**IDS Working Paper 144**

# The effect of globalisation on industrial districts in Italy: the case of Brenta

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November 2001

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This paper is an output of the research project 'The interaction of local and global governance: implications for industrial upgrading'. This project, which is funded by the Volkswagen Foundation, is a joint initiative of the Institute of Development Studies at the University of Sussex and the Institute for Development and Peace of the University of Duisburg, Germany.


ISBN 1 85864 395 3

## Summary

This paper is concerned with the impact of globalisation on local competitiveness in Brenta, one of the most important Italian footwear districts. The aim is to integrate the typical industrial district approach with the global value chain approach. To understand the changes confronting Brenta, the paper distinguishes between enterprises operating in (a) the top brand chain, dominated by the owners of global brands in the luxury market, and (b) the high quality chain in which German buying groups aggregate many independent footwear stores. The questions addressed are: is globalisation pushing Brenta into new value chains? What types of governance characterise the relationships between local and outside actors? Do the chains' leaders come from inside or outside the districts? Does the integration of industrial clusters in global value chains enhance or weaken local upgrading strategies? One of the main findings is the increasing importance of the top brand value chain in the district. To be part of the chain, Brenta's shoe producers accept a functional downgrading, abandoning design and marketing and focusing on production. Nonetheless, the remarkable recent growth rates in the luxury industry, which is built around global top brands, have allowed local producers in this chain to perform better that those in other chains.

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## 1 Introduction*

The turn of the century coincides with a divide for the Italian shoe industry and more generally for the fashion industry altogether. Due to increasing globalisation, major changes are taking place: international relocation of production, increasing concentration in distribution, mergers of fashion firms and acquisitions of additional brands and the formation of financial multi-product giants (Saviolo and Testa 2000). Nothing remains the same, not even in a long established industrial district such as *Riviera del Brenta*, a highly specialised and strongly export oriented footwear cluster, located near Venice.

This paper is concerned with the impact of these global transformations on local competitiveness in Brenta, one of the most important Italian footwear districts. The aim is to integrate the typical industrial district approach,[1] traditionally focused on analysing the local sources of competitive advantages, with the global value chain approach which stresses that activities such as design, production and distribution are often located in different regions or countries (Gereffi 1999 and Kaplinsky 1998).

In the typical industrial district most of the activities along the value chain have traditionally been locally undertaken and competitiveness of producers has mainly come from intra-cluster vertical and horizontal relationships generating collective efficiency, namely increasing returns from incidental economies of agglomeration and active co-operation (Rabellotti 1997; Schmitz 1995 and 1999). Recent changes in production systems, distribution channels and financial markets, accelerated by the globalisation of product markets and the spread of information technologies, suggest that more attention needs to be paid to external linkages.[2]

Furthermore, industrial boundaries are blurring and the shape of industries is no longer conforming to the standard industrial classification (Mytelka 2000). This is the case of the footwear sector, analysed in this paper, which is increasingly integrated in the fashion industry, dominated by a few multi-product oligopolies, exploiting economies of scale and scope in activities such as distribution, marketing and branding across traditionally separated industrial sectors such as shoes, clothing, glasses, perfumes and leather goods. Accordingly, to understand the effect of these changes on a cluster such as Brenta the adoption of a more enlarged perspective of analysis, including linkages with actors external to the district, becomes necessary.

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* I am very grateful to Hubert Schmitz who inspired this research project and then commented in great detail on successive drafts of the paper. I also would like to thank Tania Pasin for assistance in interviewing enterprises. Furthermore, Brenta's entrepreneurs, ACRIB (Associazione Calzaturifici della Riviera del Brenta), the Regional Government of Veneto, the US National Shoe Retailers Association, the buyers interviewed at the Düsseldorf shoe fair, Sabino Ventura, Roberto Vergelio and Heinrich Zumnorde are kindly acknowledged. A special thank you goes to John Humphrey, Raphie Kaplinsky, Jorge Katz and participants at workshops held at the Institute of Development Studies, University of Sussex and University of Molise who provided valuable comments on earlier drafts. Financial support from the Volkswagen Foundation and the Department for International Development is gratefully acknowledged. The shortcomings of the paper are my responsibility alone.

