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Connections and Competences in the Governance of the Value Chain. How Industrial Countries Keep their Competitive Power.¹

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The aim of our paper is to analyze the governance of the value chain operating in the traditional sectors of textile, clothing and shoe, pointing particularly to delocalization through sub-contracting. The case studied deals with Veneto firm relations with Romania that have profoundly affected the structure of production in both territories in the last decade.

After having described and “quantified” the internationalization process of Veneto districts towards Romania we turn to discuss possible consequences of this process both on the district of origin and on the recipient area. We highlight, through the concepts of linkages and of competences how the productive internationalization process may determine a progressive weakening of the network of linkages that characterize the native district, and discuss the main obstacles to a successful transfer of know-how and technologies in the host system.

From this discussion emerge the vision of some policy measures to amplify possible positive effects and counter negative consequences of the fragmentation of production in the native and in the host country.

Key words: Internationalisation, Clusters, Industrial Districts, Delocalisation, Organization of Production

JEL classification: F23, L22, L23, L67

The global economy has significantly changed during the past decades, and these changes are rooted in how the global economy is organized and governed. The development strategies of countries today are affected to an unprecedented degree by how industries are organized and the transformations in the industrial organization affect not only the flows of goods and services across national borders, but also the processes for how countries move up (or down) in the international system (Gereffi, 2005,160).

Production delocalization toward low wage countries is part of the strategy being followed with growing intensity by industrial countries to meet competition from one another. The erosion of the competitive advantage in international markets is being faced with a mixed strategy of product upgrading and productivity increase at home and labour cost reduction abroad, through international fragmentation of production (Finger, 1975, 1977). Through such means industrial countries in continental Europe such as Germany and Italy have been able to keep their world market share or at least to prevent a drastic fall. These suggest the need for a new framework to understand both patterns of competition among international firms and the development prospects of countries that are trying to upgrade their position in diverse global industries.

These suggest the need for a new framework to understand both patterns of competition among international firms and the development prospects of countries that are trying to upgrade their position in diverse global industries. The topic of the global economy is inherently interdisciplinary. Scholars in this field thus have to master “the art of trespassing” (Hirschman 1981) and frequently cross the frontiers of established academic disciplines. In developing our theoretical framework along interdisciplinary lines we use two main analytical tools. First, the concept of forward and backward linkages that was devised by Hirschman in the 50s in his analysing the problems of economic development (Hirschman, 1968). Second, the concept of “competences” that emerged from the debate on industrial districts in Italy during the seventies (Brusco 1992, Becattini and Rullani 1996), derived from the tacit knowledge ideas of Polany (Polany, 1957) and the more recent elaborations of Nonaka and Takeuchi (1995).

The new aspects of modern world trade relevant to our discussion are (1) the rise of intraindustry and intraproduct trade in intermediate inputs; (2) the ability of producers to “slice up the value chain,” in Krugman’s (1995) phrase, by breaking a production process into many geographically separated steps; and (3) the emergence of a global production networks framework that highlights how these shifts have altered governance structures and the distribution of gains in the global economy (Gereffi, 2005, 166).

This paper discusses the new organization of production taking as an example the recent delocalization flows that has linked the Veneto, a manufacturing region of the Italian North East, and Rumania and that make some Italian commentators speak of the Timisoara region as the Veneto 9th province, because of the magnitude, the pervasiveness and the rapidity of such flows (in the American mirror, see Berger and Locke, 2001).

Veneto is characterized by a presence of important brand-holding final firms in footwear and clothing, and a large network of small subcontractors that work on their behalf; we focus on these two sectors in order to discuss the change in the competitive advantage of the region and the reorganization of the production chain.

Many of the final firms, in the last decade, have experienced a strong production delocalization process towards low wage countries, mainly in Eastern Europe. Veneto enterprises have outsourced production abroad both by making direct investments and also through international subcontracting relationships. The first, direct investment, strategy has been adopted by many large enterprises that have acquired or established factories abroad, thereby moving away from participation in subcontracting relationships (quasi-market) to hierarchical relationships. This is the case, for example, of Geox, an important Veneto footwear producer which in 1998 estab-

lished its own large factory in Timisoara, Rumania, after changing from a previous strategy of using many sub-contractors. The second strategy, international sub-contracting, is quantitatively more relevant than FDI, and is adopted mainly by small Veneto final firms that have substituted local with foreign subcontractors. The relations that takes place between the contractor and the supplier – market, dependence, modular, relational and hierarchical, according to the value chain literature – are influenced by product complexity, ability to codify the information concerning production, level of competences and market power (Gereffi et al., 2005).

Table 1 shows that Rumania is the most important country in Eastern Europe for Italian direct investments, in 2004. 88 Italian enterprises had manufacturing plants in Rumania employing 22.000 workers².

Table 1.
Italian Foreign Direct Investments in Eastern Europe. 2004

| | Partecipated* | | | Partecipated > 50% | | |
|-----------------------|---------------|-----------|----------|--------------------|-----------|----------|
| | Firms | Employees | Turnover | Firms | Employees | Turnover |
| | n. | n. | mil. € | % | % | % |
| Rumania | 729 | 55.806 | 2.614,6 | 79,4 | 89,1 | 81,1 |
| Russia | 157 | 53.347 | 2.050,0 | 66,2 | 24,2 | 41,6 |
| Poland | 391 | 37.743 | 5.522,3 | 84,4 | 88,3 | 93,6 |
| Hungary | 181 | 15.500 | 2.565,9 | 85,6 | 77,5 | 63,5 |
| Ceckia | 151 | 15.328 | 2.850,4 | 80,8 | 86,5 | 43,7 |
| Bulgaria | 166 | 9.723 | 456,5 | 87,3 | 93,6 | 87,6 |
| Slovackia | 123 | 8.610 | 508,8 | 83,7 | 66,9 | 69,6 |
| Albania | 157 | 7.905 | 500,4 | 88,5 | 87,1 | 87,9 |
| Slovenia | 101 | 5.743 | 579,2 | 77,2 | 77,7 | 82,0 |
| Ucraina | 66 | 5.018 | 422,5 | 80,3 | 84,0 | 83,1 |
| Serbia and Montenegro | 97 | 3.732 | 537,1 | 85,6 | 31,5 | 90,7 |
| Croatia | 75 | 2.885 | 601,8 | 90,7 | 85,7 | 94,2 |
| Other countries | 331 | 6.989 | 817 | 84,0 | 64,5 | 79,1 |
| Total | 2.725 | 228.329 | 20.025,9 | 82,1 | 70,0 | 73,6 |

Source: CNEL, R&P and Politecnico di Milano. The data base refers to ltd firms in mining, energy, manufacturing, services , participated by more than 10% of their share capital.

² Capital flows into Rumania have been fully liberalized since the early nineties. Direct investments in Rumania are now 4,7% of gross national income (The Economist, 2006). Investments, in large part, depend on the outsourcing processes of large manufacturing (Continental, Michelin, Daewoo, Renault, Sumitomo, Yazaki, Panasonic) and distribution firms (Metro, Carrefour, Billa, Unilever) and the main European banks (“Survey on the Entrepreneurial Veneto Presence in Rumania”). In 1996, the biggest 25 Rumanian manufacturing factories controlled by foreign firms had a turnover of around 2000 million dollars. This amounts to 6% of the total turnover produced by private Rumanian firms.

These figures explain only a part of the production delocalization phenomenon. Foreign direct investment do not take into account the sub-contacting flows directly dealt by Italian multinational firms that are very important in apparel and footwear industries³.

The production delocalization process can be measured according to three indicators: the amount of foreign direct investments, the number of firms set up in other countries owned by foreign entrepreneurs, and the trade flows of finished and semi-finished products under the coordination and control of multinational firms⁴.

