Small Firms and Big Markets

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Introduction: why one should care about regional economies in a globalized world

In recent years there has been the formation of an extensive literature [1] that argues that Keynesianism demand management is dead. Globalization has made it impossible for states to manage their economies by balancing of supply and demand through macroeconomic policies. The benefits of expansionary policies in a globalized world, it is argued, cannot be contained in one nation and simply invite a slew of imports.[2] This is one aspect of what Bob Jessop calls the "hollowing out" of the nation state; some powers have been lost, and while not all states ever were "keynesian" in the sense that they were primarily concerned with maintenance of demand, the fact remains that now they no longer can be [Jessop, 1994]. This puts at least one nail in the coffin of the nation state as the center of economic management, especially when coupled with other changes that have put the mode of production[3] prominent in the golden years of the post-war boom, fordism, in such trouble.

Fordist mass production is a system that produces extremely large quantities of standardized goods at very low costs by exploiting economies of scale . Fordist firms, as an ideal type, have very long production runs and use inflexible mass production techniques that depend upon ever expanding markets. This mode of production meshed particularly well with macroeconomic demand management policies that helped to ensure these mass markets, but that seems to have broken down in recent years as demand has become unstable and world economic growth more uncertain [Hirst and Thompson, forthcoming]. The exact reasons for the breakdown of mass markets are not entirely clear, but they do seem to be linked to the loss of the state's power[4] to create them, and perhaps also to an inevitable saturation effect. Though this does not mean that all mass markets have disappeared, or that there is no more fordism [Hirst and Zeitlin, 1991], it is the case for enough markets to argue that there now exists a new mode of production that is referred to as being post-fordist.

Jessop describes the post-fordist growth model as being characterized by "flexible production, innovation, scope economies, innovation rents, and more rapidly changing and differentiated patterns of consumption." Jessop argues as well that there has been a new trend towards technological change as the motive force of economic expansion, although he separates this analytically from post-fordism in a way that does not seem useful, as it is really part of the same shift. In this new world dominated by post-fordist production, states who wish to manage their economies must find a new way [Jessop, 1994]. They can no longer simply put together a simple corporatist model using incomes policies to regulate the size of the market as there is too much international spillover. Intervention on the demand side, the post-fordist literature argues, cannot be done in a globalized world. Economic management by the "hollowed out" state must limit itself to intervention on the supply side. The state must undertake policies to try to make its industries more competitive, providing incentives or means to allow its industries to compete through permanent technological innovation and flexibility in production in order to capitalize on the changes in market conditions that every individual state experiences as an exogenous force.[5]

This "supply-side bias" imposed on states from outside has led to a great increase in the attention paid to regional governance, where the "region" is understood as an intermediate level between the national and local levels. The fragmentation of world demand requires a flexibility that the old-style large firm is unable to provide. Instead, the needed flexibility is best provided by networking arrangements in which firms share risks, expertise and perhaps collective services. As will be argued below, such a situation does not imply that a large firm cannot exist -- only that it must adjust -- but it clearly leaves the door considerably more open for systems of small and medium sized firms with flexible cooperative arrangements that can be quickly reorganized as needed. When the supply-side state decides that it wants to undertake an effort to manage its economy, it finds that the national level is somewhat inadequate for the servicing of these flexible systems of firms. Instead, there is a need for the intimate knowledge of the exact and changing needs of the integrated system of firms argued to be central to responding to the changes in the world economy [Piore and Sabel, 1984, Hirst and Thompson, forthcoming]. As the firms are often networked at the regional level, that seems to be the logical level to regulate them.

Another advantage to using the region as the locus of state action for economic management is that it permits a great deal of experimentation. Regional interventions tend to be relatively low cost, largely focused on encouraging public-private partnership, and thus hold considerably less risk than a national level program to "bet" on certain technologies or industries deemed strategic with massive R&D expenditures. There are also, obviously, many more regions than nations, which also renders experimentation and risk-taking more feasible [Hirst and Thompson, forthcoming]. The increase in the need for state intervention at a regional level should not be taken to imply that the nation-state has become irrelevant. It still controls the purse and can often have a good deal of say about what powers are delegated. It also is the only actor that can in any way bargain with the TNCs and MNCs, which, even if much production is carried out through regional systems, remain major players in the world economy. Despite these caveats, there does seem to be an increased demand for, and potential effectiveness of, regional production and governance at that level, particularly when production is organized in networked form. While this is not necessarily the only response of states to their "hollowing out" by the strains of globalization, it is one of them, and the one that will be investigated more deeply in this essay.

The debate about the regionalization of production has not infrequently had as one of its core examples the Italian region of Emilia-Romagna, whose dynamic and particular small-firm driven regional economy was first brought to the attention of scholars in Italy by Arnaldo Bagnasco in his very important 1977 work, Tre Italie: la problematica territoriale dello sviluppo italiano,[6] and later made the subject of international discussion by Piore and Sabel in The Second Industrial Divide [Bagnasco, 1977; Piore and Sabel, 1984]. This region, as well as those surrounding it in central and northeastern Italy in an area referred to by Bagnasco (and others after him) as the third Italy,[7] is well known for the industrial district model of production, based on networked small and medium sized firms.[8] The economies in these regions were extremely successful in the 1970s as well as into the 1980s, and the third Italy seems in some ways to be a textbook example of the potential for a region to carve itself a place in the world economy by capitalizing on the fragmentation of world demand. However, globalization does not only mean the fragmentation of markets and their opening up to small and innovative firms who use hit-and-run tactics, exploiting the cracks caused by rigid mass production techniques. The increased need for technological change, while it can at times serve the small and innovative, can also be exceedingly expensive. Large firms also can use networked production models, with or without a regional base, closing off to the small and medium sized firms some of their competitive advantage. These and other problems provided the third Italy and its famously effective regional governments[9] with some very difficult challenges in the 1980s, challenges that perhaps have some very interesting implications for theorizing about the role for regional economies in a globalizing international economy.

This essay will attempt to analyze the position of the region in the global economy in light of all this attention that it has gotten of late. The focus will be on the third Italy's regional economies, with the hope that an understanding of their development in a period of increased globalization will shed some light on hypotheses such as that of Hirst and Thompson's that "extensions of effective regional economic governance would...secure advanced industrial societies at the local level against at least some effects of increased international openness." Critics may charge that analysis only of small firm economies that have done famously well is sure to give a biased picture of the world situation. There would be some merit in this criticism, if the goal here were to claim that a solution has been found, and that all regions need merely copy Emilia-Romagna. However, this risk will hopefully be circumvented by a different focus, in which the goal will be to elucidate the pressures placed by a globalized world economy even on one of the most dynamic regional economies in the world. While globalization's eating away at national governments power to directly intervene in the economy is leading to an empowerment of the regional state, this new power brings with it new challenges that are also effects of globalization. These new challenges, if not met, threaten to fundamentally change the lauded localist character of the third Italy's economies.

A road map for the rest of the essay

The remainder of this essay will focus on the third Italy's regional economies, beginning by giving a brief explanation of exactly what kind of a model we are talking about, with some explanation of why it is so viable under some of the economic conditions created by the globalized economy. The essay will then go on to examine the difficulties that have arisen for small firm regional economies, focusing on their manifestations in these areas. There will be an attempt to understand the role of the regional government and its potential for meeting these challenges, with an analysis of their attempts to do so. Finally, some attention will be paid to the possible futures in these areas. While there will be no attempt to draw any sort of a general conclusion from this evidence with respect to the grand claims being bandied around about a world of self-contained regional small-firm economies, it is hoped that this evidence of pressures both toward and away from the industrial district model will at least illuminate realistically some of the possibilities for other regions that are not quite so well situated as is the third Italy.

