BusinessWeek

April 14, 1980 • $1.50

INTEL
The microprocessor champ gambles on another leap forward
Page 92

CORPORATE STRATEGIES
- **American Motors**
- **Volkswagen of America**

Page 80

SUPPLEMENT
The new smart cameras
Page 136

What really keeps the Italian economy afloat

Millions of individuals work, produce, and save, despite everything we can invent to impede, stop, or discourage them.

—Luigi Einaudi, former President of Italy

Italy's small industrial entrepreneurs and their hard-working labor force are the engines that drive the country's troubled economy—and this is even more valid today than when the late Einaudi recognized their vital role more than two decades ago. While productivity and profits lag at Fiat, the Montedison group, and other corporate giants plagued by restrictive labor laws, strikes, and the rigidities of sprawling organizations, tens of thousands of small and medium-sized Italian companies are thriving—and adapting to the rapid changes in markets at home and abroad.

The outpouring of textiles, shoes, furniture, ceramics, and specialized machinery from small plants clustered around the industrial cities and towns of northern and central Italy helped push the Italian economy to a real 5% growth rate last year—the highest in the European Community—despite sluggish output by major industries (chart). And the small industrialists' aggressive selling in foreign markets accounted for a big share of the $5.2 billion balance-of-payments surplus on current account that Italy posted last year in the face of an $11.9 billion oil import bill. Such enterprise has made small and medium-sized businesses "the marching wing of Italian industry," according to Rodolfo Banfi, former chief economist at Banca Commerciale Italiana and now chairman of Mediocredito Centrale, a financial institution that specializes in lending to small companies.

'A cemetery of companies'

Among the marchers is Clodo Righi, president of shirt manufacturer Confezioni Frarica (1979 sales: $20 million), who keeps the framed quotation from the late Einaudi on a wall of his office in the northern Italian city of Carpi. When cheap Far Eastern shirts invaded Frarica's markets at home and abroad three years ago, Righi adapted quickly by shifting to a higher-quality product line and kept sales from his two family-owned plants expanding at an average 20% annually for the past two years. Righi worries about Italy's inflation, currently rising at a 20% annual rate, and about the business slump that is forecast to start later this year. But small and medium-sized companies like Frarica, Righi predicts, will fare much better than large ones. "Our overhead is lower, and everyone in the family works in the company," he says, citing a total of eight family members who are active employees. "And we are flexible, very flexible."

By contrast, Italy's big corporations are so hamstrung by government regulations, union contracts, and escalating costs that they have little flexibility. Companies with more than 15 workers are practically prohibited from laying off or firing workers, and those with more than 200 must get union approval for investment decisions. Automatic wage escalator provisions translate inflation directly into steep labor cost increases. Italy's militant labor unions, moreover, concentrate their demands on big companies such as Fiat, which had a $62 million loss on auto sales last year, thanks to 9 million man-hours of strike time that cost the company 200,000 car units. Operations of the Montedison group ran in the red, as did Pirelli's in tire-making, while state-controlled companies such as Italsider and Alfa Romeo, which make up a big segment of the economy, are now threatened with bankruptcy unless the government bails them out.

The plight of the industrial Gullivers has so alarmed the labor unions that they are quietly loosening some strands in the web of restraints that has the companies virtually paralyzed. Fiat says it is being allowed to shift workers from one production line to another, thus achieving a mobility in its work force that unions had previously denied. And unions have agreed to some overtime, especially at the plant where Fiat's new Panda is manufactured. Even the Communists are talking, although not yet

Carlo Cerchioli

DISA's Buscaroli: A hands-on managerial approach combined with flexible marketing.

doing much, about the need to make industry more productive. "It is an illusion to think we can have greater social productivity in a country which becomes a cemetery of companies," Luciano Lama, head of the Communist-led CGIL union, said recently. The government, for its part, is offering low-interest loans to companies that must restructure their operations because of high energy costs and is encouraging the formation of bank consortiums to rescue stricken companies.

It may take years, however, for such measures to restore big industry to financial health and competitiveness. In the meantime, thousands of small and medium-sized companies have evolved strategies to free themselves from some union and government regulations. Ironically, their solution, in many cases, is to reverse the centuries-old trend in industry toward economies of scale by spinning off operations small enough to escape the rigors of employment laws and by farming out production to suppliers and service companies—a device that holds down capital requirements and overhead and helps to stabilize production costs because the suppliers work to fixed-price contracts. In addition, the small entrepreneurs are able to move faster than large companies to exploit market opportunities, while the close personal contact between owner-managers and employees enables them to escape much of the labor strife that wracks major industries.