Some large Italian final firms have encouraged their domestic sub-contractors to move abroad in order to continue, at lower labour cost, the previous business relationships that they had in their country. Nowadays there are many small firms managed by Italian entrepreneurs living in Rumania that work as subcontractors for multinational firm.

During the '90, the import of manufacturing Italian firms have concerned mainly Romania, but in 2004 China has become the most important supplier for Italy in apparel and the second, after Rumania, in footwear production. Veneto remains, still nowadays, highly dependent from Rumanian imports. On the total Italian imports from Romania in apparel and footwear production, Veneto keeps in 2005 a share respectively of 33% and 52%.

Out of 18.000 Italian firms registered in 2005 in Rumania, 3.900 have a "Veneto origin", i.e. 22% of the total (respectively 12.000 and 2000 in 2002: Regione Veneto, 2006⁵). For this reason, Timisoara-Arad, a strongly industrialized area that has known a fast development during the last ten years, is highly interdependent with Veneto.

Forty-five of the Veneto firms, that have moved production abroad, are in Rumania, 17% in China; Poland, Bulgaria and Tunisia follow at distance (Capitalia, 2005, table D73).

The advantage of Romania in attracting foreign investments and subcontracting orders is due to the lowest cost of labour among East European countries, that is 8% of the EU-15 average (Table 2). Because of the inferior productivity and various organizational costs connected to the production made abroad this gap reduces to 50-60%, according to Graziani spec-

³ On the effect of FDI see Navaretti, Falzoni, Turrini (1999) and Navaretti, Bruno, Castellani, Falzoni (2002). On the necessity to assess the delocalization flows magnitude through adequate study of commodity flows, see among others Yeats (1998) and Kaminsky and Ng (2000).

⁴ According to Dicken (2004) "a transnational company is a firms which has the power to co-ordinate and control operations in more than one country, even if does not own them".

⁵ These numbers include possible non active units that have not been cancelled.

ulations (1998, 2001). This kind of comparison requires, a lot of caution. In the case of Romania the apparel firms are totally unbranded and specialised in sub-contracting production, while in a developed country, such as Italy, many firms sell branded products and perform design and marketing activities. The lower per capita value added of Rumanian firms is not a result of low production efficiency – as implied in the Ceeps-WIIW report (2005, tab.4) – but is the effect of “slicing the value chain” keeping the core business in the advanced economies and outsourcing, under enhanced price pressure from the stagnant clothing market, an increasing share of non core manufacturing activities at very low profit (sewing, ironing, packing and wrapping).

Table 2.
Apparel manufacturing. Yearly labour cost in € per employee.

| | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | % of the cost EU-15 in 2001 | average yearly variation 1997-02 |
|----------|------|------|------|------|-------|-------|-----------------------------|----------------------------------|
| Cekia | 3436 | 3732 | 3817 | 4424 | 4843 | 5758 | 21.7 | 0,11 |
| Hungary | 3417 | 3414 | 3608 | 3939 | 4382 | 5236 | 19.7 | 0,09 |
| Lituania | 2175 | 2413 | 2712 | 3016 | 3018 | - | 13.5 | 0,09* |
| Poland | 3270 | 3489 | 4247 | 4067 | 4683 | 4533 | 21.0 | 0,07 |
| Slovakia | 2898 | 3318 | 2805 | 3296 | 3427 | 3640 | 15.4 | 0,05 |
| Slovenia | 8095 | 8694 | 9000 | 9480 | 10023 | 10372 | 45.0 | 0,05 |
| Bulgaria | 860 | 1114 | 1185 | 1267 | 1345 | 1418 | 6.0 | 0,11 |
| Rumania | 1214 | 1478 | 1419 | 1715 | 1806 | 1831 | 8.1 | 0,09 |
| EU-15 | - | - | - | - | 22282 | - | - | - |

Source: CEPS-WIIW (2005, table 5a)

*1997-2001

I. The global Value Chain Management: Linkages and Competences.

I.1. Industrial Relations between Italy and Rumania.

In Italy, mainly in the industrial districts, many transactions take place among a high number of small enterprises. In particular, Veneto has a very high entrepreneurial density and the labour market is close to full employment, with high activity rates. The higher the number of people acting in the market, the easier and the quicker the knowledge diffusion - about production techniques, raw material suppliers, demand trends and consumer tastes - and the more that confidence and trust are diffused among economic agents.

In a backward country like Rumania, that has emerged 15 years after the fall of Ceausescu and the associated communist regime –apart from the Buchares-Iflow and the Western regions - many markets still do not exist or are at an initial stage, and are not regularly utilised. Knowledge about technology and the international market is scarce and incomplete. The legacy of a planned economy, together with a long-lasting period of economic uncertainty with slow growth occurring between 1990 and 1996, and a still partial privatization process, have not allowed the market to fully work. Furthermore, managerial competences are still scarce and inertia comes from a lack of self-organization and from a strong aversion to risk⁶. A manager of an ex-state large clothing factory, Rapsodia, told us:

“During the Communist regime the Rumanian clothing industry had 46 large plants with an average number of workers ranging from 2000 to 5000, and the country was split into three centrally organized districts. Production planning was centralized in Bucharest and all the products were produced on stock. Two collections were launched each year and presented at a fair in Bucharest, that was visited by foreign operators. Rumanian producers did not receive any foreign currency and all the production and distribution decisions were centrally planned. A bureaucratic commission fixed the sale prices without having direct information about production costs.

In 1989, all the Russian market was lost and the domestic one shrank because of a fall in employment and in real wages. A dramatic socio-economic situation ensued that began to reverse only at the end of the nineties. In such a distressed situation it proved very difficult for Rumanian enterprises to enter the capitalist market and continue the few relations they had established with Western firms, mainly because lack of financial support and of any marketing experience. Many Rumanian clothing firms began working as sub-contractors for Western companies.

Table 3 shows as few years after the fall of Ceausescu, Rumania had almost completely lost the Soviet market, after Germany and Italy started to delocalize in that country part of their apparel and footwear production. Nowadays, a large part of Rumanian apparel industry are dedicated to the transformation of raw materials and semi-finished goods, mostly imported from Western Europe and re-exported towards these same countries at a more advanced level of manufacturing. This phenomenon is shown by the

⁶ According to the International labour office between 1990 and 2000 the industrial employment and the wages of the workers (in real terms) have reduced (Laborsta in www.ilo.org). On the contrary, the Rumanian Central Statistical Office asserts that wages, during the nineties, registered a modest increase (Insee, various years). Anyway, as the strong employment reduction is not to be questioned, the employees aggregate purchasing power has certainly declined.

high Rumanian apparel and footwear export value toward these countries and by the correlate import quantity of textile and leather (table 3, in bold). Only the products destined to the Russia market are manufactured using yarn, fabric and leather bought directly by Rumanian firms in the domestic or international markets.

The trade data show also the growing importance of Italy (Baldone, Sdogati, Tajoli 2001, 2002; Graziani, 1998, 2001) that has replaced Germany as first trade partner of Romania. This latter country has strengthened its own Rumanian presence in other higher capital intensive industries, such as chemistry, electro-mechanic, optical and means of transport⁷.