The industrial districts of the third Italy[10]

The concept of the industrial district is one that was originally raised by the economist Alfred Marshall, and refers to towns, or series of towns in close proximity, that specialize in a particular product, and form a large interdependent horizontally integrated production process. In the industrial district, the unit of analysis is no longer the single firm, but an entire area made up of many firms, and the product can be a consumer good or an investment good, easy or hard to produce, and involving at times relatively sophisticated technology. The important thing is that it be a product whose production readily breaks into stages.

In the third Italy, the largest number of industrial districts are involved in the fashionwear industries. They specialize in textiles, clothing, footwear, leather goods and tanning, and wooden furniture. The other major industries in which industrial districts are found are metal goods industries, mechanical and electrical engineering, ceramic goods, musical instruments and toys [Sforzi, 1989]. They are usually in industries in which the area has a history of specialization, and as a result, the knowledge and skills required by the particular production process are possessed by many people in the district. A skill that is abundant locally can still be quite scarce on the world market, and this has undoubtedly been important to the Third Italy's success [Brusco, 1990].

Production in an industrial district is carried out amongst many firms under many different roofs, and while no individual firm is large, the district itself is, and is able to capitalize on what Marshall called external economies of scale. After all, as Sebastiano Brusco points out, there is no necessary "advantage in producing all the components of a product under a single roof: whether they produce similar or different pieces, twenty lathes have substantially the same productivity if they are gathered together or dispersed in separate buildings" [Brusco, 1982]. In a vertically disintegrated industrial district, the minimum efficient scale is reduced to the size necessary to have sufficient technology for an aspect of the production process, rather than an entire process.

In the industrial district, there are essentially three types of firms. There are those that produce for the final market, and in some third Italian districts up to 30 per cent of firms can be found in this category. Then there are those which can be termed "stage-firms" which are involved in only one phase of production, though not by any means necessarily in the simplest or dirtiest part of production. There is also a third type of firm which, though involved in a different industry, is part of the same vertically integrated sector. An example of this would be a button factory, part of the chemical industry, that is located in a clothing industrial district [Brusco and Righi, 1989]. The key here is that the vertically integrated sector is the unit of analysis, and what the firms sell on the final market comes entirely, or almost entirely from the same small area, but not from the same factory. The lines are not tightly drawn between the "final-firms" and the "stage-firms." All the firms are small, and can employ as many as 10,000-20,000 workers in 1,000-3,000 firms many with less than 20 employees each [Brusco, 1990]. In the district, there are also medium sized firms with larger workforces, but no firm is very large, and the vast majority have less than 100 employees [Bianchi and Gualtieri, 1990].

Within the district, there is a great deal of co-operation between firms, in terms of the commissioning and sub-contracting of work between firms involved in different parts of the production process. That is, there is vertical co-operation. There is also some horizontal co-operation, in the form of trade associations that attempt to give the small firms the advantages of economies of scale where they are possible, such as giving them professional book-keeping services and the like.

In general, however, there is a great deal of competition horizontally, in that the firms that do the same kind of work compete with each other for orders, and thus production quality and efficiency must be kept high. Firms are not dependent upon any one buyer, and if orders from one place dry up, the flexibility of their production methods allows them to seek orders from others who have a need for similar products. What is particular to a competitive industrial district is that the stage-firms are not dependent price takers, but are often on the cutting edge of production trends, and new products and machines have been invented in these areas.

This method of production is very well set up to take advantage of the changing conditions in world demand described in the previous section. The many firms concentrate on having very flexible production methods that are able to produce quickly whatever is asked of them by a firm they contract with, and they generally concentrate on being able to turn a profit on a very short production run. The combination of each firm having a fairly wide production range, and the extreme ease with which the subcontracting arrangements can be adjusted allows the firms that do have final market access to produce exactly what the market demands, and quickly. It is for this reason that this mode of production has been dubbed flexible specialization [Piore and Sabel, 1984; Hirst and Zeitlin, 1991].

Industrial district economies are well placed to take advantage of what are called economies of scope, in which it is cheaper to produce two products together than it would be to produce them separately. Usually, a scope economy is caused by the gains to be had from being able to adjust one's inputs to fit whatever the market desires at any given moment, so the cost savings are not necessarily strictly related to the theoretically lowest possible cost of production.[11] This ability to quickly adjust allows a firm to avoid revamping production due to any changes, and allows them to keep greater stocks of inputs on hand. The key gain from a scope economy, however, is simply that something a firm makes is always selling, guaranteeing a steady income stream. In the industrial districts, there is a combination of both internal and external scope economies; internal in that most firms are able to produce a variety of products depending on what a contractor requests, and external in that the district itself has a product range that really runs the gamut of the particular sector.

The aspects of the industrial district thus far described are both important and central to an understanding of the how the district works and why it is so viable in the current economy, but they are only one dimension of industrial district production, and they are not necessarily exclusive to territorial production agglomerations. There are also some other unique and very important sociological conditions that have the dual effect of lowering transactions costs in the subcontracting relationships and, at least in what will be defined as a "marshallian" industrial district, stimulating the learning that allows district firms to survive competition from otherwise privileged competitors.

Trust, transactions, and ongoing industrial adjustment

There are two competing explanations for the vitality of territorial agglomeration in networked production models. One simply stresses the lowering of transactions costs, and the vast improvement of information flow that is to be had when producing firms are in close proximity, while the other stresses the learning process and industrial adjustment.

The transactions cost argument is essentially that in any situation in which there is contracting, there are costs to the transaction that must be taken into account and set against the gains to be had from the externalization of the operation. In a situation such as that of the third Italy, where the firms depend on meeting special orders quickly, and where production is carried out across several firms creating the need for a great deal of coordination, transactions costs are greatly lowered by proximity, so any firm wishing to be involved in the process must locate itself within the agglomeration or have extremely low operating costs in order to offset the losses created by coordination costs and increased uncertainty. This is essentially the standard transactions cost explanation for any agglomeration, including cities, but in an industrial district, and particularly in the third Italy, there is another wrinkle that is said to further lower transactions costs.

Central and northeastern Italy has a long history of localist political subcultures that are said to have fostered high amounts of trust amongst the many small firms, allowing for the high amounts of cooperation that are required to make all the subcontracting so effective. In addition, there is an extraordinarily high incidence of associationalism in these regions that greatly facilitates information transfer between the various entrepreneurs, workers, and the regional government. The embedding of the production network in a dense network of institutions that allows for a series of shared rules, conventions, and knowledge, and allows for the punishing of rogue elements makes the cooperative elements much more powerful, and removes the prisoner's dilemma dynamic of contracting outlined by Oliver Williamson in his important work on transactions cost economics [Storper, 1995; Williamson, 1986].

Contributing to the high levels of associationalism is a strong historical political subculture that has a particularly localist character. In much of central Italy, there has long been a dominant presence of the Italian Communist Party (now the Democratic Party of the Left) while in the Veneto and northeastern Italy, there is a strong Catholic subculture. Although these two subcultures are ideologically quite different, they both have in common the defense of the local society, in the Catholic areas as a matter of ideology, and in the communist areas as a matter of necessity since the party was long shut out of government in Rome. These subcultures have contributed greatly the sense of a common purpose that makes it much easier for government, industry and unions to work together [Trigilia, 1986]. The strong local society has the further advantage of fostering such things as trust that greatly reduce the need for risk discounting in subcontracting relationships.

The institutional structure that facilitates successful industrial districts is described by Ash Amin and Nigel Thrift with the concept of "institutional thickness" [Amin and Thrift, 1994]. An institutionally thick region, they write, is one that has a strong institutional presence, a high level of interaction amongst the institutions in the area, the development of structures (due to the high level of interaction) that are capable of formulating "collective representation of what are normally sectional and individual interests," and the mutual awareness amongst the participants in the institutions that they are involved in a common enterprise. This sort of institutional structure is present in the third Italy, with its strong local society and well developed associations representing and articulating the many interests involved.