1 With typical industrial district we refer to the Marshallian concept and particularly to its Italian variant. For a collection of classical papers see Pyke, Becattini and Sengenberger (1990). A recent collection of papers on industrial clusters in developing countries can be found in Nadvi and Schmitz (1999).

2 Markusen (1996) broadening the definition of industrial district discusses four types of districts. In the 'satellite platform' type, consisting of a congregation of branch facilities of externally based multi-plant firms, she acknowledges the importance of external linkages.

In our study of the effects of globalisation on Brenta we try to fill this gap in the literature on industrial clusters using some of the findings of the global value chain approach, which helps to take into account activities taking place outside the cluster and in particular to understand the significance of the relationships with key external actors.[3]

An important aspect stressed in the literature on value chains is that the various activities in the chain are subject to some degree of governance or coordination (Gereffi 1994). This coordination may take place through arm's-length market relations or non-market relationships. In the latter case, following Humphrey and Schmitz (2000), we distinguish between three types of governance: the network implying co-operation between firms of more or less equal power which share their competencies within the chain; a quasi-hierarchy involving relationships between legally independent firms in which one is subordinated to the other and with a leader in the chain defining rules that the rest of the actors have to comply with and finally hierarchy when the local firm is owned by an external firm.

Among the different forms of governance, the literature on value chains, which is mainly concerned with developing countries, stresses the importance of the quasi-hierarchy type, distinguishing between those cases when coordination is undertaken by buyers ('buyer-driven chains') and those in which producers play the key role ('producer-driven chains') (Gereffi 1994). Moreover, the same Gereffi (1999) together with Dolan and Humphrey (2000) conclude that the increasing concentration of retailing in developed countries makes buyer-driven chains a growing phenomenon. In this paper we aim at contributing to this debate, broadening the analysis to developed countries, showing that quasi-hierarchy may be also a relevant form of governance to represent linkages existing between producers from one of the main shoe cluster in Italy and the lead fashion firms governing the chain.

The following questions are addressed: Is globalisation pushing Brenta towards new value chains? What types of governance characterise the relationships between local and outside actors? Do the chains leaders come from inside or outside the districts? Does the integration of industrial clusters in global value chains enhance or weaken local upgrading strategies?

The concept of upgrading is used here in the sense proposed by Humphrey and Schmitz (2000). Process upgrading means transforming inputs into outputs more efficiently by re-organising the production system or introducing superior technology; product upgrading is moving into more sophisticated product lines and functional upgrading is acquiring new, superior functions in the chain, such as design or marketing. Furthermore, from our empirical analysis in Brenta a different possible form of functional upgrading coming to the fore is the externalisation of low value added functions to focus on more advanced activities or higher value added segments of market.

This paper tackles the above questions in the case of *Riviera del Brenta* shoe cluster. The study is based on the findings of field work carried out in Brenta in summer 2000, interviewing 40 shoe manufacturing enterprises, randomly selected from a list provided by ACRIB (Associazione Calzaturifici della Riviera del

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[3] The need of using the market channel approach to study industrial clusters was first advocated by Knorringa (1999) in his work on Agra, a footwear district in India.

Brenta), the local entrepreneurial association of footwear producers.[4] Qualitative information was also collected through in-depth interviews with trade organisations, fashion firms, retailers and other key informants. Furthermore, in September 2000 during the international shoe fair in Düsseldorf we interviewed six buyers belonging to some of the main European buying groups.

To understand the changes confronting Brenta we could also compare the information collected in 2000 with the findings of a previous study we carried out in the early 1990s, which gives a detailed picture of the district at that time with a focus on internal linkages (Rabellotti 1997).

Here, we disaggregate the cluster by value chains and analyse the two main ones: the top brand chain operating in the luxury market and the German chain, dominated by groups aggregating the majority of independent footwear stores in Germany. Compared with our previous work on Brenta (Rabellotti 1997) we are therefore shifting the focus from the internal to the external linkages of the cluster trying to close a gap in the literature, which traditionally privileged the study of local relationships.[5] Nevertheless, we agree with Schmitz (2000) that the challenge is not one or the other but rather understanding the interaction of internal and external linkages. The main aim of this paper is therefore to investigate Brenta's problems and opportunities arising from globalisation, analysing external linkages, local relationships and how they interact.