Table 3.
Rumanian Trade for selected commodities and markets (values in million \$)

| 1991 | Imports | | | | Exports | | | |
|----------------|---------|---------------|---------|---------|---------|---------------|---------|---------|
| | World | Italy | Germany | Ex-Urss | World | Italy | Germany | Ex-Urss |
| Textile | 91,1 | 5,8 | 8,4 | 4,5 | 99,5 | 7,9 | 11,9 | 22,2 |
| Apparel | 52,3 | 6,1 | 2,6 | 0,0 | 296,3 | 29,7 | 72,2 | 96,2 |
| Tanned leather | 4,7 | 0,4 | 1,0 | 0,0 | 0,9 | 0,0 | 0,4 | 0,0 |
| Footwear | 44,4 | 5,6 | 10,3 | 0,0 | 85,0 | 7,6 | 9,2 | 34,2 |
| 2004 | | | | | | | | |
| Textile | 3.329,2 | 1147,0 | 464,0 | 7,2 | 562,1 | 146,0 | 117,0 | 0,0 |
| Apparel | 645,5 | 249,0 | 33,6 | 0,0 | 4417,3 | 1592,0 | 1027,0 | 6,9 |
| Tanned leather | 762,1 | 600,0 | 29,6 | 0,0 | 80,7 | 31,8 | 12,3 | 0,0 |
| Footwear | 387,8 | 271,1 | 7,0 | 0,0 | 1.512,5 | 1092,7 | 89,6 | 0,0 |

Fonte: <http://unstats.un.org/unsd/comtrade>.

Large production delocalisation of Veneto firms toward Rumania is explained by the geographical proximity of the two territories and by the particular structure and specialization of apparel industry. Veneto has a larger presence of firms producing standardized products in large batches (i.e. jeans and sport garments) than the other Italian regions, such as, for example, Emilia Romagna, where female fashion and high quality garments make delocalization abroad difficult. Such different productive structures explain the different historical patterns in the organization of production followed by the two regions (Crestanello 1996), although, under the pressure of demand for more fashionable and customized products, Veneto is now rapidly moving towards producing less standard items and the differences with Emilia Romagna tend to reduce.

⁷ On the German position in respect to Eastern Europe, see Pellegrin (1997).

In Rumania thousand of Veneto entrepreneurs and technicians control, both through foreign affiliates and local sub-contracting firms, respect for quality standards and delivery times for items produced to designs sent by home enterprises⁸. Rumania plays a particular role in attracting foreign firms because of the presence of abundant low-cost labour specialised in clothing and footwear production.

1.2. Links and Competences.

Forward and backward linkages have been appropriately defined by Hirschman (1968, p. 48-50). Linkages are the result of a series of investment decisions, each dependent upon the other, taking place in the course of a process of economic development. Backward linkages take place when the final demand stimulates the production of inputs (semi-finished products, raw materials and machinery) necessary to the productive process, while forward linkages develop starting from the production of an input to include other downstream products. Backward and forward linkages develop where there are prospects for profit for local entrepreneurs, and also where there are abilities to make products that can be sold on the market. Competences must also develop for the efficient production of machineries and of raw material requested by the growing industry. The role of domestic competences, neglected initially by Hirschman (Brusco, Paba, 1992, p. 234), plays a crucial role in translating opportunities generated by the growth of demand into entrepreneurial actions⁹.

Important production links, that existed in the past in the Rumanian economy, need to be rebuilt. This is the case of the textiles industry that was important before 1989 but which was later largely abandoned because of the rapid technological obsolescence of its plants and the difficulty to produce the high quality yarns and fabrics required by the sophisticated Western market¹⁰. Many Rumanian textile firms have closed down and some have converted to clothing production, such as, for example, as has

⁸ In Rumania the number of firms controlled by Italian entrepreneurs or working on behalf of Italian multinational enterprises are estimated to be round 10.000-12.000.

⁹ In the 50's the economists approach to the problems of economic development was centred on demand factors, while the supply capacity to respond to new entrepreneurial opportunities was neglected. Hirschman is aware of the importance of supply but decides not to focus on it. He explains that a more radical break with the paradigm came through suggestions that a determining influence on growth may issue from the production side of the economy. Sociologists like Bert Hoselitz and others took this point of view when they focused on the conditions for the emergence of entrepreneurship. "As an economist I preferred to simply assume an insufficiency of entrepreneurial motivation and then to systematically search for such constellations of productive forces as would move private pr public decision makers to "do something" through special pressures" (1977, p. 70).

¹⁰ A firm's textiles sample collection is generally developed over a very wide range of fashion products differentiated by the blend of material used, the colour, the printing, etc.

happened in the case of the enterprise Rapsodia. The EU moreover has promoted a custom agreement that made it easy to import raw materials and semi-finished products. In the nineties, imports from the EU were subject to OPT (outward processing trade¹¹) provision and then in 2000 were completely liberalized, while finished products were exported to the Efta countries without duties. Through such means, the EU countries have protected their textile industries from the competition of important producers, such as Turkey, whose exports to Rumania are penalised by import tariffs¹².

Therefore, after the fall of the Ceacescu regime, not only were investments needed to renew machinery and textile production, but foreign investors could import into Rumania all the necessary raw materials produced elsewhere, enjoying low tariffs¹³. Exactly the same process occurred in the tanning industries with the closure, during the nineties, of nearly all the Rumanian firms¹⁴.

Table 4 shows the strong employment and production reductions that occurred in the Rumanian manufacturing industries between 1990 and 2001. The restructuring process has affected the textiles and the footwear industries much more than apparel industry - which has maintained stable employment. Between 1990 and 2001 these three industries altogether lost 316.000 jobs. The aggregate data nonetheless do not fully reflect the heavy restructuring processes, with the closure of many State companies and radical changes in labour and production organization.

¹¹ The outward processing procedure constitutes a customs procedure under which goods are exported from the customs territory of a specified country for the purpose of their processing within a designated period of time and subsequent re-importation of compensating products manufactured of the exported goods with their complete or partial exemption from customs duties and taxes.

¹² Hirschman notices that imports play a creative role in the process of development but that the "exporting countries can make political and economic pressure in order to prevent or delay the loss of important markets" (1968, p. 151).

¹³ See Chakravarthi Raghavan da Ginevra 7 Dec, 1995 in www.sunsonline.org/trade/process/followup/1995/12060095.htm. See also UN's Economic Commission for Europe (ECE), Economic Bulletin, v. 47, 1995.

¹⁴ A case of non-existent or negative consumption linkages. As Hirschman had noticed: "it is now widely recognised that during the first phase of export expansion in the countries of the periphery an important effect is, not the creation of new industries to satisfy rising consumer demand, but the destruction of established handicraft and artisan activities...as new import of consumer goods compete successfully against them" (1977, p. 72-73)

Table 4.
Production Value and Employment in Rumania. Selected Industrial Sectors.
Turnover in Billions of Lei, at Current Prices.

| | Production | | | | Employees | | | |
|--------------|------------|---------|----------|---------------|-----------|---------|----------|---------------|
| | Textile | Apparel | Footwear | Manufacturing | Textile | Apparel | Footwear | Manufacturing |
| 1990 | 78 | 40 | 20 | 1.076 | 414.000 | 258.000 | 127.000 | 3.452.000 |
| | 7% | 4% | 2% | 100 | 12% | 7% | 4% | 100 |
| 1998 | 8.880 | 9.224 | 4.108 | 252.570 | 128.000 | 239.000 | 76.000 | 1.907.000 |
| | 4% | 4% | 2% | 100 | 6% | 17% | 5% | 100 |
| 2001 | 23.454 | 37.966 | 14.420 | 749.760 | 98.000 | 290.000 | 98.000 | 1.590.000 |
| | 3% | 5% | 2% | 100 | 6% | 18% | 6% | 100 |
| Var. '90-'01 | - | - | - | - | -316.000 | 32.000 | -29.000 | 1.862.000 |

Source: Insse (2003), 3.1.11, and 9.9. 2001 is the last year available for production data.

(*) Without building, energy and mining.