The institutional thickness of the third Italy almost certainly does lower transactions costs by reducing opportunism and effectively spreading information, but lowered transactions costs are not necessarily a satisfactory explanation for the continued vitality of the industrial districts. After all, we are in the age of a communications revolution that has lowered transactions costs enormously for any subcontracting arrangement regardless of geographic proximity. In fact, another explanation has been offered, an explanation that traces its lineage to Marshall's original elucidation of the industrial district. The same institutional and sociological elements described above also play a role in the creation of what will here be called a marshallian industrial district (MID).

As has already been mentioned, one of the elements of the globalized economy is an increasing premium on permanent innovation and permanent industrial adjustment. That is, there is what can be called a learning economy, where the ability to learn is what is required for success. An industrial district becomes marshallian precisely when it has the ability and creativity, due to its structure, to acquire the learning needed to constantly innovate. Giacomo Becattini writes that the "MID is either creative or it is not a (true) MID" [Becattini, 1991]. An institutionally thick industrial district is extremely well placed to remain on the cutting edge of change in production processes due to a combination of the widespread flow of information and the large number of people who are allowed input into the production process. Subcontracting arrangements in the third Italy often involve intensive collaboration between firms, but control is fairly dispersed so a firm that finds a better way is allowed to use it, and the widespread cooperation ensures that such innovation will quickly find its way to other firms in similar situations. In part due to the sheer number of firms attempting to do the same thing, and in part due to the diffusion of similar knowledge to many people, there is an enhanced ability to innovate, or so argue the proponents of the "marshallian" argument for industrial district vitality [Storper,1995; Brusco, 1982; Becattini, 1991]. This ability to innovate and the diffuse knowledge of the productive process was called by Marshall an "industrial atmosphere," which he said was "in the air" [Bellandi, 1987].

This explanation for the continued vitality of the industrial district model in an increasingly competitive environment is considerably more satisfying than the simple transactions cost explanation because it is capable of explaining dynamic and continued success even in the face of technological change. If the districts, despite their lack of formal structure and slew of small firms indeed have a competitive advantage in the acquisition of innovation rents, their survival seems to be explainable in terms of an ability to continuously stay one step ahead of the industrial adjustment game, allowing them to always be amongst the first to exploit any new markets or cracks in old ones. This should not be taken to imply that the transactions aspect is unimportant, only that it may not tell the whole story.

While attention here has largely been on industrial districts as ideal types, with only scattered reference to the actual existent systems of firms, it is hoped that the reader will accept the claim that what is found in the third Italy is in fact a series of marshallian industrial districts. This not implausible claim has been cautiously advanced by a series of Italian observers in the 1980s [see Goodman et al, 1989; Pyke, Becattini and Sengenberger, 1990; Becattini et al, 1987], and has even been accepted, with some qualification, by ardent critics of much of the flexible-specialization hypothesis such as Ash Amin and Nigel Thrift [Amin and Thrift, 1992; also Amin and Robins, 1990]. This is not to imply that the book is closed on the "real" dynamic in the industrial district, or that the learning is necessarily the key aspect in the districts success, but there does seem to be some consensus that these things are all factors, so hopefully we can use the term without too many problems.[12]

The downside to a globalized world for the third Italy's industrial districts

The break from fordism, while it has been in a part a tremendous boon in terms of market opening for systems of small firms, has also brought with it some new challenges, particularly in the 1980s. These new challenges are of three main types. One is presented by a recovery of the big firms who have become, in Bennett Harrison's words, "lean and mean" [Harrison, 1994], taking away some of the relative flexibility enjoyed by the small firms. The second is a result of the downside to being small and traditional in a big and modern world where markets are hardly perfect and control is often exercised by the powerful. The final new challenge to Italy's regional economies is presented by the increased competition presented by the Single Market Programme, though the Single Europe is likely to be a challenge mostly for the districts that produce higher technology products. However, this does not mean that the areas that produce traditional products can rest easily, as they find themselves under increasing competitive pressure from the NICs.

Big firm readjustment

There are two conceptually separable aspects to the readjustment of the large firms in Italy. On the one hand, they have discovered networked production and are competing directly with the industrial districts in the arena of fragmented production while they integrate control and strategy. This aspect will be dealt with in the next section, which will attempt to understand the challenges of smallness amongst the giants when both trying to do much the same thing. In this section, the focus will simply be on the partial removal of some of the small firm's comparative advantage vis-a-vis the big firm as traditionally understood, with reference solely to the ability to compete in terms of cost of production.

Despite all the claims that the industrial districts' flexibility comes from the ability to quickly change inter-firm arrangements, (quantitative) flexibility in labor use has been an important factor for the individual firms [Amin, 1989]. They have had a relatively greater labor flexibility in large part due to the weaker presence of unions in the smaller firms and to the much less stringent labor regulation for firms that are classified as artisanal.[13] In recent years, large firms have greatly closed this gap with the help of a restructuring of labor relations. Italian industrial relations have become a great deal less conflictual, even to the extent that the union will set rules at a national level that are "interpreted flexibly" by the union at the plant. There has also been an increase in "micro-concertation" that has focused less on salaries than on allowing firms labor use flexibility [Regini and Sabel, 1989; Regini, 1995]. This increased flexibility in labor use is obviously of great help to a firm that must quickly adjust to changes in mass demand. Inactive capital goods are even more expensive when you still have to pay the workers.

Having flexibility in labor use but technology that does not allow you to employ it is, however, not terribly useful. The big firms have also paid attention to this problem. A 1988 study by the Italian economists Camagni and Capello[14] finds that the 1980's saw a considerable narrowing of the small firm/large firm profitability gap, and that output per employee was 20 per cent higher in large firms. They attribute this difference to the greater uptake and utilization of new and potentially more flexible technology by the large firms. In the approach dubbed "neo-fordism" or flexible mass production, firms do not attempt to deal with market fragmentation by ceasing to separate planning and execution, which was a hallmark of fordism. Instead they use new CAD (computer-aided design) techniques to greatly shorten the time to market of their products.[15] Although they still do try to predict the market, they render themselves technologically capable of producing many variations of the same product, still essentially in a mass production format trying to capitalize on economies of scale. In addition to this, firms are employing such imported techniques as just-in-time production to acquire greater flexibility [Regini and Sabel, 1989].

These technological and labor flexibility aspects of large firm restructuring should in no way be assumed to tell the whole story nor should it be assumed that a recovery of the old way of production is what is in the cards. Nevertheless, not all demand has been totally fragmented, and it is important to understand that some of the competitive advantage of productive decentralization is found in the niches created by a production method too rigid for the demand it is trying to service. Even Marino Regini and Charles Sabel, who are critical of attempts to explain big firm recovery in terms of neo-fordism, say that what is often found is a mix of productive decentralization and single-roof restructuring. But they also say that the real key to understanding the big firms' attempts at meeting the ever-changing demand of global markets is in the growth of a new firm structure that is able to combine the flexibility gains of productive decentralization with scale advantages where they are really needed. That is, they have begun to compete with small and medium sized firms on their own turf [Regini and Sabel, 1989].

A decentralized body with a centralized head

In general, large firm restructuring in Italy takes as a presupposition that massive market oscillation is going to be a fact of life. Regini and Sabel write that "successes and failures of new products have become the best indicators of what the market will absorb. When the failure of a product becomes the most dependable form of market research, it means that markets are truly unstable" [Regini and Sabel, 1989].[16] The result of this is that there is an effort to organize production in such a way that it can very quickly adjust, and that does not depend on long runs. The way that has been found is essentially the subcontracting model, at least for actual material production.