The result has been an explosion in the number of companies employing from 20 to 500 workers to 110,000—an increase of 35% over the past decade—according to an estimate by the Confederation of Small & Medium-sized Companies. And this figure does not include small factories with fewer than 20 workers, which are manned, in many cases, by moonlighters working at second and even third jobs. Some of these workers and companies are part of Italy's largely untaxed "underground" economy, which—if it were accounted for—might add 35% to the country's gross national product of $281 billion.

While few small and medium-sized companies are on the leading edge of technology, they are quick to spot market openings and create products to fill them. That is how Bancor s.r.l., a Milan company set up four years ago by Luigi Alessandrini and the Piazza brothers, Gianluigi and Attilio, developed a photocopier for use in processing the *cambiali*, or promissory notes, that Italian banks handle in large volume. Olivetti, where Alessandrini formerly was a product manager, considered the market too small. He therefore enlisted the Piazzas, who managed a family concern that specialized in printing equipment, to set up Bancor as a new venture to manufacture a machine that automatically photocopies the notes, tabulates data from them, and stores the information in a memory cartridge. Sales last year totaled $6 million, half in Italy and half abroad—mostly in Spain and Greece.

Subsequently, Bancor's three owners organized another small company, Sirima, with Alessandrini's brother as a fourth partner, to sell office supplies, and it is working on a new product, a sorter, that could spawn yet another company. "The trouble with most small companies is finding a second product to sell," says Alessandrini. "That is why we are working on the sorter."

International markets

The spinoffs and Bancor's production pattern show how small industry manages to flourish amid restrictions that are choking Italy's big companies. Bancor buys 50% of its components from other small suppliers and does the final wiring and assembly in a shop behind its headquarters. The system holds down capital outlays and stabilizes costs under fixed contracts with suppliers. It has another crucial advantage: Neither Bancor nor Sirima, which conducts a $2.5 million annual business, has more than 15 workers, so they are free of curbs on hiring and firing. Says Alessandrini: "We will never have more than 15 workers in one company."

Such fragmentation of operations has virtually eliminated large, integrated companies in Italy's woollen and cotton textile industries, furniture making, and some machinery manufacturing. Instead, in textiles, for instance, the makers of end products farm out dyeing, finishing, weaving, and other processes to a host of small companies. As a result, Biella, a wool center in the Piedmont area with a population of 55,000, is estimated to have one industrialist for every 40 inhabitants. And Prato, a city of 300,000 near Florence that has been making cloth since the 13th century, is a beehive of small companies supplying products and services to wool textile concerns that market $2 billion worth of products annually, half abroad. Similar fragmentation has occurred in the knitwear industry centered around Carpi, in Sassuolo's ceramics industry, and among the shoe manufacturers of Vigevano and the Marche region.

Other small industries have carved out niches in world markets by means of their flexibility in matching products—and production runs—to the needs of special markets and individual customers. That is the strategy of 71-year-old Guido Buscaroli, owner of DISA, a company near Milan that sells $7 million worth of diesel injection parts and oleodynamic equipment annually, mostly in Italy and the U. S. When patents on diesel engines run out, Buscaroli makes spare parts for them, including parts for General Motors, Cummins, and Caterpillar equipment. Buscaroli's technical staff and shop foremen also work out methods—from designs provided by customers—for manufacturing high-preci-

How small companies prop up Italy's economy

In expanding industries, small companies set the pace for fast growth and rising exports ...

Industry	Share of total industry sales by small companies* (Percent)	Increase in industry output, 1979 vs. 1978 (Percent)	Increase in industry exports, 1979 vs. 1978 (Percent)
Leather	59%	13%	20%
Furniture	57	17	39
Shoes	49	10	38
Food processing	38	8	53
Textiles	32	14	15
Clothing	28	14	27

...but where giants dominate, both production and exports lag

Industry	Share of total industry sales by large companies (Percent)	Increase in industry output, 1979 vs. 1978 (Percent)	Increase in industry exports, 1979 vs. 1978 (Percent)
Synthetic fibers	98%	1%	0%
Autos	95	2	8
Chemicals	92	7	9
Iron & steel	88	1	−2

*Small companies employing 20 to 99 workers

Data: Central Statistical Institute, Confindustria

sion oleodynamic equipment, which DISA then produces to order. "We can make 500 pieces and make money," Buscaroli says. "Big companies find this too small for them."