Today, however, profit opportunities in textiles production in Rumania have increased, clearly as a consequence of downstream demand increases, and foreign investors showing interest in starting up textile production at the local level. For example, a firm in Botosani, controlled by the French Cantex Group, has set up a new local factory to supply high quality fabric. The same has happened in Zalau with Samtex - owned by the Italian Campagnolo group - that now produces and dyes good quality jersey partially used directly, but mainly sold to Italian firms that subcontract sport-clothing in Rumania. Since fabric supply is the most important input in the apparel chain, a country that wants to upgrade its position in the value chain needs to develop a proper textile industry. The process – if a process will develop – is just on its infancy and currently, the greater part of textiles is imported from abroad.

Forward linkages take place when a foreign final firm outsources all or part of its production to Rumanian subcontractors, but to-day the largest quantity of thread and textiles is imported from abroad. Furthermore some capital-intensive stages of the clothing production process, such as for example washing and printing have a cost in Rumania close to the cost in Italy, but have been recently established in Rumania under the pressure of foreign firms that need to complete in that country their value chain and ship the finished product (already controlled and packed) to Italy. Sometime these firms are established by small Italian entrepreneurs, that following their customers internationalisation process and their suggestions, have transferred abroad their manufacturing activities. This has made possible for Gas, an Italian firm that controls in Rumania an important production factory, and for Benetton, that has an important ready dyed sweater production, to com-

plete abroad the product cycle, ironing and wrapping included. If the Rumanian economy could develop apparel value chain, so that a larger share of the international industrial organization might be supplied by Rumanian firms, this country would acquire a significant competitive advantage in respect to other sub-contractors in Eastern European and North Africa, that are in competition to attract investments from abroad.

At present, in Rumania, the purchase of raw materials and capital goods for the clothing and footwear industry comes from foreign countries while the domestic market only offers some basic inputs, some repair and maintenance activity at the initial stage. Rumania lacks able craftsmen that can quickly intervene in case of a machine breakdown, so that for firms to carry on production they are forced to hold some machines in reserve in order to replace those that are out of use. Moreover, the modest price which the foreign customers pay in Rumania for semi-finished products does not allow local firms to develop an adequate financial capability to amortize the costs of modern machines. The machinery used is in fact older than that in use in the Veneto plants.

How is it that people in charge of the numerous textile plants maintenance, during the Ceausescu regime, at the overthrowing did not constitute a humus where the germs of a small mechanical industry could develop? A director of Samtex s.s. tells us:

During the Regime textile production was self-contained. Samtex had machines for hemp, linen and cotton. 700-800 employees worked in Samtex, but were reduced to 150 just before the privatization. Looms were built in Rumania under Imatex licence. Maintenance of textile plants was regularly made by well equipped internal teams. In fact at the Ceausescu fall the demand for textile yarns had drastically diminished, ex-state firms did not invest in new plants because both of lack of demand and of finance, and while a plant broke down, the looms were not repaired and were substituted by other looms set aside that were not in use. The maintenance teams were the first to be dismantled and many mechanical workers were fired and emigrated.

Lack of demand for maintenance certainly does not explain the backwardness of the Rumanian mechanical industry, that lost in the five years after independence, 50% of its employees, around 300.000 workers, but this story enlighten the role played by the impoverishment of the country manufacturing base in the early 90s, due to the heavy industrial restructuring and large emigration flows of skilled workers.

Forward linkages develop when a foreign firm place an order for all or part of its production to a Rumanian supplier, that is able, subcontracting possi-

bly to other local firms, to perform the required production. In the case of a clothing firm, for example, it means a Rumanian firm supplying, in addition to other upstream production stages such as cutting and sewing, quality control, packing, shipping and logistic operations. In the case of a Rumanian firm receiving from a foreign enterprise a semi-finished product to be processed, forward linkages are still weak. In many of the cases examined, transport services for Italian buyers in Rumania are supplied by Italian firms and even the packing cases are imported through the OPT regime from Italy.

In short, the opportunities for developing, through the delocalisation process, upstream and downstream industries only offer a weak stimulation to the birth of an autonomous domestic entrepreneurship. And it is the lack of technical competences, and also of local managers that, on the one hand, keep high the imports of intermediate products and services, while, on the other hand, leave the potentialities for internal production at a virtual stage, unable at the present to substitute for foreign production¹⁵.

We are speaking about backward and forward linkages that can be established in respect of a product designed by a foreign enterprise to be sold in the export market. The role of the home market in favouring economic development is crucial, as the existence of an effective and perceivable domestic demand renders profit opportunities visible and real- according to Hirschman. In its absence the position of local subcontractors is very weak as they depend on foreign buyers and do not have any autonomy¹⁶. Products demanded in the domestic market are totally unsophisticated and very different, in terms of price and quality, from those sold in the international market. Even the distribution circuit is different¹⁷. Prices are kept low because of the poor population consumption power and the fierce competition of standardised cheap products imported from China and India.

The manager of Filty, a large Rumanian footwear company in Timisoara with 1400 employees that, before the nineties, produced exclusively for the home market and for the Comecon countries and today works almost exclusively as subcontractor on behalf of Western enterprises, asserts:

¹⁵ A high flow of intermediate imports, according to Hirschman, is a clear indicator of the existence of a potential market; consumers and firms that buy the imported goods could purchase similar good were they domestically produced.

¹⁶ See Hirschman (1968). For an East Asia perspective see Ginzburg and Simonazzi (2003) and Akamatsu (1962). Gereff (2005, 171ff.) tells us the fascinating history on the upgrading of East Asian sub-contractors in the apparel sector to original, high quality, brand name manufacturing.

¹⁷ Consumption goods imported by Western European countries do not compete with production for the domestic market and the two productive structures, that of Western European countries and that of Balkan Europe, remain very different.

“Our company produces for the home market approximately 5% of its production and sells it at a price so low that it pays only the cost of labour; we make this production only in periods of productive capacity underutilization”

Production planning and commercialization of clothing or footwear products requires various types of skills: information on market trends, acquaintance with distribution, brand promotion, and the capacity to devise a price policy able to support product quality and style. This is knowledge that the enterprises learn in the first place through selling on the home market. But this process of learning is still far away in a country such as Rumania that has, together with Bulgaria, one of the poorest East European consumption markets. In this country, the disposable income per capita is in fact 40% of the Polish income, 37% and 18% of the Hungarian and Slovenian income¹⁸ and it has not changed in the course of the nineties. The distribution of employee wages has become more unequal through time with a rapid increase in the number of employees that belong to the lower deciles (Insee, 2001, ch. 9 and 3).

A rising income induces in turn a more sophisticated demand and this influences the supply. In other words, a sophisticated consumer creates a sophisticated producer¹⁹. And this not only through the obvious demand stimulation, but because inside a company, as an entrepreneur of Vigevano transplanted in Rumania has explained to us, the workers that in that country are poor consumers do not care for the quality of the product, do not give attention to the details, while an Italian worker, who is a sophisticated consumer, surely would do.

The demand factor is therefore important, but it can also happen that a backward region does not have at its disposal all the skills necessary to undertake production opportunities. A high import of intermediate products indicates the existence of a potential market: consumers or import firms could buy them on the domestic market if someone was able to produce them at an attractive price.

“Imports scout the local market and shape it; the existence of an import flow fades away uncertainty, reduces selling costs and shortens the time gap to begin domestic production. The moment in which to start production is determined by the minimum size of the enterprise and by cost and localization factors” (Brusco and Paba, 19, 233).

¹⁸ The conjectured wage increase due to the delocalization process, if ever materialized in a labour market with a high rate of disguised unemployment, would not affect significantly the average Rumanian wage which is still one quarter of the average wage in Hungary or Poland

¹⁹ As noted by Porter, the level and quality of domestic demand is one of the factors in the competitive advantage of an industry. As the author says *“demanding buyers make pressure upon domestic firms to satisfy high quality product and service standards”* (Porter, 1990, p.117).