There is no necessary reason that a vast series of relatively small firms must be set up in an industrial district. Large firms can farm out parts of their production process to a series of subcontractors that they essentially control. Often, the firm will keep to itself certain strategic functions such as planning of new products, the construction of prototypes, marketing and control of image, while decentralizing the actual material production and demanding extremely short delivery times from firms that are kept quite dependent on the central firm. In this way, the large firm retains control, but acquires the flexibility that it needs [Brusco, 1992]. This sort of practice is essentially what is done by firms such as Benetton (though they do contain territorially much of their production). [Harrison and Storper, 1991].

The essential characteristic of these large firm "flattened hierarchies" is that they decentralize production, sometimes to wholly or partially owned subsidiaries, sometimes to dependent subcontractors, but they do not give up any of their market and financial power. Martinelli and Schoenberger write that the "combination of increasing fragmentation of the productive system on the one hand and increasing concentration of capital and control on the other may be one of the most distinctive features of the new regime of accumulation" [Martinelli and Schoenberger, 1991]. In this arrangement, a large firm can enjoy some of the advantages of the industrial districts. While they may not have the same "blend of cooperation and competition," losing out perhaps on the learning and trust dynamic that leads to such close collaboration in the third Italy, they do get the simple flexibility and capacity to survive market irregularity. This clearly erodes some of the competitive advantage of the industrial districts.

The concentration of capital and control in a market dominated by large firms that are able to meet consumer demand also creates great pressures for the third Italy's industrial districts. There are some things that still retain quite natural economies of scale, particularly in a globalized market. The large firms' easy access to cheap capital plays a role not only in the obvious day to day sense of operating costs, but also allows for centralization of R&D, which, in a market that demands permanent innovation, has proven to be difficult for small firms. Although the MID seem to have an organizational ability to innovate (or so it is argued), this can be offset by big spending by competitors.[17] Another key advantage to access to capital is that large firms, or their subsidiaries, have much less trouble upgrading their technology, which has been at times a difficulty for the small firms in the districts. Perhaps the most important economy of scale, however, has to do with strategies of market control. Large firms undertake efforts to control distribution networks and use policies of branding in order to stabilize the demand curve. Thus, even if the small firms are perfectly capable of producing as cheaply or more so than the large firms, that can still have trouble getting access to markets. As Patrizio Bianchi points out, capital is not "just productive capacity for manufacturing homogeneous goods, but a variety of strategic investments," such as "R & D, product differentiation and advertising, flexible manufacturing systems, marketing and branding, distribution and assistance," all of which serve as barriers to potential competition [Bianchi, 1992]. In some sectors essential to the third Italy's economy such as machinery, garments, and food processing equipment, there were recent efforts by large firms to control distribution networks [Cooke and Morgan, 1994]. It is extremely difficult for the small firms to compete with such natural economies of scale, though they have made some efforts which will be outlined later in the essay.

The 1980's were a period of enormous rise in foreign direct investment, mergers, takeovers, joint ventures, and strategic alliances amongst large corporations [Jacquemin, Buigues and Ilkovitz, 1989]. Ash Amin and Kevin Robins write that the period was one of "international fragmentation and subcontracting of the production process, accompanied by greater control of the production network." In addition, they note that there was a great deal of horizontal and vertical integration especially in "the areas of finance, R & D, and marketing and distribution." Multinational corporations, they say, remain the real "shakers and shapers of the world economy" [Amin and Robins, 1990]. In short, market fragmentation in and of itself does not imply that there can be no large firms, or that hierarchy is dead and gone. Economies of scale are fully existent in some aspects of the world economy, and while the industrial districts of the third Italy may have some advantages of their own, it is hardly a given that they will be able to survive in the current conditions of the world economy. While E.F. Schumacher may have been right from a moral standpoint that "small is beautiful," being small in the global economy could mean being crushed.

The challenge of the single market

The single market programme brings with it the specter of increased competition for all industry across Europe which has obvious implications for any firm in Europe, though it should be noted that as far as direct competition is concerned, many of the third Italy's districts are in product markets that feel at least as much pressure from the NICS as from Europe. In the higher technology districts of Emilia, the new pressures come from the EU [Cooke and Morgan, 1994]. Although the size of the market will increase, an improvement in its quality[18] is hardly necessarily the case. The increase in mergers in the mid 1980's seems hard to separate from firms' preparation for the single market. The Padoa-Schioppa report said that the creation of a larger market does not in and of itself create more efficiency, and that the economies of scale do not get passed on to consumers but are dissipated by monopoly rents accrued by firms with dominant positions [Padoa-Schioppa, 1987]. The implication of this is twofold. On the one hand, the pattern of large firm market control strategies, in the absence other changes, is expected to be enhanced. On the other, there is a strong need for an active competition policy, and the facilitation of new market entry. This in part takes place in EU attempts to stimulate local and regional development through such things as the structural funds and the European Regional Development Fund, some of which may find their way into regional governance coffers in the third Italy, perhaps partially offsetting the effects of even larger competitors, though what actually happens remains to be seen [Bianchi, 1992].

Signs of strain (and hope) in the third Italy

While the extensive treatment of the large firms' response to the same conditions that made the industrial districts so effective may have seemed a bit afield, its salience should become considerably clearer in this section. There are some considerable signs of strain in the industrial district and many of them have precisely to do with the need to compete. The traditional form of the industrial district may be breaking down and converging to something that resembles the same sort of networks that the big firms are setting up. That is, there seems to be the growth of hierarchy, restriction of the subcontractor networks, and extreme pressures on the smallest firms. The merger mania of the 1980's was also no stranger to the third Italy. This section will attempt to elucidate the current context of the third Italy's industrial districts with attention to these signs of strain, although it will close with the signs of hope that are hidden amongst them.

Life under pressure: acquisitions and hierarchy

There was a large number of mergers and takeovers in the 1980's, and it seems to have had strong effects in at least some areas of the third Italy.[19] Between 1983 and 1988, there were 329 major transactions involving firms in Emilia-Romagna, which is just under 10% of the national total (in a region that produces about 8.5% of the GDP). These data also do not include some of the transactions involving the smaller firms (20-50 employees) so they somewhat underrepresent things [Brusco, 1992; Bianchi and Gualtieri, 1990]. The takeover phenomenon was largely concentrated in manufacturing sectors and, consistent with the trend in Europe as a whole, was rarely a case of a "fusion" in which the two companies genuinely become one as equals. A European Commission report on the takeover phenomenon in Europe found that most acquisitions resulted in the formation of "groups" in which the acquired firm was left in many ways separate, but the group nevertheless maintained a "strategic overall view of its operations" to "exploit synergies and serve a general objective at headquarters level" [Jacquemin, Buigues, and Ilkovitz, 1989]. This description, though at a general level for Europe as a whole, nevertheless depicts fairly accurately what happened in Emilia-Romagna. In Emilia-Romagna the phenomenon usually consisted of cases of larger firms acquiring smaller firms. 80 per cent of the firms bought had less than 500 employees, including a sizable percentage with less than 100, while 57 per cent of those buying had more than 1000. 90 per cent of the firms acquired had a total annual turnover of less than 100 billion lire,[20] which indicates that an inability to raise capital may have been the reason that the firms were unable to remain independent [Bianchi and Gualtieri, 1992]. The phenomenon seems generally to have been a case of concentration of ownership, in that it was large firms buying smaller firms and leaving the acquired firm essentially alone insofar as its status as a productive entity was concerned. Many of the transactions were by holding companies, that is, industrial groups [Bianchi and Gualtieri, 1992], which means that the data tend to underestimate the size of the acquiring firms, in that there are cases where a firm becomes a subsidiary of a larger firm that is itself a subsidiary.

Further evidence that the 1980s saw a real and not merely financial concentration of production in Emilia-Romagna is that purchases were usually of firms in the same general activity as the purchasing company, indicating that it was not a process of diversification so much as it was of integration, especially in the distributive phase of the process. The data on firm acquisitions seems to show that there is a reorganization of the productive structure in Emilia-Romagna. The bought firms are generally maintained unaltered in terms of juridical and operative status, but strategic functions are transferred elsewhere. Where once the districts were organized in a quasi-market way (mediated by relatively egalitarian networks), with many small firms relating to each other, there is now the insertion of hierarchical control of the subcontracting relationship [Bianchi and Gualtieri, 1992][21]. This is unquestionably a break from the ideal type model, and seems to be spurred by the difficulty firms face in the areas that do have scale economies as outlined above.