The hands-on managerial approach that such specialized operations require is one of the strengths of Italy's small companies, as are the incentives and satisfactions that managers derive from ownership. "Once in a while someone walks in from Australia or South Africa, throws a part on my desk, and says, 'You made this, I can tell from the precision of the machining,'" Buscaroli says. "That is what satisfies me." Adds Giorgio Frascaroli, president of an earthmoving equipment maker in Modena: "In a big company, when a manager makes a wrong decision, he loses somebody else's money. When I make a mistake I lose my own, so I care about the company." Indeed, Italy's small industrialists plow a big share of the money they earn back into their businesses—one reason why the country's investment rate, equivalent to 22% of gross national product, is among the world's highest. Both Bancor and DISA finance expansion internally by reinvesting profits, and both are debt-free.


Carlo Cerchioli

Bancor's Alessandrini and the Piazza brothers: Products that spin off new companies and a limit of 15 workers per company.

Significantly, small and medium-sized companies in Italy are also relatively free of the serious troubles with labor unions and the absenteeism that plague big plants. That is partly because small-scale operations avoid the boredom of huge assembly lines and give workers more pride in their product. But it is also because the small industrialists are able to keep in touch with their workers. "Most of these people grew up in my company," Buscaroli says of his 180 employees. "We all know each other, and they see me working as hard as they do. If they have a grievance, they come to me right away, and we resolve it."

Small companies also pay 10% to 15% higher wages than big manufacturers for comparable jobs—partly because their workers tend to be more skilled and partly because other small concerns are anxious to hire skilled people away. Offsetting the higher wages are the efficiencies that small companies gain from their flexibility in scheduling work. Most are able to get their employees to work Saturdays or overtime—which big corporations usually cannot do. And in rural areas, where many small companies are located, workers' continuing ties to the land provide an element of labor stability that is lacking in cities such as Milan, Turin, and Rome, where crowding and inadequate services have created severe social tensions.

To offset the disadvantage of their limited marketing resources, Italy's small companies band together in cooperatives and consortiums to sell their products abroad. A group of three machine toolmakers in the Modena area, for example, jointly market big transfer machines, containing products of each, overseas. Small companies in Prato and Vigevano that have moved into machinery manufacturing have set up consortiums to sell complete woolen textile and shoemaking factories abroad. Formation of such combines is aided by the clannishness of small industrialists, who swap ideas "over coffee and even at the soccer match," says Antonio Lucchesi, head of yarn manufacturer Industria Italiana Filati and president of the Prato Industrial Assn. Prato's small industrialists also bypass the banking system to lend each other money—and defaults are unknown.

Trouble ahead?

Despite such individual and collective strengths, there are signs that rising costs and increasingly fierce international competition may start taking a toll even among these resilient small industrialists. The buffeting suffered by knitwear maker Gianni Salvaterra, although he has since recouped, may be a sample of what is in store. Salvaterra's company, Smarty, used to turn out inexpensive sweaters in large volume, as did other firms in Carpi, the knitwear capital of Italy. Then cheap products from the Far East invaded Smarty's market, 90% of it in the U. S., and sales fell from the $10 million annual level of the early 1970s to $4 million in 1975. Like Righi of Confezioni Frarica, Salvaterra responded by shifting to more expensive products such as mohair and cashmere sweaters and three-piece women's suits. He also hired a designer and started a casual-wear boutique line. "I no longer aimed at quantity, but quality," he says, and he managed to rebuild Smarty's sales to nearly $10 million last year—but at the sacrifice of much of the big U. S. market, which now takes only 20% of the company's output. Most is now sold in Europe, where consumers are accustomed to higher prices for quality products.

The question is whether such marketing agility will enable these companies to conquer the still more competitive environment of the decade ahead. "Small and medium-sized companies operate mostly in traditional industries—textiles, clothing, shoes, furniture—that less developed countries are moving into with cheaper labor and lower costs," says an economist at Confindustria, the Italian industrial association. "We can upgrade our products in those industries for a few years, but then the market will be taken over by the LDCs." Economist Romano Prodi, a former Minister of Industry, agrees. "Electronics is the wave of the future, and our smaller companies just do not have the knowhow," he says.

That is why the willingness of labor unions, the government, and the political parties to create a more favorable environment for big industry (BW-Nov. 12, 1979) is crucial to Italy's future. Nevertheless, small companies will continue to play an important part in that future, insists Aldo Cambi, a Florentine banker who specializes in financing such companies. "At the beginning of the 1970s we had a similar debate about whether the small and medium-sized companies could buoy the economy through the decade—and they did," he recalls. "Now we are asking whether they can do so in the 1980s. They are very imaginative—do not count them out." ■