In spite of the presence of a potential demand, some productive sequences will not take place if the required induced activities need skills and technologies that are lacking in that country. This is particularly likely to be the case when the product, because of its degree of complexity and refinement, demands the employment of modern expensive technologies, whose maintenance requires foreign technicians²⁰, and when the semi-finished components and raw materials cannot be found on the local market and can be easily imported. In many cases the competences increase is limited to a better trade acquaintance by the importers, and involves the development of little familiarity with advanced production techniques.

In the case of Rumania, the process of production de-localization from Italy and other countries of Europe has made possible a local production of sophisticated products. All this has happened thanks to the presence in that country of numerous enterprises and/or Italian technicians. A transfer of tacit competences occurs through the movement from Italy to Rumania of technicians and entrepreneurs who transmit their knowledge, resolving practical problems, correcting errors, and putting into work the best production techniques.

Subcontracting interact with local competences in a different way from foreign investments. Subcontracting stimulates local managerial resources to organize themselves, to relate to foreign customers, to produce sophisticated products, to respect rigid delivery times and solve cost management problems. Although sometime the result is not efficient and foreign customers are not satisfied.

Italian entrepreneurs judgement about the performance of the Rumanian worker is very varied. Italian entrepreneurs that have their own firm in Rumania since several years and that have trained Rumanian workers are mostly satisfied, while entrepreneurs that rely on local subcontractors point to all organisation dysfunctions proper of Rumanian managed firms. An unsatisfactory situation that reflects in unstable relations and almost never develop into a stable form of collaboration.

²⁰ The lack of adequate maintenance is considered by Hirschman (1969, p.170) "one of the most problematic problems for any developing country". Hirschman continues saying that once the problem has been picked up, the most direct way out of it is to launch production processes that do not require maintenance, or on the opposite, that require a very rigorous and compulsory maintenance programme, that once put into practice, can play a positive role in the process of economic development (p. 172). This seems not to be the Rumanian case, although a positive development along these lines is not to be ruled out completely.

I.2. The importance of the delocalization process from Veneto to Rumania.

A straight assessment of delocalization magnitude is provided by the value of Veneto clothing and footwear imports from Rumania and the corresponding number of jobs created there.

According to the Rumanian custom office 98% of total apparel and 95% of shoes exported from Rumania towards all countries were produced as a result of OPT trade, in 2003. Let us assume that all imports of the Veneto in apparel and footwear are totally under the control of manufacturing firms. It means in 2005 a value respectively of 439 and 476 million of euros²¹, included raw materials and subcontracting value added. In Rumanian apparel firms, raw materials are on average 75% of the value of the final product, so that the value added produced in Rumania is 85 million of euros. This corresponds to 25.000 jobs, assuming an average turnover value per employee of 3500 euros. In footwear factories, raw materials represent a larger quota of the final value and the corresponding jobs are 26.000 (table 5).

Table 5.

Jobs devoted to manufacture Veneto flows in Rumania and equivalent jobs in Veneto. Apparel and footwear. Year 2002.

| | | Apparel/ knitwear | Footwear |
|---|------------|----------------------|----------|
| Veneto Imports from Rumania | Millions € | 439 | 464 |
| Rumanian Subcontractor: Raw materials/Turnover | % | 75 | 80 |
| Veneto Subcontractor: Raw materials/Turnover | % | 50 | 50 |
| Turnover/employee in Rumanian subcontractors | € | 3.500 | 3.500 |
| Turnover/employee in Veneto subcontractors | € | 20.000 | 20.000 |
| Raw materials exported from Veneto to Rumania in OPT | Millions € | 329 | 371 |
| Rumanian subcontractors value added | Millions € | 110 | 93 |
| Value added in Veneto necessary to transform OPT exported raw materials | Millions € | 329 | 371 |
| Jobs in Rumania connected with OPT trade | n. | 31.357 | 26.514 |
| Equivalent jobs in Veneto | n. | 16.462 | 18.560 |

Source: Inse, Statistical Yearbook, 2003, ch 12. and www.coe-web.istat.it.

If the same raw materials and accessories exported in Rumania, were manufactured directly in Veneto, jobs would be different because of the differ-

²¹ We have previously explained why Italian statistics undervalue the OPT flows. Italian imports in apparel and shoes in 2002 amounted to 1.121 and 951 million € , but only 196 and 223 were OPT flows according to the Italian Central Statistical Office. Rumanian statistics place the exported values at 1.277 and 923 million € and OPT trade, all together, at 928 million €.

ent productivity in the two countries. Raw materials represent roughly 50% of the turnover value in Veneto subcontracting firms. Nowadays the employment in subcontracting apparel firms of Veneto is estimated to be around 31.000 (Crestanello, 2006). So only the employees that work in Romania on behalf of the Veneto final firms represent more than the 50% of the workers who are in Veneto. The average value added for a Veneto subcontractor is on average 20.000 € and the corresponding jobs in Italy, needed to make the same amount of production moved abroad, would be 16.000 for apparel and 18.000 for footwear. There is of course no guarantee whatsoever that without the advantages deriving from delocalization in terms of lower prices, the same products and the relative jobs would have been available in Veneto. But the estimate provides an idea of the impact of delocalisation phenomenon on the employment both in Veneto and in Rumania²².

II: Dynamic Value Chain Analysis: Three Sector Cases.

In this section we analyse how the global value chain has evolved in the Italian footwear and clothing industry through some case-studies of firms that have delocalised their production into Romania, through direct investments or subcontracting relationships.

II.1. Direct Investment: Geox spa.

Geox is a large international footwear producer, whose head office is located in the district of Montebelluna (near Treviso). Nowadays, Geox production is almost completely made abroad; all sport shoes are produced in the Far East; and 80% of leather 'classic' shoes (the main product of Geox) are manufactured abroad, in Slovenia, in a Geox factory employing 300 workers and, also, particularly, in a recent Rumanian plant (in Timisoara) that houses 2.800 workers. All the production made abroad is imported into Italy. Geox does not have sales points in Rumania; neither does it use the domestic market in order to place faulty shoes²³.

The main problem in delocalising production abroad was the transference of tacit competences from the Italian home firm to the foreign subsidiaries located in Timisoara. Before the fall of the Ceausescu regime, going back to the Austro-Hungarian empire, Rumania had a flourishing footwear production, mainly concentrated in large firms such as Filty and Gubam, that

²² The authors provide a second estimate based on the data of turnover, export value and employment provided by Rumania central statistical office in 2002 and get very close numbers. See Crestanello and Tattara, 2005, table 7.

²³ The practice is prevented by the strict application of the OPT import clause.

until the eighties employed several thousand workers. Nowadays, only Filty has survived, halving its employment to 1400 workers. The Geox plant therefore has been established in a rich context of footwear competences where qualified workers can be easily found or trained. Today, only 12 Italian technicians work in the Geox Rumanian plant (4% of the total labour force) and all of them have a technical high profile (all the other workers are Rumanian). Geox is interested in increasing the professional skill of its workers by using wage incentives tied to productivity. The most skilled workers belonging to a first selected group (20-25% of the total) receive more than double the average salary of all the workers. This practice is not appreciated by the Rumanian Trade Unions that consider it as a way to split the workers' cohesion (in Geox, as in almost all the foreign firms, there are no trade union representatives).