When reference is made to hierarchical inter-firm relations in the third Italy, what is intended is that lead firms maintain a great deal of control of the production process. Whereas in the 1970s a firm would order single pieces, or contract out single jobs to hundreds of small firms in such a way that any firm able to do the job would have a chance, in a hierarchical system, the lead firm will maintain a few trusted suppliers who will get essentially all contracts and will then contract out to a lower level and so on. The top firm will attempt to maintain control of market access so that the lower firms are dependent, where in the 1970s, numerous firms had direct market access. In a hierarchical district setup, control of the top of the supply chain is what is most important, as the key is to limit the options of the supplier firms lower down in the production chain.

Another dimension of change that involves change of ownership but that is not necessarily about the formation of hierarchy involves the growth of more formal relations even amongst firms of the same size, particularly amongst medium sized firms (around 100 employees). These formal relations often involved such things as minority share swaps. A recent study found that the firms that had the most formal relationships tended to be the most innovative firms on a technological level. These firms, while not becoming a strategic unit as occurs with the holding companies, nevertheless found a need to combine resources for market research, R & D, and the like [Brusco, 1992]. This aspect of the 1980s for the industrial districts is more one of evolution than death (as complete hierarchy would be) but it does point once again to the difficulty for small and medium sized firms in a big world. Formal groups seem to be forming throughout the third Italy, and while not all are hierarchical, many are, and both cases are indicative of the pressures and changes from the traditional model. While this section has focused on data from Emilia-Romagna, the phenomenon occurred elsewhere as well. Bellandi and Romagnoli report, in talking about the Pratese textile district, that there is a good deal of vertical integration and the creation of groups through a common capital holding. They also found that the need for an improvement in intrinsic product quality, in order to remain competitive on world markets, led firms to form more stable relationships with subcontractors through such things as mutual share ownership [Bellandi and Romagnoli, 1994]. Amin and Thrift found growth in hierarchy in Tuscany's Santa Croce leatherworking district as well [Amin and Thrift, 1992]. Within groups, Cooke and Morgan report instances of firms withholding information from others in order to stake themselves out a spot as a "network leader," which is a clear break from the cooperation cited as essential to the districts' successful character [Cooke and Morgan, 1994].

Another change: internationalization and externalization

The 1980s not only saw a changing internal structure of the third Italy's regional economy, there also was what Leonardi and Nanetti refer to as the "de facto internationalization of the Emilian[22] economy through mergers and the influx of foreign capital" [Leonardi and Nanetti, 1990]. The survey of mergers and takeovers referred to in the previous section found that foreign capital was present in 28 per cent of operations. In addition to the buying of Emilian firms by foreign groups, many Emilian companies bought firms that were outside the region [Bianchi and Gualtieri, 1990].

It is quite likely that the widening of the ownership pattern, with its emphasis on group formation, contributed to another important change in recent years. There was a considerable geographic spread of the subcontracting networks. Brusco has found that the metalworking firms of Emilia had orders from an increasingly wide geographical area. A similar occurrence was found in the textile district of the Carpigiana, where there were orders commissioned as far away as Turkey. The larger the commissioning firm, the further away it was willing to look for a subcontracting relationship [Brusco, 1992; Cooke and Morgan, 1994]. The reason cited by firms around Carpi for the distant production was the same one given by firms all over the place who have production done in low wage areas. It was far cheaper, and small supplier firms around Carpi, who generally work only 6 or 7 months of the year as it is a seasonal business, have to charge quite a lot to offset the down time. This externalization of the production process, while it is hardly complete, nevertheless raises the specter of a transformation of the districts into centers that maintain only the highest value added parts of the process, such as design and distribution, while farming out the actual production. Were this to occur, it would certainly mark a fundamental transformation of the industrial district production model, and would remove the high levels of proximity and cooperation between all levels of firms in the production process that provides, it has been argued previously in this essay, such opportunities for innovation.

The toughest times are at the bottom of the production chain

Both of the changes thus far discussed in this section are hardest on the very small artisanal firms that do not have direct market access and make their living solely through subcontracting. These contiterzisti risk finding themselves shut out when the groups are formalized, whereas in the past they were able to solicit orders from many firms in the district, that has changed as relations are more hierarchical and less "quasi-market." The shrinking of the number of people that they sell to cannot help but put them increasingly in the role of price taker.[23] Externalization of subcontractor networks also hits hardest at the bottom of the supply chain. The smallest firms are the ones who have the greatest difficulty in acquiring the capital needed to upgrade their technology, and often compete largely on price. These are the firms that depend mostly on very quick delivery and competitive prices, and if they are forced to compete with lower wage areas, they will have difficulty unless they are able to acquire technology that allows them to be more labor-efficient. Studies in both Emilia-Romagna and Tuscany have found that the artisanal firms found the 1980s to be a very difficult period [Bellandi and Romagnoli, 1994; Cooke and Morgan, 1994].

Some signs of hope

More explication of the possibilities for survival in a globalized world will be dealt with in the next section, where attention will be paid to the role of regional governance in stemming some of the pressures. In this section, the goal is really just to remind the reader that increased globalization may mean an increase in market segmentation which, while it does not rule out the hierarchical production structure, it also does not rule out the more traditional egalitarian industrial district, and it certainly does not eliminate the role of the small-firm driven economy, at least in these areas. The 1980s in Emilia-Romagna saw an increase in the number of small and medium sized enterprises, which, as of 1989, were 68,500, employing two thirds of its industrial workforce [Leonardi and Nanetti, 1990]. Throughout the 1980s, Emilia-Romagna continued to have a higher labor force activity rate than Italy as a whole, a very high, and growing, percentage of Italy's external (foreign) commerce, and a growing percentage of Italy's GDP. In terms of GDP, Tuscany held steady throughout the 1980's which were thought to be crisis years for the third Italy, the Veneto's percentage grew strongly, as did that of Le Marche. The third Italy's unemployment rates are lower than the national average as well [Brusco and Russo, 1992].

In the sub-section above on mergers and acquisitions, there was also a mention of the increase in formalization of cooperation through partial ownership swaps, especially by some of the most dynamic firms. This can also be viewed, with perhaps some qualifications, as a sign of hope, as it shows that there are responses to the crisis that do not involve subsidiarization to a large holding company, though the implications of such activities are not entirely clear for the districts as wholes.

In short, the 1980's did not spell economic doom for the third Italy, but there were unmistakably signs of changes in the districts, and some tendency of the districts to converge towards the very same "flattened hierarchy" that seems to be a tendential evolutionary direction of the partially decentralized multinational.

The pressures outlined in this section have not gone unnoticed by the regional governments of the third Italy who have taken on a series of activities to try and maintain the competitiveness of the industrial districts and overcome some of the disadvantages to small size in ways that hopefully will allow them to retain at least some of their traditional local character.

Regional governance of small firm economies in a globalized world

In this era of monumental government budget deficits and the difficulty of traditional central government macroeconomic policies (for reasons elucidated in the initial section), the region is increasingly being looked to for the supply side policies that seem to many to be the last province of government economic management. The traditional industrial policy of the Italian state had been primarily based on a system of financial incentivization that failed famously in the south of Italy, where it has resulted in a series of what are derisively called "cathedrals in the desert," large factories with no local linkages at all that do practically nothing to stimulate a viable regional economy [Martinelli, 1985]. In the third Italy, on the other hand, the regional government has taken quite a different tactic. Of course, they never had the budget of the Cassa del Mezzogiorno, so the southern model was never a real option, but the policies eventually undertaken nevertheless break quite completely from the model of direct subsidy favored by the central state [Bianchi, 1992].