After an overview on Brenta and its main markets, the paper concentrates on two main chains. Firstly in the top brand chain, which is becoming one of its most important markets, we analyse the recent entry of some global fashion leaders into the footwear sector. An increasing number of fashion companies, originating in other sectors, have penetrated the footwear industry looking for skilled manufacturers in order to outsource the production of shoes sold with their brand names. This is why in Brenta many producers have begun to work as subcontractors, abandoning key activities such as design and sales, which are the core competencies of fashion companies. The latter have become the new lead firms of the chain.

In the second chain analysed, high fashion and top brands play less of a role but high quality is important. We call it the German chain because Germany and neighbouring countries constitute the main market. A key feature of this market is that independent retailers are organised in large, powerful buying groups. These groups are network organisations supplying credit and information to their members, helping them to reduce transaction costs and risks.

The paper then analyses how global linkages have affected local linkages, stressing that the latter have weakened in recent years: in backward linkages the weakening is due to the increasing outsourcing to Romania and other nearby low-wage countries and in forward linkages it is due to the forced abandonment of activities such as design and marketing, notably in the top brand value chain.

The final section draws together the main conclusions and reflects on how Brenta's future evolutionary path is influenced by its recent redefined participation in global chains.

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4 We asked ACRIB to select among their members a list of firms selling in different geographical markets and to different types of customers. Then from this list, the sample of firms was randomly selected.

5 Notable exceptions are Weijland (1994) and Knorringa (1999).

## 2 Brenta: past and recent history

In Brenta the origins of the footwear industry date back to the establishment of *Calzaturificio Voltan* in 1898. It was founded by Giovanni Voltan, an artisan who, after spending some time in the United States to learn the trade, returned to his small village (Strà) with some machines for making shoes to set up his own business. By 1904, the firm employed 400 people, producing 1,000 pair of shoes per day. It was the first shoe factory in Italy. At the beginning of 1900, many workers from Voltan's enterprise began to set up their own independent businesses in Strà and other nearby villages. This was the beginning of a shoe district, named *Riviera del Brenta* after the river which flows through it.[6]

During the footwear industry boom after World War II, the sector progressively absorbed most of the rural workforce available in the area. In the 1960s, the local enterprises expanded and increased their exports, specialising in the upper segments of the market. In 2000 88 per cent of the shoes produced in the area were medium-high and high price women's shoes with an average ex-factory price of 58 Euro.

**Table 2.1 Number of pairs and sales in Brenta 1981–1999**

| | Number of pairs (thousands) | Growth rate % | Total sales at 1995 prices (Euro millions) | Growth rate % |
|---|---|---|---|---|
| 1981 | 8580 | – | 174,9 | – |
| 1982 | 8270 | -3.61 | 194,8 | 11,4 |
| 1983 | 8005 | -3.20 | 223,1 | 14,5 |
| 1984 | 8600 | 7.43 | 250,6 | 12,3 |
| 1985 | 8660 | 0.70 | 264,9 | 5,7 |
| 1986 | 8420 | -2.77 | 272,7 | 2,9 |
| 1987 | 8175 | -3.00 | 267,4 | -1,9 |
| 1988 | 7929 | -3.10 | 251,0 | -6,1 |
| 1989 | 8005 | 0.95 | 255,4 | 1,7 |
| 1990 | 7895 | -1.37 | 254,5 | -0,4 |
| 1991 | 8100 | 2.59 | 265,6 | 4,4 |
| 1992 | 8073 | -0.34 | 286,0 | 7,7 |
| 1993 | 8505 | 5.35 | 336,3 | 17,6 |
| 1994 | 8691 | 2.18 | 342,5 | 1,8 |
| 1995 | 8810 | 1.37 | 363,9 | 6,2 |
| 1996 | 8509 | -3.41 | 384,5 | 5,7 |
| 1997 | 8399 | -1.30 | 393,2 | 2,3 |
| 1998 | 8138 | -3.10 | 401,3 | 2,0 |
| 1999 | 8203 | 0.80 | 441,3 | 10,0 |

Source: ACRIB (various years)

[6] From an administrative point of view, the district is divided into two provinces of the Veneto region: Venice and Padua.