The Rumanian plant is completely integrated with the Italian head office. The shipment of the prototype and of the technical schedule that is realized in Montebelluna must still be made in Italy. The prototypes are the result of the work of a high-qualified staff (the Montebelluna plant employs 400, divided between designers and staff engaged in quality control and organization, as well as providing outsourced work to other local external qualified technicians and designers). In the home company, part of the staff working on classic shoes prototypes has been recruited in the Marche, that is one of the most important Italian footwear districts, far from Montebelluna and specialised in the production of classic shoes²⁴. The Geox centre supplies the tanned leathers (coming mainly from the two main Italian tanning districts), the polyurethane necessary for the soles production, all the accessories (including the boxes for packing), the sole aluminium moulds and equipments and machinery (mainly Italian). The import of these materials into Rumania is absolutely necessary as there are not yet local firms capable of satisfying this particular demand for production inputs. According to our interviews, only shape cutters for trimming machines are produced by local mechanical firms.

Although the high level of vertical integration based on hierarchical relationships makes the exchange of information and the transfer of semi finished products between Italy and Rumania easier, Geox management acknowledges the existence of problems and inefficiencies arising from managing a design process that is split from production. To overcome the lack of information from feedback from the production process, the Italian management is planning the establishment of a small design department in

²⁴ Geox has another small design centre in the Marche where 25 employees design the models and make the prototypes for its more important fashion collections.

Romania employing local technicians coordinated by an Italian product manager. The Timisoara plant director asserts that:

“Being far away, the information that is generated in the production cycle is lost, there is a break between shoe conception, design and its production realization and the attempt to establish an industrial design centre (modellieria) in Rumania is a rational decision to reduce such a break in the tacit knowledge transmission process”

Nearly all knowledge linkages (technical information, knowledge, raw material supplies) with external enterprises (advisers, designers) are concentrated around the Montebelluna head company; footwear machinery and raw material suppliers are almost all Italians. In Rumania, Geox uses only 6-7 footwear subcontractors. These firms are used, in addition to the internal production capacity, to satisfy the peak demands (usually in May-July) and for producing more fashionable products in shorter runs (mainly female shoes), that require high competence and ability. Half of the production outsourced in Romania by Geox goes to firms managed by Rumanian entrepreneurs and the other half to enterprises managed by Italians. Geox helps its own subcontractors by providing them with tanned leather and accessories, the necessary machines and in one case granting the use of its property.

Both the Italian and Rumanian sub-contractors are dependent on Geox within a “captive” framework (Gereffi et al, 2004). They receive all the inputs they need in production (design, raw materials and accessories), have small dimensions, except Filthy, a Rumanian firm that works also on behalf of other foreign firms, and their limited size does not allow to enter directly the international market, while the domestic market is secluded - too poor to allow a profitable sale of quality shoes.

II.2. An Italian Sub-contractor: Intercolor

Intercolor is an industrial laundry whose manager Bruno Maule owns also a clothing company that works on behalf of some Veneto firms. Bruno Maule was a Benetton employee from 1976 to 1982. Then he worked for Marzotto and Zanella, two important Veneto firms. In 1985 Maule opened a firm producing clothing, casual trousers and shirts; the Benetton group is one of his customers.

In 1993, only a few years after the fall of the Ceacescu regime, Maule arrived in Rumania. At the beginning, he subcontracted to local enterprises; he did not go personally to Rumania, but employed an intermediary who stayed in that country a couple of days a week, to co-ordinate the local subcontractors and explain to them the technical details for making the products.

“The Italian buyers are very severe and if the subcontractor does not stick to the standards, they send back the entire truck without too many compliments. In 1998, I gave an order to a Rumanian subcontractor that did not deliver the merchandise on time. I risked a complete failure. Then I decided to come here, to Rumania, and control and carry out the production by myself. I loaded a truck in Italy with my old firm machinery and I rented an abandoned shed, hired 12 workers, and started to produce there. I realised that I would have to stay in Rumania and I worked hard. At the beginning, workers were not able to sew properly. Here, people are accustomed to having trousers with legs of different length and out of shape – acceptable for Rumanian consumers but not for the sophisticated European market. I told my workers the importance of details. At first, they did not understand my stubbornness, but in the end I was able to respect the standards of my clients”.

In Rumania, Maule started to produce 200 pairs of trousers daily for Benetton, at that time his only client. Nowadays, he produces, in a flexible way, 5000 items a day with 5 production lines and a part of the production is outsourced to two Rumanian subcontractors. To-day 80% of the Benetton production is manufactured abroad, while in the mid nineties the quota abroad was less than 20%. Benetton keeps in Italy only high quality and quick time-to-market products such as flash collections and re-orders, and the remaining production is outsourced abroad (re-orders in Italy are delivered in a week time)²⁵.

An average production run for Intercolor consists of 4000-5000 items per model²⁶. Bigger runs are an exception, such as when Maule produced in 5 months 100.000 pieces of the same model for Benetton²⁷. The delocalization process has geared the closure of many sub-contractors in Veneto.

At the beginning, Benetton sub-contracted to Maule only the sewing phase; today Intercolor makes a finished product from cutting to packing and sends it to the Hungarian Benetton productive platform, that deals with all East Europe and concentrates 26 over a total of 108 million pieces produced²⁸. The Hungarian plant receives the textiles yarns, cuts and distrib-

²⁵ Italian global buyers, Benetton, Gas, Stefanel, Max Mara etc etc. are never exclusively retailers and brand companies or “companies without factories”, but keep some direct manufacturing activity

²⁶ In Veneto, Benetton subcontractors produce runs of few hundreds of items for a model.

²⁷ In Hungary, Benetton has built a production platform in order to manage the relationships with subcontracting firms in PECO countries that represent a free exchange area with the European Union. The Hungarian plant manages around 50-55 subcontractors and is supplied from Italy with textiles, either produced by Olimpias, the textiles company of Benetton group, or directly imported from other countries outside Eastern Europe. Textiles and accessories are then distributed to all the subcontractors located in Eastern Europe. The production made in those countries are “substituting” the old French, Spanish but mainly Italian production plants. On Benetton (Tattara, 2005).

²⁸ Crestanello and Dalla Libera show how the Vicenza clothing industry lost 20.000 jobs from 1990 to 2000, due to outsourcing into foreign countries (2003, p.27)

utes them to 50 subcontractors, mainly located in Rumania. The textile printing unit is also part of the Benetton Hungarian plant: textile printing is nowadays compulsory in sport-fashion and the lack of textile printing technologies is one of the main bottlenecks in the Rumania value chain.

Benetton Hungary carries out a sample quality control and then sends the products to Italy, where a further control is accomplished and from where the products are delivered all over the world.

Maule works also for some final firms located near Vicenza such as Gas and Diesel. Gas - which has its own factory in the South West of Rumania - has convinced Maule, which has a laundry in Vicenza, to establish a new one in Rumania. The industrial laundry is a high capital-intensive investment, and is managed in Rumania at a cost not much less than the cost that would result if operated in Italy. However, the Italian buyers have interest in carrying out the washing in Rumania in order to complete abroad the downstream production stages that are very labour intensive. For example, jeans decolouration with airbrush, a treatment with abrasive and similar grinding materials, are made piece by piece manually and the cost is very high, till ten time the cost of simple washing²⁹. Maule is now able to complete in Rumania the whole Gas value chain, including, in addition to cutting and sewing stages, also washing and packing. The Timisoara laundry has been rebuilt and much enlarged in 2004 and nowadays works for other foreign firms.

This example make clear the possible contrast between the logic of comparative advantage and that of the value chain: while the logic of comparative advantage helps to explain the slice of the value chain across national borders in order to reap the lower costs (location specific), firm specific advantages explain the decision on what activities and technologies should move along the value-added chain in order to perform efficiently relatively to competitors (firm specific scope economies).