Under Italian law, regions do not have the authority to undertake an employment or industrial policy, but they are in charge of "territorial development, artisan, and professional training" [Bellini, Giordani and Pasquini, 1990]. In addition, the regions, under a 1970 law, are allowed to set up developmental and promotional boards so long as they are not officially part of the regional government and are technically private entities, out of the direct control of the regional legislature. They are also allowed to set up specially equipped industrial sites and development zones [Bellini, 1990; Brusco and Righi, 1989]. From a legal standpoint they are somewhat constrained, and there have been calls for increased power delegation to the regions,[24] but despite this hamstringing by the central state, and particularly exploiting the 1970 law allowing for the setting up of "private" financial agencies, the regions have undertaken numerous initiatives in the industrial arena, acting to help the small firms of the industrial districts in precisely those areas that make them a bit undersized in a globalized world.

The rest of this section will describe the role the regional governments have played in stemming the pressures on the industrial districts, focusing largely on the way in which the third Italy's governments have exploited the laws allowing them a sort of backdoor industrial policy. The way in which they have done so, by acting essentially as a facilitator, will also be the subject of attention as these regions seem to play this role particularly adeptly, due to some exceedingly sociological reasons having to do with associationalism.

Fixing market failure: the business service centers

The previous two sections of this essay outlined the considerable difficulties that the firms of the industrial districts have due to their small size. They have trouble acquiring sufficient capital for expansion, they are too small to undertake effective R & D and have trouble acquiring and finding out about new technology. Marketing can be a big problem for an individual small firm, and training of skilled workers is too risky for a small business that cannot be sure it will have the resources to keep on the trained worker. All of these things are difficult for individual small and medium sized firms, but they also have the character of collective goods. The industrial districts themselves are quite large, and if they are able to organize themselves and cooperate sufficiently, it is possible for them to undertake a common policy for the provision of these things with many firms sharing the cost. There has indeed been an attempt to respond collectively to these difficulties. The regions have exploited the 1970 law allowing for the creation of private development agencies facilitated by the regional government. These agencies are initially underwritten by the regional state, but many firms become members and many of the agencies manage to become largely self-financing. The "business service centers" are of two main types. There are those that are specific to an industry, such as the CITER textile center in Carpi or the CEMOTER center in Ferrara for earth removal machines. Then there are centers that are territorial in focus, which concentrate on specific services for a wide range of industries, including centers such as ASTER, a technological development agency for all of Emilia-Romagna. In Emilia-Romagna, all of the centers are coordinated by a group called ERVET[25] which was initially set up in 1973 [Bellini, Giordani, Pasquini, 1990]. These centers do not, it should be noted, exist only in Emilia-Romagna, and there are numerous projects in Tuscany's districts, particularly around Prato. They exist throughout the third Italy, though are perhaps less common in the Veneto with its less interventionist Catholic background [Bellandi and Romagnoli, 1994; Trigilia, 1986]. They are all supposed to be largely self-financing within a few years of their founding, taking fees from the member firms, though there can at times be help from regional coffers.

The service centers undertake numerous activities, but mostly what they do is provide the small firms with information some of which can be very costly to gather.[26] This includes information about markets, what new technology is available, and advice on technical, administrative and commercial matters. They undertake applied research and planning, and sometimes take on aspects of quality control and product reliability testing [Bellini, Giordani, Pasquini, 1990]. Essentially, what they try and do is provide the small firms with the same sorts of business services that are available to their larger competitors. The goal is to provide a basis for structural change in the industrial districts -- that is changes that are permanent and which generally have to do with such things as process restructuring, product diversification, or a change in the growth of the market. The business service centers, in addition to providing high quality technical services to the industrial districts, serve as laboratories for the diffusion of innovation, extremely important in a global "learning economy."[27]

The need for professional training is of course another essential aspect for the success of the industrial districts, and while this is only sometimes a competence of the business service centers, it is also taken care of by regional and local governments. For example, Bologna's metalworking district has had access to graduates of the Istituto Valieriani, a technical school founded in the second half of the 19th century and deemed quite important in the original growth of that district in the Bologna area [Capecchi and Alaimo, 1992]. While this example may seem a bit out of date, the school still exists, as do other technical schools (i.e. a ceramics school in the Faenza ceramics district, connected as well to the district service center).

Another dimension of regional training policy is the apprenticeship system and its administration. All new apprenticeship contracts must be approved by a regional tripartite body. Since 1985, all small firm training has been a competence of the regions, and apprenticeship has often been the vehicle. 71 per cent of apprenticeship contracts are in firms of 50 employees or less, and the distribution of apprenticeships and work/training contracts is also disproportionately in the center-north [Perulli, 1993]. This is at least consistent with the hypothesis that these regions are more effective in using the system, though the strength of these economies leading to greater labor demand probably plays a role as well.

The need for credit is also potentially partially serviced by facilitation of cooperation at the regional level, though this remains a bit of a difficult point due to the underdevelopment of the Italian national and regional risk capital market

[Cooke and Morgan, 1994]. Sebastiano Brusco, however, has found an example in Modena that is somewhat encouraging, though he says that he has no data on similar initiatives elsewhere. Nevertheless, the case in Modena is one in which the artisans have founded a credit cooperative in which they underwrite each other's loans in order to get the lower interest rates to be had by reducing default risk.[28] The Modenese cooperative is extremely successful and has an extremely low default rate, which is probably because the loans are extended very much on the basis of trustworthiness, as understood by artisans who know each other, rather than on traditional bank criteria [Brusco and Righi, 1989]. In fact, this concept of trust amongst a local group, referred to earlier as a part of institutional thickness, is deemed by many to have played an important role in the creation of the sociological/institutional infrastructure that has underlain the third Italy's regional governments' ability to mobilize the districts.

Associations and institutional thickness

The special ability of these regions to have self-sustaining and endogenous growth cannot be chalked up only to "economic factors." The business service centers can remedy some of the market failures caused by the smallness of their constituency, but the unique ability of the regions to mobilize the many businesses to support and utilize the service centers has been at least in part the result of the strong localist and associational subculture, what was earlier called "institutional thickness." The regions of the third Italy were made famous for their long tradition of associationalism by Robert Putnam in 1993, who found exceptionally high membership in associations by citizens of these regions. This provides for extremely effective organized interest representation, and makes it much easier for the regional government to undertake projects. When they need to talk to the artisans, they can simply talk to the well organized artisan's association. Although the firms in the third Italy are small, many small enough to not have required union presence, there is still an extremely high union density, though one that tends to be less conflictual than in other parts of Italy [Trigilia, 1986; 1990]. The widespread presence of collective representation greatly facilitates the coordination required for the sort of industrial policy undertaken by third Italian regional governments, particularly because they do not have the resources to do everything themselves. They have primarily played the role of entrepreneur/facilitator for collective action by the firms in partnership with other groups. One perhaps odd downside to the high amounts of localism is that it seems to have somewhat impeded the ability of the regional governments to fully wrest power from communal (city) authorities who are constantly undertaking new projects that create unnecessary redundancies in services [Garmise and Grote, 1990; Bellini, 1990]. Trigilia also says that excesses of localism have made it hard to form a regional identity, and that things are too much connected to the locality, which has been somewhat superseded as a locus of policymaking as it is simply too small and limited [Trigilia, 1991].

Tying it all together: some possible futures in the third Italy

Perhaps it makes the most sense to begin with the least likely future in order to simplify the agenda. The third Italy's regional economies are extremely unlikely to fall completely apart and become something akin to what is currently found in the mezzogiorno. Certainly there is great competition from the NICs which could fundamentally change the character of the districts, creating unemployment particularly amongst the weakest of the artisan class. However, there is simply too much capital -- both human and physical, and too much productive infrastructure to not ensure that something will continue to be produced in the region.

