographical density of subcontractors is decreasing from north to south, but even this is an unreliable simplification, for a reason which we will soon explain. It goes by itself, that the more traditionally industrialized regions can rely on a large and well established subcontracting, originally born to supply the local industry. This applies first of all to pioneer regions of north-western Italy, Piedmont and Lombardy. We have however other regions in Italy, which went through a much younger process of industrialization, mostly in the second half of the twentieth century. In some of these regions you won't find large and/or long established industries, the requirements of which could have started the development process of subcontracting. Some of these regions, which went through a later industrial development, have consciously played the relatively safe card of SMEs and of subcontracting.

It is not even possible to identify any definite kind of specialisation in the Italian regions: with a lot of overlapping, every area is more or less endeavouring to manufacture everything.

Some structural features and problems of the Italian subcontracting industry and their solution.

We have pointed out that the Italian subcontracting industry consists mostly of small units. Back in the seventies and eighties, the Italian industry coined a slogan which sounded “small is beautiful”. It was supported by the bare reality of the European industrial fabric, where SMEs were and most probably still are by far the greatest employer in Europe and the supporting pillar of European economy. This slogan, “small is beautiful”, can be perfectly true, up to the point at which it denotes a handicap, which happens when one understands that his Company is too small to reach the targets he is aiming to.

When one or the main of such targets consists in achieving a position on one or more export markets, the small size of a Company can prove a big obstacle. Let’s discuss this in detail.

We have affirmed that one of the trump cards of Italian subcontracting is its high or even top high technological level. Here arises immediately a question: is it possible that “small” or even “very small” production units can rely on top level technology? In the Italian case the answer is “yes”. And it is also true, that competitiveness, quality and positive evaluation of the products is at the base of the good reputation which the Italian subcontractors generally enjoy. But it is in the contacts between buyers and small subcontractors that some (small) difficulties can arise. Most often they restrict themselves to communication problems. As most of the leaders of SMEs have a technical background, the development of their Companies as well as the technical level of the same and the fact that all the investments are directed towards technology must be ascribed to their technical culture. But as a consequence thereof other capacities in the Company are less (or later) developed, or at least not enough to cope with the technical possibilities of the Company. A common case: communication in German or in English is difficult. The reason why is that a foreign correspondent “cost like an advanced CNC machine tool” and therefore “the turnover with Germany is not enough to justify the cost of a foreign correspondent”, and on the other side “the turnover with Germany does not take off because the Company is not in the position to communicate in German”. Add to this that reliable German or English Speaking people are far from being easy to find.

But let us temporarily leave these considerations aside, and let's come back to the technological level, in which I have identified the base of competitiveness. I know personally a good number of Italian subcontractors. By many of them, beautiful, modern, advanced technology is a real personal hobby. They live in a continuous competition for who, at least at local level, has the most advanced pieces of machinery. Some of them buy the best cars of the world not to drive them but to keep them as collector's items. This is an extreme aspect of a refined technical culture, which leads them to a continuous personal presence for flawless workmanship and quality.

We may say, that a good share of even the smallest Italian subcontractors can cope with the highest requirements in quality and reliability.

A further influential point, is that the majority of Italian SMEs, and therefore the majority of subcontractors, are family enterprises. This can sometimes strongly influence their development. As most of the same were established in the last decades, they are still in the hands of the "first generation". This is posing a harsh question on what will happen with the handing over to the next generation, and in several cases is an obstacle to a thrust towards development, especially if the representatives of the next generation do not show interest for their father's achievements.

Propension to operate on the export markets

This interest and the deriving trends and developments must be seen in the general frame of the capability of each Company to react to the challenges which came from the market over the years. What kind of challenges? Heavy, almost recurrent economical depression, local or worldwide, investing the entire economy or just one or few productions branches, or involving just the main or even the "only" customer of a shortsighted subcontractor. Let me say shortly that only the Companies and/or the Company leaders who have been able to properly react to such challenges have been rewarded by the development and consolidation of their business. The selection has been in many cases ruthless: many conservatively run units have been confined to a limbo of lower class small, no-consequence subcontractors, or have simply disappeared. But the good ones transformed the problems and the challenges into good opportunities and prospered. The youngest companies could avail themselves of the experience of some long established ones. Altogether, the entire branch went through a harsh selection, one of the results of which is that now the real "go-getters" are not only strongly export oriented, but are also following clear and sound politics in the choice and number of their customers, with a special

attention to the risks deriving from the dependence from too few or even from one single customer. I lived an instructing event in our Chamber of Commerce, when a local subcontractor stated that he was currently supplying around 250 customers operating in 40 production branches. The statement arose the reaction of an American journalist, who asked him how he could work without focusing on anything. The answer was very simple: I subdivide the risk, and I can work without the risk of becoming dependent from one branch, one land, one customer. To cut it short, moving to the international markets is most probably the most effective form of diversification.

Connections and co-operation with the customer

In the early days of subcontracting, the buyers required the subcontractors to supply them mostly with parts: made to measure, made according to the buyer's drawings and specifications, or made to the buyers specifications but designed by the subcontractors, but always and still "parts".

From upper level subcontractors, today's buyers all over the world don't require any longer just parts, but mostly aggregates and subassemblies, which in many cases also require the co-operation of more subcontractors. And the subcontractors have developed over the years the capability to cope with this new purchasing policy of their customers. This new philosophy of subcontracting has fully invested Italy, and, by-passing the traditional local individualism and wariness among SMEs which makes any other Company a competitor and/or an enemy or both, many Italian SMEs have joined forces, technologies and know-how to be able to produce even the most challenging aggregates.