The competences are not lacking, as far as the employees are concerned; the Rumanian labour force is generally well trained and knowledgeable and the presence of Italian technicians is limited to a couple. The Veneto entrepreneur suggests that it is not profitable in Rumania to use productive electronic machines because of the high cost of their maintenance. Local workers are not able to repair them and in the case of a breakdown the firm needs to call technicians from Italy resulting in a long delay. In addition, the higher productivity of these machines does not compensate for their cost when comparison is made with the cheap cost of Rumanian labour. On the

²⁹ In some cases double the cost of a simple washing (in Rumania, from 0.20 € to 2-3 € for each piece).

same vein, the “French Formen”’s manager in Botosani asserts that it is not useful to employ sophisticated machinery with such low cost labour, but the use of modern CAD placement and cutting stations in his factory is required by the high quality of the fabric that must not be wasted.

Maule puts out part of his production to other sub-contracting firms managed by Rumanians. In this way, he promotes the establishment of forward linkages towards domestic firms. He supplies to the subcontractors some machines that his firm does not use any more, in commodatum, and he sends his shop foremen to control production quality.

II.3. A Rumanian Sub-supplier: Rapsodia Conf. s.a.

The previously state-owned companies, Rapsodia, Starmod and Asco, represent well the typology of Rumanian clothing large ex-state enterprises working exclusively for foreign enterprises. These companies are localized in the North-East regions, a poor zone on the Ukrainian border, and employ more than one thousand workers each. The first two are managed by Rumanian managers that own also a small equity quota; Asco is controlled by foreign capital. In the past, these companies had also a textiles production and employed a higher number of workers.

Today, they produce classic male clothes receiving from their buyers all the necessary raw materials and accessories that are not available in Rumania and which are imported under the OPT regime. Asco receives the models via internet and co-operates with its clients in the industrialization of the product while the others receive the paper-pattern. Rapsodia makes the sample collection starting from the design supplied by the buyers. It prepares a real size model and develops the technical schedule that must be discussed and approved by the buyer. In this way, both Asco and Rapsodia have developed good technical competences and performs a series of roles associated with production and export activities behind the pure assembly phase. Rapsodia has recently shifted from Incom, one of its traditional main customers, to Luck (a Mavecom spa brand) and produces casual and classic male good quality clothing. Luck was used to produce in Croatia but has now brought all its delocalised production in Rumania and has transferred 5 Croatian technicians and all its high-tech machines to Rapsodia. Rapsodia has also started a subcontracting agreement for Benetton and this denotes a considerable autonomy and capacity to play with different players and product mixture. Rather different is the situation of Confstar, a apparel firm in Baia Mare, in Maramures, producing low quality apparel for a German brand with a captive relation. The German brand is the unique client, the products are rather low quality (some items are also sold directly in the local market in a shop within the firm premises) and the firm has neither design neither marketing capacity.

Foreign customers of these sub-contractors have their own workers that operate permanently inside the Rumanian factories to verify, at the end of each production line, the product quality. Through such means, Veneto firms have accomplished a remarkable product upgrading in Rumania. However, the director of Italpant, a Veneto enterprise of the Incotex group, previously in Portugal and now transplanted in North East Rumania, asserts that the productivity in his factory is much higher than that existing in his Rumanian subcontracting firms, such as Rapsodia.

This is partially the result of the fact that Italpant personnel policy is based entirely on a piece work wage while Rapsodia pays a monthly fixed wage, but more generally the existence of a productivity divergence in Rumania between enterprises controlled by Italians and enterprises organized directly by Rumanian managers is a widely diffused opinion among various Italian technicians. The knowledge gap is underlined by a request for consulting services to reorganise its production lines by Asco to an Italian technician who manages several Rumanian producers on behalf of a large Italian brand. Low productivity is the result of the way the work is organised, the premises functionality, the vintage and the kind of the machines in use.

Rumanian workers are generally skilled. Rumania has an important 'textiles' polytechnique in Iasi and a large supply of workers (mainly female) specialized in clothing and footwear is available. Italian sub-contractors that came to work in Rumania have taken large advantage of these workers at a low cost. As an example, Italpant has taken on two 'maestre' from Rapsodia in order to establish its production lines and this type of connection is rather frequent. The Italians who in Rumania start up an enterprise, even a small one, can offer higher wages than those paid in the (often larger) factories managed by Rumanians and can compete for attracting the more qualified workers. The basic wage in Moldavia is less than 100€ a month and the additional cost to attract the skilled workers is very small in terms of manufacturing cost. The larger Rumanian factories contribute to creating a qualified labour force that is drawn upon by the foreign small entrepreneurs.

III Summary and Conclusions.

European firms have faced strong competition from businesses in other industrial economies that are commonly outsourcing their production to low wage countries. In order to reduce production costs and keep prices competitive, German, Danish and Swedish firms began outsourcing in the eighties, but massive outsourcing began after the fall of the socialist regimes of East European countries, such as Czechoslovakia, Hungary, Poland, Rumania and Slovakia. Italian clothing and footwear firms started outsourc-

ing later than their German and Nordic competitors, but accelerated after the advantage of the weak lira exchange rate faded away as Italy joined the EMU and the competitive pressure in the international fashion market increased.

In the last decade, in the Veneto clothing and footwear industries, the displacement of local subcontractors, due to the continuation of the de-localization processes, has been significant. Production phases that remain in Veneto are planning, quality control, shipment and distribution, and sometimes the high capital-intensive parts of the production process, such as weaving, dyeing, printing and in few situations automatic computerized placement and cutting. In general, short series with a quick time to market (re-order and flash) are not delocalized and this is also the case of some other products, such as high quality and fashionable clothes or seamless knitting – a high capital intensive process, operated by very modern machines, that is still usefully kept in Veneto (Gomirato, 2004).

Peco represents an alternative to delocalising towards far away countries as China. In the case of Italian shoes and apparel this process has favoured a vertical process disintegration and has maintained in Italy a large quota of the value added. This is the result of the fact that subcontracting still uses textiles and leather of Italian origin, universally recognized to be best in the world in terms of quality and designs. at a cost similar to the cost in Italy, but of the fact that initial (design) and final (logistic and marketing) phases of production are still manufactured in Italy. Today 50% and 25% of all clothing and footwear products imported into Veneto from the low wage countries come in fact from Rumania and workers employed in Rumania on behalf of Veneto enterprises in these industries are estimated at around 55.000, and the estimate for the whole of Italy reaches 120.000. Such a huge delocalization process in apparel and shoes brings to our attention two sets of key questions.

Firstly, in respect of the relation between outsourcing and the development of the outsourcee, we may ask: Can foreign direct investments and international sub-contracting lay the ground for industrial development in the receiving country? Are they able to stimulate efficiently economic activities, complementary to the fields in which delocalization has taken place? Could the growth of domestic competences and the prospects for profits actually activate a robust autonomous growth, in a manner similar to the development process that has taken place in the Italian districts? Secondly, final firms have taken clear advantage from outsourcing abroad and their profit, after delocalization, have systematically increased (Gianelle and Tattara, 2006) but the question regarding the possible impoverishment of the outsourcing territory is nonetheless pertinent. What are the effects of such a rapid outsourcing process in the Veneto regional economy, both in terms of employment decline and loss of competences?