We can safely rule out absolute disaster, at least in the short to medium term, but this does not mean that fundamental change is not a possibility nor that change could not dramatically lower the welfare of many in the districts. The implications of the change in ownership patterns has both the potential to remove control of the economy from the region as well as undermining the characteristics of the districts necessary to making them competitive despite their limitations.

In the realm of realistic futures, there are essentially two main possibilities. The most optimistic scenario is one in which the district is able to evolve in such a way that it is able to continue to be an endogenously controlled and successful economy, while the more pessimistic possibility sees a successful entry by the multinationals who buy up the most successful firms and use them to exert control over the district, reaping the short term benefits to be had from the years of development of specific skills but changing the character of the district in such a way that it is no longer able to continue to learn and endogenously meet the demands of an ever changing world economy.

The end of endogeny?

The risk of a convergence of the Emilian model onto the conventional "flattened hierarchy" model of the large networked corporation is not merely that it threatens the status of the thousands of very small firms that do nothing but subcontracting work. Rather, the fear is that Marshall was correct, and that an "industrial atmosphere in the air" is genuinely essential to the ability of a regional economy to stay ahead. Previously in this essay, in the section that outlined the signs of strain in the third Italy, the formation of groups and the entry of control from outside the region was described. If this continues to occur, it does not mean that the third Italy cannot remain an extremely viable regional economy. Indeed, it likely will continue to have a great deal of success. The regional government is widely considered to be extremely effective at providing the inputs at a regional level that theorists such as Hirst and Thompson and Jessop argue are the new province of economic management. The labor force, at least at the moment, is highly skilled, argued to be essential for successful competition in the current world economy [Wood, 1994]. As has been previously claimed here, networked production does not have to be organized in a "quasi-market" format in order to meet fluctuation in demand, so the formation of groups and hierarchies in an environment that was once the province of many equals does not necessarily mean the erosion of the purely "economic" competitive advantage of an industrial district. The third Italy's regions, even if there are great changes, remain well positioned by most standards to compete in a world economy that demands efficiency from everyone.

In this scenario, in which there are fundamental changes in the pattern of organization in the district, what changes is control. Foreign (in the sense of outside the district) ownership, or control by lead firms creates a centralization of control of future investment, production and employment. It means a full entry into the global economy and becoming what Ash Amin and Nigel Thrift call "neo-marshallian nodes in global networks" [Amin and Thrift, 1992]. In the short run, this is not disastrous by any means, though it does have its downsides. The most obvious of these is that it will continue to marginalize the smallest firms which do still employ quite a few people, leading to potentially quite negative distributional results. Increased hierarchy is likely to lead to an externalization of the lowest value-added parts of the production chain, and perhaps a partial transformation of the economy into a more service-oriented economy with only the final aspects of production in the third Italy, as it becomes more typical of other rich regions. The impact of this on the lower socio-economic strata is quite hard to gauge, but it seems unlikely to be an improvement. Another downside, whose value is again quite hard to know, is that there is some value to tradition and constancy in the way of life of a people, and the local control of the economy means that firms were far more likely to choose to make investments locally, regardless of the high social wage and prospects for lower wages elsewhere.

This not-all-that-sad story of the potential transformation of the third Italy only in terms of final control of investment and production does not tell the whole story, however, and there could be some very real costs to changing the structure in the longer run. If one accepts that what is found in the third Italy is a series of Marshallian industrial districts and that the real key to their success is not merely a proximity-induced transaction cost lowering along with good factor inputs, then a change in the structure threatens the learning and ability to constantly undertake industrial adjustment. The hypotheses about the MIDs argue that this special ability is the fruits of an institutionally-thick local society where constant interaction and social networks facilitate information transfer and trust. The sustainability of the "institutional thickness" and the "industrial atmosphere," however, is hardly a given if the character of the district is fundamentally changed.

Outside control of the firms means that the manufacturers and business leaders will no longer have the stake that they once had in the many associations that do not serve only the instrumental purpose of information dispersal. If the districts are no longer controlled by local entrepreneurs, there will be no reason for the entire local society to feel that it is involved in some sort of a "common task." This is also threatened by the growth of hierarchies and the decreased egalitarianism in the production networks, as it changes the subcontracting process from a positive-sum to a zero-sum game, and changes the status character of associational life. Brusco and Russo write that "in a labor conflict with Panini (local company), the mayor could usefully get involved, and maybe even the Bishop; with Maxwell (a multinational) bargaining is, purely and simply, on the basis of relative strength and the professional qualifications of the union" [Brusco and Russo, 1992]. The superior ability of these regions in the provision of collective goods is the potential casualty.

Diffusion of parts of the productive process outside of the district destroys the "industrial atmosphere" that comes from large numbers of people knowing something about the productive process. One of the theoretical underpinnings to the learning hypotheses was precisely that there are many people who have the freedom to decide what process they feel works best. This, when combined with the rapid diffusion of new ideas when found, is the essential characteristic of the industrial atmosphere that has come into favor amongst Italian scholars to explain the innovational capacity of the districts [Becattini et al, 1987]. In short, the removal of local control may not just be "sad" and the end of a tradition. It could mean that what is occurring in the third Italy is a case of spending all the innovational capital in a very short time span.

There is no way of knowing if all this gloom and doom about the long term future of the third Italy in the face of a failure to maintain local and relatively egalitarian control will actually come about. This scenario is fundamentally premised on assumptions about both the nature of a Marshallian industrial district and the appropriateness of this term for the regional productive agglomerations in northeastern and central Italy. If these are not true, perhaps the insertion of the third Italy into the global economy in a "normal" way is simply overdue. Another possibility is that we are indeed talking about MIDs, but that the place of an MID in the world economy is a thing of the past, and that innovation has simply gotten outside their budgets. Perhaps they did it well, this story would go, but they are no longer viable under current conditions, and it is not simply a question of their being bought out by their bigger, jealous, but less efficient competitors. Whether or not the districts will indeed cease to be "marshallian" remains to be seen. If they do cease to exist as such, perhaps the final word can be written about the "true" nature of the industrial district, but for now, things are still too murky.

But the end is by no means assured

An evolution of the industrial district is undoubtedly underway, but this does not mean that it will cease to exist as such. As mentioned in the previous section, the region continues to play an essential role, as it always has, in providing the various economic factor inputs needed to allow a regional economy to compete, but this is no longer enough in these regions. And, as also has been mentioned, the regional governments are attempting to meet the new challenges presented by the encroachment of the multinationals onto what has traditionally been smaller firm territory. There have been some real successes amongst the business service centers, and to some extent, the continued viability of the numerous small and medium sized firms is in itself a testament to the potential for survival of the districts, even if there are some signs of strain.

Little more need be said in this section about the way in which the districts could survive more or less intact, as it was covered previously in the essay. It really quite simply depends on the success of the regional interventions outlined above in the circumvention of the problems presented by the need for constant technological upgrading, and, perhaps most importantly, the oligopolistic market practices that present the greatest threat. The third Italy has a long history of being particularly successful in the solution of collective action problems, and it seems unlikely that those of a chiefly productive character will doom the districts. Perhaps there will be some partial re-integration vertically of parts of the process in order to provide firms with the capital needed, along with growth of more formal arrangements amongst the medium sized firms, but these are not things that need fundamentally undermine the localism needed to retain the traditional character and storehouse of institutional public goods. The "oligopolization" of the economy is somewhat more intractable, but need not necessarily mean the end. Consortiums of firms can also acquire the sophisticated marketing required for branding and worldwide product reputation. The end results in this arena may also depend on the evolution of an EU competition policy, but for now, we must simply adopt a wait and see approach, remembering that it is altogether too early to eulogize the traditional model.

A few final words about the region in a global economy: can any lessons be drawn from the third Italy, or is it too special?