Since the second half of the 1980s, the area has suffered from increasing competition in the international market and sales have stagnated, fluctuating between 7.9 and 8.8 million pairs (mainly due to exchange rate fluctuations). In value terms, however, sales continued to increase in most years (Table 2.1). It may be useful to add that Brenta's performance is in line with that of the rest of the Italian footwear industry, which suffered from stagnating European demand and from increasing international competition (ANCI 2001).

As regards the structure of the district,[7] in 1999 there were 635 firms; of these, 214 were shoe producers, 300 firms manufacturing inputs such as heels, soles, lasts, 60 design firms with 141 employees and 61 trading companies (Table 2.2). The number of firms has decreased continuously from the second half of 1980s as well as the number of employees, which declined from over 10000 in 1985 to 8797 in 1999 (Table 2.3).

**Table 2.2 The district in 1999**

| | Number of firms | Number of employees |
|---|---|---|
| Footwear companies | 214 | 6411 |
| Accessory manufacturing companies | 300 | 2053 |
| Shoe designers | 60 | 141 |
| Trading companies | 61 | 192 |
| **Total** | **635** | **8797** |

Source: ACRIB (2000)

**Table 2.3 Number of firms and employees in Brenta 1981–1999**

| | No of firms | No artisanal firms * | No of trading companies | Total no of companies | Total employees |
|---|---|---|---|---|---|
| 1981 | 147 | 302 | 74 | 523 | 10181 |
| 1982 | 149 | 349 | 73 | 571 | 10130 |
| 1983 | 154 | 385 | 73 | 612 | 10107 |
| 1984 | 170 | 406 | 76 | 652 | 10131 |
| 1985 | 177 | 436 | 77 | 690 | 10067 |
| 1986 | 183 | 515 | 77 | 775 | 10008 |
| 1987 | 195 | 546 | 81 | 822 | 9971 |
| 1988 | 194 | 548 | 88 | 830 | 9823 |
| 1989 | 200 | 602 | 90 | 892 | 9751 |
| 1990 | 190 | 603 | 93 | 886 | 9597 |
| 1991 | 193 | 562 | 77 | 832 | 9419 |
| 1992 | 173 | 524 | 74 | 771 | 9007 |
| 1993 | 172 | 535 | 68 | 775 | 9101 |
| 1994 | 180 | 529 | 68 | 777 | 9137 |

7 For a detailed analysis of the main characteristics of the Brenta district also see Rabellotti (1997).

**Table 2.3 continued**

| | No of firms | No artisanal firms * | No of trading companies | Total no of companies | Total employees |
|---|---|---|---|---|---|
| 1995 | 179 | 522 | 71 | 772 | 9139 |
| 1996 | 171 | 495 | 61 | 727 | 9003 |
| 1997 | 174 | 484 | 61 | 719 | 8912 |
| 1998 | 163 | 470 | 66 | 699 | 8791 |
| 1999 | 146 | 428 | 61 | 635 | 8797 |

* Artisanal firms are those defined as having fewer than 20 employees.
Source: ACRIB (various years)

Shoe factories in Brenta are characterised by their small size. According to the latest available industrial census (1996) 78 per cent of the firms employing 40.4 per cent of workers have fewer than 20 employees and 18 per cent, corresponding to 34.4 per cent of total employment in the shoe industry, have between 20 and 49 employees. The average size is 15 employees (Table 2.4).[8]

**Table 2.4 Size distribution of shoe enterprises in Venice and Padua provinces: 1996**

| | Number of enterprises | % | Number of employees | % |
|---|---|---|---|---|
| < 20 employees | 545 | 78.0 | 4329 | 40.4 |
| 20–49 employees | 124 | 18.0 | 3679 | 34.4 |
| 50–99 employees | 23 | 3.0 | 1745 | 16.3 |
| >99 employees | 7 | 1.0 | 951 | 8.9 |
| **Total** | **699** | **100.0** | **10704** | **100.0** |

Source: Istat, Industrial Census (1996)

The total value of shoe production is about 762 million Euro, close to 10 per cent of the total turnover of the Italian footwear industry. Over the years, Brenta's orientation towards the external market was increased from about 70 per cent of sales exported at the beginning of the 1980s to 88 per cent in 2000, which represents more than 10 per cent of total Italian exports in the sector (ACRIB 2001).