The main constraints in the production delocalization process towards Rumania are the lack of organizational and entrepreneurial resources and technical competences. The first aspect represents the greater bottleneck faced by Rumanian domestic development. For this reason many factories in Rumania that work on behalf of foreign final firms are managed by Italians. Many small entrepreneurs who worked in Veneto as subcontractors decided to move abroad under the pressure of low prices and the threat of losing orders, but also under pressure to fill up some specific bottlenecks that have shown in the chain structure (laundry, fabric printing, automatic cutting etc)

At present, the absence of a domestic market is the key factor that explains the insufficient autonomy of Rumanian producers; risk aversion and the failure to bear responsibility is a characteristic complaint by various Italian entrepreneurs in respect of Rumanian employees (Callegari, 2005). However, Rumanian workers' professional knowledge in these years has grown significantly, the domestic market has developed, (GDP per capita is steadily increasing since 4-5 years) and the range of clothing and footwear products that can now be delocalized into Rumania has widened. The advantages for these Rumanian industries comes from the fact that this country is capable of manufacturing larger production volumes than other East European countries and has benefited from a decennial curve of experience in trade relationships with Western enterprises. Rumania textile-apparel-shoes production currently employs approximately 500.000 workers and the country is one of the bigger textile producers in the world, even if Rumanian enterprises have no direct access to the distribution and consumption networks at the international level and exports are under the control of foreign buyers.

The ability to sell fashion products on the international market requires marketing skills and an acquaintance with the complex fashion circuit, factors that do not find favourable conditions in poor or little sophisticated markets. And there is no reason to think, at a distance of ten years from the first experiences of production delocalization, that Rumania can become in a short while a dangerous competitor for Italy on the world international market.

Rumania competes basically on cost elements with other low wage countries on the subcontracting and unbranded market. However, access to the European Union is considered by many entrepreneurs as one of the elements that could raise labour costs to the level of Hungary or Poland (where labour costs are 4 times higher than in Rumania) due both to an *imitation* process and to an exchange rate stabilization. The history of the 90s' tells us that the de-localization processes directed towards some East European

countries such as Hungary and Poland have, in the following years, been redirected towards Rumania and Bulgaria. A similar situation had already taken place in respect of Portugal when it joined the European Union in 1986. A significant number of French and German firms outsourced into this country their clothing production, but subsequently, when the attractiveness due to the low wages faded away, foreign enterprises redirected their production towards other countries (Thiel, Pires and Dudleston, 2000; Ceps-WIIW, 2005, p. 94).

Of course, the above mentioned countries have changed their production structures and have subsequently hosted new kinds of less labour intensive production, but the crucial question is whether in the future Rumania will witness also a migration of production, under the control of the foreign branded firms, into cheaper labour cost countries or will expand a set of capabilities that allow to pursue an upgrading trajectory in apparel, shoes and other sectors as well? The judgment of Italian entrepreneurs is not unanimous. Some entrepreneurs that govern simple value chains, and whose product does not require very short times to market, seem more prone to move production toward the cheapest wage areas such as Ukraine and Moldova.

Main brands, that outsource large part of the production (from cutting to washing, ironing and packing) and exert a strong control over the production process, are well aware of the economic damages caused by mistakes in production, or by delays in sending the products, and tend to have more trust and stable relationships, that are built over time. These firms acknowledge the advantages of the production experience made in Rumania, that are not equalled in any East European country, and have convinced part of their Veneto sub-contractors to establish new firms there. Supplier loyalty only allows the production of short batches, with a time to market of a few weeks. Nowadays Rumanian firms are able to produce short runs of more qualified products respecting the delivery times requested by the buyers.

Overall, it is acknowledged that in Timisoara and Arad, where the main Italian enterprises are concentrated, a network of external economies has been created consisting of the presence of qualified workers, of services related to production, (washing, dyeing, transport services and accessories, mainly owned by foreigners), and of financial services provided by large foreign banks. The often alleged mobility of the Italian value chains in order to search for more profitable situations, in response to the prospect of a possible wage increase, fading fiscal incentives and new – more restrictive – labour legislation, are perhaps more imaginary than real. It would mean that the increases in skills and competences, of the services, and of the infrastructures have not produced any long-lasting advantage for foreign firms.

Reasonably, it can instead be assumed that Rumania can aspire to upgrade the apparel, shoe value chains and then accommodate some of the logistic functions that today are localized in Italy.

Is the end of the multi-fibre agreement modifying this situation, moving the interest of the Veneto entrepreneurs towards China? In China, India, Bangladesh and other Asian countries, Italian firms outsource full production or quasi-full production (as they retain some control of the raw material supply) - what they call "semi-manufactured" - and move along the de-localization strategies followed by the great brands of European distribution attracted by the volume and low prices of Chinese apparel exports (Crestanello and Dalla Libera, 2003). Usually raw materials and accessories are acquired in the Asian market, where it is possible to find quality and variety³⁰.

East Asian manufacturers have for many years been coordinating the flow of orders from the U.S. and the European buyers to a large numbers of domestic clothing factories (Gereffi, 2002). China, although far away from the European market, with a long transport time, offers a large rapidly developing consumption market. China additionally is endowed with organizational resources, and an innovative capacity that make it a dangerous competitor for Rumania, in its ability to attract foreign investments.

A massive and fast outsourcing of production activities can lead to an impoverishment of old production areas, not only in terms of employment but also of knowledge and skills. The innovations that are at the root of the "Made in Italy" success have been nearly always developed out of a very tight contact between people that design and people that make; are based on product and process innovations that have arisen out of the production process; and which have come out from the daily familiar use of machines and production materials. If the industrial districts lose the production competences do they run the risk of losing also their competitive advantage in designing successful products? Can a favourable scenario be reasonably assumed where Veneto textile-clothing maintains within its own regional border the "more high value added" production stages, such as marketing, design and logistics, and realizes in other countries the more labour intensive and less skill intensive components? The question has a solid ground because some entrepreneurs have demonstrated increasing difficulties in finding in Veneto workers with the necessary skills and knowledge, and this is a clear indication that the local pool of competences, from which the

³⁰ On the East Asia and Mexico supply chain evolution and on the threat posed by China, with its high volumes and low prices, see Gereffi (2005, 173).

enterprises have drawn in the past, is today being diluted.³¹ On the other side, firms need highly qualified people to assist their delocalisation process abroad.

Veneto enterprises de-localizing their production into a foreign country are aware of the danger of losing their technical competences, and some Italian firms, for example Marzotto, keep a part of their production in Italy in order not to lose their capabilities in making innovative products³². In Italy, many firms retain the quality control stage and the staff needed to assist the production transference into other countries.

Some Veneto entrepreneurs that have moved to Rumania, often far from their families, are already discussing the problem of finding their successors. It can be difficult to find other people able to replace them and some entrepreneurs are thinking of selling or closing down their companies. This fact, within a few years, could change the strategic scenario of the Italian enterprises that have established their subcontracting relationships within the network of Italian entrepreneurs living in Rumania.

One of the main bottlenecks is due to a lack of a new layer of Italian young technicians and entrepreneurs to replace in the Eastern countries the current ones. The crisis in Veneto clothing and footwear industries generates much uncertainty and distrust, that renders it unappealing for young people to enter this field of activity. Furthermore, many small entrepreneurs are not prone to invest in plant modernization. In the past, Benetton sub-contractors were known to have renewed or increased the size of their plants, after being assured that their customer, at least for some years, would continue to provide the orders necessary to amortize the investments. Today, on the contrary, those same subcontractors are invited by Benetton to address other customers because the guarantee of stable orders is no longer available³³. As a small entrepreneur from Vicenza in Veneto told us "Today nobody possesses any certainties".

³¹ One needs to speculate if it is profitable today to manage an efficient international division of labour within the same firm and if this process is under way in other countries and in other sectors. This is the case of Singapore that favoured the outsourcing of low value added production into Malaysia and decided to keep the more qualified processes in the domestic territory (R&D, quality control etc.)

³² Just remember the German firm Baumler that outsourced to Styl in Hungary many years ago and ended up by purchasing a majority equity participation in the Hungarian firm in order to be granted access to the latter's know-how (Pellegrin 1999, p. 15)

³³ The share of Benetton production made in Italy has declined from 80% to 30% in the last ten years and is further declining.

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