It certainly is a special model, and other places that wish to adopt the practices of Emilia-Romagna should not assume that they will be able to easily institute the "institutional thickness" aspects. With that said, there still remain lessons for other regions, chief among them that public provision and facilitation of collective goods can have an impact on the sustainability of regional control of the economy. Perhaps it can have more of an impact in Emilia, but this does not change the potential usefulness to other areas should they be able to provide the inputs collectively. In this sense, the third Italian story does lend support to those who say that the region could be an effective level for supply-side intervention in the economy, while its special character makes it necessary to caution against drawing any conclusions about the ease of doing so.

The other main lesson to be drawn is not quite so positive. Even though the third Italy is very successful in its ability to mobilize at the regional level for public good provision and continues to have a viable economy, even its special status does not seem to be able to protect it from the pressures of a globalizing world economy. It has been claimed in this paper that it is extremely unlikely that the third Italian regional economy will fall apart, and that supply-side policies can be expected to retain some manufacturing in the region. However, this does not mean that control will remain in the region, or that it will necessarily be able to retain its special character in the long run due to its eventual full immersion in the global economy, in a story in which it would become just another effective producing region, a part of the decentralized body of a centralized head made up of oligopolistic firms. Perhaps the tide will be stemmed, but the pressures are very real, and if they are felt here, in one of the most famously localist places in Europe, it is hard to believe other places will have an easier time of it.

Throughout this entire essay, and indeed, throughout most of the literature, an unstated assumption is that all regions are competing against each other for investment and to be the place that produces most efficiently. An effect of globalization, with its rampant capital mobility, is to enhance this pressure. The third Italy, and other regional economies, can provide all the inputs of production, but there remains the constant threat of being outcompeted by some other region, despite the extremely high productivity in the region. The global economy seems to be increasingly taking on the character of zero-sum competition amongst regions, with large corporations arbiting the game, bestowing the right to work on the winners. In this sort of a competition, the third Italy is altogether quite likely to make out all right, but the fact remains that it is not a pleasant game, and it would be nice if they could stay out of it. Local control means local investment, even at the expense of forgoing the short term gains to be had from lower wages elsewhere, while full integration into the world economy as more than simply a trading partner implies external control with no incentive to stay the course.

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[1] See especially Trigilia (1991), Hirst and Thompson (forthcoming), and Jessop 1994. There are also others who make similar claims.
[2] The example of France in the early 1980's is frequently pointed to as a colossal failure to recognize the changes in the world economy.
[3] This term is drawn from the terminology of the regulation school, and I do not intend to defend its use here, as it is not particularly central to my argument.

[4] Or for that matter, willingness. I would argue that they cannot, at least not easily, but it is sufficient that they be unwilling.
[5] Which is not to say that it is exogenous to the international economy as a whole, but it is to the actors involved.
[6] Three Italies: the territorial difficulties of Italian development.
[7] The area includes the regions of Le Marche, Umbria, Tuscany, Emilia-Romagna, the Veneto, Friuli Venezia Giulia, and Trentino-Alto Adige.
[8] As little as possible will be said about the first years after the discovery of the industrial districts, and the great success in the 1970's. The minimum feasible will also be said about the workings of an industrial district, and it is hoped that the unfamiliar reader will refer instead to Brusco, 1982, or Piore and Sabel, 1984. Goodman et al, 1989 is another possibility.
[9] Famous thanks in part to Robert Putnam and Making Democracy Work.
[10] This section has no intention of "explaining" the success of the industrial districts in any sort of complete way. Space is limited, so the focus will be on the more "economic" aspects of the districts, touching only on the most important sociological and institutional aspects in a general way. The goal will be to elucidate those aspect that relate particularly to the current changes in the world economy wrought be globalization. This should not be taken to imply that many of the other sociological variables that have been cited (i.e. the strong connection to the land, family structure, etc.) are unimportant. They simply lead a bit afield. In the sense that a firm that had a guaranteed market might be able to produce something more cheaply using completely inflexible methods. This would theoretically be cheaper, but it is not cheap to produce anything that does not then get sold. More could certainly be said to defend these claims here, but it would lead a bit afield, particularly since no substantial claims rest on this hypothesis. Rather, the remainder of the essay will focus on the stresses on the truly existent district, and only later will these claims be returned to, and it will still be in a "if it is true that..." format. I will say that I am convinced by this argument, but the skeptical reader can still get some value from the remainder of the essay.
[11] Which in Italy is defined no by activity but by size, and is, with some qualifification, available to firms with less than 20 employees.
[12] Reported in [Amin, 1989]. I was unable to acquire the original study here in Wisconsin.
[13] Heavily used by some industrial district small firms as well, for the same reason.
[14] Translation by me, as will be the case whenever an Italian source is cited.
[15] The relative weakness in small firm capital and R&D access is noted by numerous observers including [Bianchi and Gualtieri, 1990, 1992; Brusco, 1992; Blim, 1992].
[16] That is, the assumption that enlarging it makes it more "perfect."
[17] I only have merger and acquisitions data about industrial districts in Tuscany and Emilia-Romagna, and much more complete data on Emilia, but as these are the areas thought to "exemplify" the third Italian economies, what happens there, even if it is not exactly mirrored in the Veneto, or elsewhere, still seems relevant. There is also anecdotal secondary evidence of it happening elsewhere.
[18] Depending on the exchange rate, somewhere in the neighborhood of $60 million, which is not terribly high -- this is not profits, but the money that passes through the firm.
[19] The reader may note that I am basing much of this section on work done by Bianchi and Gualtieri. In large part this is because they are the authors of the study that provides the data used, but this should not be taken to imply that other authors on the subject have not also noted the increased presence of hierarchy in the third Italy. Itis a rare study of the third Italy in this period that does not mention it. The reader can also refer to Amin, 1989; Martinelli and Schoenberger, 1991; Cooke and Morgan, 1994; Brusco, 1992. It is a widely recognized phenomenon.
[20] As before, my data is limited to Emilia, but other studies find a similar phenomenon in other areas.
[21] Their assets become increasingly specific in Oliver Williamson's terminology.
[22] In the recent elections, this idea was bandied about by both sides, and is also, of course, the raison d'etre of the Northern League. For an academic call for such a change, the reader can refer to [Trigilia, 1991].
[23] Ente Regionale per la valorizzazione economica del territorio -- Regional Agency for the Economic Improvement of the Territory.
[24] It should be noted that information undoubtedly has the character of a public good. One person's knowing something in no way takes away from the ability of another to know it. At times information acquisition can

be quite expensive, and its wide possession can detract from a party's ability to capitalize on it, in a zero-sum game. The value of information above and beyond its public good aspect is in its scarce provision, and its diffusion outside of that is potentially costless (unlike a naturally scarce resource -- such as a physical input), excepting future information provision problems due to externalization of benefits.

[25] The implementation of the service centers has not been entirely unproblematic. [Blim, 1992] has found that in shoe districts in Le Marche, many firms were reluctant to utilize them, and only the most dynamic firms patronized them. He attributes this to excessive traditionalness being both a weakness (not going, refusal to change) as well as a strength (entrepreneurial subculture) of the firms.

[26] Reducing the risk that the creditor will not receive the money. In fact, the rate of default to the consortium is extraordinarily low as well. As Brusco notes, paraphrasing a local artisan, the man who gets a loan from the bank stays up nights wondering how not to pay it back, whereas the man who gets the loan from his colleagues stays up nights wondering how to pay it back.

[27] Schoenberger. 1991: "Oligopoly is alive and well: notes for a broader discussion of flexible accumulation" in Benko and Dunford (eds): Industrial Change and Regional Development, New York, Belhaven Press, pp. 117-133.

[28] Padoa-Schioppa, Tommaso (et al). 1987: Efficiency, Stability, and Equity: a strategy for the evolution of