8 Census data are for Venice and Padua provinces and therefore include also enterprises not located in the district *Riviera del Brenta*.

## 3 The sample

In Brenta small firms represent the majority and the size distribution of our sample (total of 40 firms) reflects this situation. Nine firms (17.5 per cent of the total sample) have fewer than 20 employees, 18 of them (50 per cent) have between 20 and 49 workers, a further 9 employ between 50 and 99 people and only 4 companies (10 per cent) have more than 99 workers (Table 3.1).[9]

**Table 3.1 Size distribution of the sample**

| No of employees | No of firms | % |
|---|---|---|
| < 20 | 7 | 17.5 |
| 20–49 | 20 | 50.0 |
| 50–99 | 9 | 22.5 |
| > 99 | 4 | 10.0 |
| **Total** | **40** | **100.0** |

Source: author's survey

In the sample, small size is not related with age because, although 20 companies were established before 1970, 10 of them still have fewer than 50 employees. Furthermore, the age distribution of the sample reflects the evolution of the district, with only 4 companies created during the last decade.

Like other Italian shoe clusters, Brenta is therefore characterised by a predominance of firms, which in the past often chose to remain small, subcontracting out specialised phases of production, sometimes for fiscal reasons. Many of the sample firms are in fact outsourcing some of their production and this means that their capability is much greater than it could be expected from their dimension. Particularly as seen later, in recent years Brenta's firms have begun to outsource to Romania and other neighbouring countries, pressured by the need to reduce costs and by the increasing local scarcity of skilled labour. Firms in Brenta do not like to talk about this process of external relocation because they are worried about the possible negative impact on their image as top quality producers and, indeed, there are signs of decreasing quality.

Nevertheless, data about the number of pairs per worker clearly show that in several cases part of the production is not carried out inside the firm. For example in our sample among firms in the category of 20–49 employees, 6 produce less than 50 thousand pairs per year and other 6 produce between 50 and 100 thousand, 3 between 100 and 500 and one, more than 500 thousand pairs.[10] Thus, in our sample the number of pairs per capita produced yearly varies enormously, between a minimum of 750 and a maximum of 20,000. Moreover, as expected there is a strong (and statistically significant) negative

[9] The category of firms employing fewer than 20 employees is under-represented in respect to size distribution presented in Table 2.3. This is because smaller firms are under-represented in ACRIB. Most of these micro enterprises are subcontractors to larger local firms.

[10] Four firms belonging to this category did not declare how many pairs of shoes they produce yearly.

correlation (-0.595) between the number of pairs per worker and the price of shoes.[11] Nonetheless, the small firm size has recently become an obstacle to investments in marketing, branding and distribution, which are increasingly becoming crucial activities in the global footwear market. This will be explored in more detail below.

Output of the sample firms seems to have remained relatively stable: 45 per cent of the enterprises maintained more or less unchanged the number of shoes produced and the value of total sales over the years 1995–2000 and the export share is stable in 70 per cent of the sample. With regard to profits, the sample distribution is more varied: 30 per cent of the firms revealed stable profits during 1995–2000, 45 per cent decreasing profits and the remaining 25 per cent increasing returns (Table 3.2).