It has been ascertained, in the universe of Italian subcontractors, that at least 50% of them entertain direct connections with their customers, both on the domestic market and abroad, but 28 % of them have no contacts whatsoever with the final customer, and supply their products only to other subcontractors, at a higher level in the production chain to which they belong.

To achieve a conclusion, we must first realize that it will never be possible to put a brand on an entire universe of subcontracting enterprises: we will always meet a sort of Gaussian distribution of the more or less developed companies, but the emerging Italian subcontracting companies, those which have invested and seriously worked to develop their activity out of the boundaries of their local districts, and, needless to say, the ones which you can meet at the Hannover fair rank among them, the emerging Italian subcontractors, I mean, have developed a full capability of assisting their customers in the

entire spectrum of modern subcontracting, putting at their disposal the four basic elements which identify and mark out a subcontractor as a possible strategical partner: production capacity, technology, capacity of assisting with the development, design and industrialization of the product, together with the quality, flexibility, accuracy and punctuality which are regarded as obvious and implicit in any industrial cooperation. Becoming a strategical partner is the top aim of any subcontractor, as it is the first and the main assurance of a solid and long lasting cooperation.

Running the business connections

A further point to discuss, and which must be added to the several which we have already dealt with, regards how the Italian subcontractors behave themselves in the dealings and in the cooperation with their international customers, a fact that can often build up the good understanding between a customer and a supplier.

We must admit, that foreign customers, foreign as seen from Italy, of course, which have not established any co-operation with Italian partners yet, may sometimes have questions to ask before going ahead with their dealings.

Furthermore, there could be an initial, sometimes cultural brake against replacing a well known subcontractor, maybe a strategical one, with a new unknown one, even if for some reason replacing the old one is unavoidable. It's understandable that the usual doubts can arise: we don't know them – are they reliable? – are they going to be punctual – will they give what they promise in quality? Will the shipment and transportation work properly? Will strikes or other force majeure prevent them from producing and thus in turn menace our production? A leap in the dark!

The only possible comment is that such fears are mostly groundless. Times has passed, and much experience has been piled on by the Italian Companies. They have learnt how they are expected to move, and have tooled up to deal in the basic foreign languages, let's say German, English and French. As per of the above questions, all of them can be answered through a visit intended to evaluate personally and directly the available production facilities and the quality control procedures. And most of them are proud to show their factories to anybody.

A further source of confidence is given by the international quality certifications, ISO or other, which have been obtained practically by all the highly ranked subcontractors, especially those operating abroad. They have fully assimilated the philosophy that quality and reliability are not costs, but assets.

The above carries to a sort of reciprocal question: are the Italian subcontractors generally satisfied with their co-operation with their foreign partners?

The answer is again a positive one, for a certain number of reasons. The same kind of co-operation that the European customers claim from their Italian suppliers they are ready to grant to them, and this applies also to some operational procedures which have achieved a top importance in modern industrial production: just a simple case: just in time supply of parts requires a solid and reliable production planning.

We are proud to state that most of the co-operation agreements between Italian subcontractors and foreign partners are long lasting ones, quite often enjoying a further development through a progressive enlargement of the line of supplied parts. All this means that the experience with Italian subcontractors is generally regarded from both sides as a positive one.

A few words on the propension to investment

The positive trend in the development of Italian subcontracting in the last 3 – 4 years have strongly influenced the already generally lively attitude of the Italian subcontractors on investment.

At present, around 67 % of the Italian subcontractors are carrying on consistent investment plans.

In general, the investments are not intended to achieve a pure increase of the production capacity, but mainly to increase productivity and the general technical and economical performance of the Companies, with an utmost attention to quality and work safety. What you can hear from the subcontractors are statements like “thank to this new machines my production capacity has increased x % without the need of engaging new workers” , or “through this new machinery I spare x persons compared to the earlier technology” - “earlier”, not “older”, and you can bet that it was not old at all.

We can assume, of course, that the propension to investment is connected to the size of the Company, but this is not fully true in Italy and with Italian subcontractors, who have definitely accepted the point that in order to secure their future they cannot afford to be one single day back with the technological progress. And even the smallest units don't draw back: they are conscious, that in a Country where labour cost is close to the world's top level, competitiveness can only be based on technology and know-how.

To conclude: looking for a subcontractor in Italy

At this point, a question could come up. "How can a potential buyer identify the Italian subcontractors which could best cover his requirements?"

To establish and foster direct contacts, the system of the Italian Chambers of Industry and Commerce is playing a primary role. Every Italian Province has a Chamber. All the Chambers are ready to help, both directly or through their special departments established for the very purpose of promoting subcontracting and of supporting its development both at home and abroad. Other organizations work under the authority of the Industry association, at national, regional or provincial level. Here, at the Hannover fair, a good number of Italian subcontractors are displaying their products and promoting their services in joint, common stands with the co-ordination of the above institutions.

Furthermore, every communication connected to subcontracting runs generally on the web, starting from enquiries including the transmission of drawings. Several organizations, starting from those belonging to the Chambers of Industry and Commerce network, have put on line large directories of subcontractors, with detailed profiles of all the entered companies.

I will close telling to you that I am here at the Hannover Fair with the subcontractors from Friuli Venezia Giulia, the north-east corner of Italy between Austria, Slovenia and the sea: I will be glad to welcome you at our stand in hall 4, with a representative selection of the products of the region's subcontracting industry.

I trust I have convinced you that Italy can be an interesting source of high technology subcontracting, and invite you to check it yourselves personally.

I am here if you have any questions, and
thank you very much for your kind attention.