**Table 3.2 Performance indicators (% of sample firms)**

| During the last 5 years | Increased | Unchanged | Decreased |
|---|---|---|---|
| Number of pairs | 35.0 | 45.0 | 20.0 |
| Value of sales | 40.0 | 45.0 | 15.0 |
| Exports | 22.5 | 70.0 | 7.5 |
| Profits | 25.0 | 30.0 | 45.0 |
| Average price | 70.0 | 27.5 | 2.5 |
| Quality of product | 52.5 | 42.5 | 5.0 |
| Number of employees | 30.0 | 55.0 | 15.0 |

Source: author's survey

Finally in order to investigate upgrading strategies, we explored process and product innovations introduced by sample firms in 1995–2000. As regards process, 52.5 per cent of the sample firms introduced many innovations and 42.5 per cent some innovations (5 per cent do not innovate at all) (Table 3.3). In most cases (90 per cent of the sample firms), process innovation consisted mainly in introducing new, more advanced machinery while in 45 per cent of the sample there was also some reorganisation of the production process and/or management system. In 37 per cent of the sample there was also the introduction of quality control systems which in most cases means employing a technician in charge of this task.[12]

40 per cent of the sample introduced many product innovations and 52.5 per cent only some innovations (Table 3.3), namely improvement of quality (67 per cent), introduction of new product lines

[11] Both the Kendall coefficient and the Spearman rank correlation coefficient were calculated. They are the same in terms of statistically significant association and therefore only the Kendall coefficient is reported here as well as in the rest of the paper.

[12] Among Italian shoe firms the adoption of quality standard like ISO 9000 is extremely rare. According to the director of CIMAC, a technological institute in charge of the diffusion of quality standards in the footwear industry, in Italy there are about 50 certified firms and among them only about 20 produce leather shoes. In Brenta there are five certified enterprises.

(60 per cent) and export towards a new geographical area (50 per cent). Less frequently, sample firms have entered into a new segment of the market (22 per cent of the sample) or introduced a new brand (27 per cent).

**Table 3.3 Process and product innovation (no of firms)**

| | Process innovation | % of sample firms | Product innovation | % of sample firms |
|---|---|---|---|---|
| No innovation | 2 | 5.0 | 3 | 7.5 |
| Little innovation | 17 | 42.5 | 21 | 52.5 |
| A lot of innovation | 21 | 52.5 | 16 | 40.0 |
| **Total** | **40** | **100.0** | **40** | **100.0** |

Source: author's survey

After this first general presentation of the sample firms, the next sections analyse how and where they sell their products, identifying the main global value chains, discussing the issue of governance in each of them and differentiating enterprises belonging to diverse chains according to upgrading and performance.

## 4 The markets

According to some estimates (Pambianco 2000), the value of the world footwear market is around US $ 47 billion, 6 per cent of which is in the upper segment of the market, 9 per cent in the medium-high, 25 per cent in the medium and the remaining 60 per cent in the low-price segment. Therefore, the high and medium-high segments are worth about US $ 7 billion, 33 per cent of which corresponds to the market share of Italy (Table 4.1).

**Table 4.1 The world market for footwear (US $ billion)**

| Market segments | World market | % | Italian production | % | % Italian production in world market |
|---|---|---|---|---|---|
| High price | 3 | 6.0 | 1 | 14.0 | 33.0 |
| Medium-high price | 4 | 9.0 | 1.3 | 19.0 | 32.5 |
| Medium price | 12 | 25.0 | 2.8 | 40.0 | 23.0 |
| Low price | 28 | 60.0 | 1.9 | 27.0 | 7.0 |
| **Total** | **47** | **100.0** | **7** | **100.0** | **15.0** |

Source: Pambianco estimates available at www.pambianco.com

In *Riviera del Brenta* the main market has for long been Europe, particularly Germany, and to a more limited extent France, Great Britain and the rest of the EU. Among sample firms, 35 per cent sell between 50 and 90 per cent and 17.5 per cent more than 90 per cent of their production to Europe. Sales to Italy are less than 10 per cent for the majority of the sample (53 per cent of firms) and less than 50 per cent for another 23 per cent of firms.

In the European market, Brenta's companies are selling to a variety of customers. In the UK, typically to large buyers or department stores, in France and Italy mainly to independent retailers and in Germany to buying groups (see section 7).

Regarding the rest of the world, Brenta's market penetration is more difficult due to small size of local enterprises, geographical distances and large investments involved. Only 9 firms (23 per cent of the sample) export between 10 and 50 per cent of their production to the USA and 12 (30 per cent) to other countries, mainly in the Far East, Russia and the Middle East. It should be added that, although data are not yet available, exports to the USA have increased considerably during the last year, boosted by the weakness of the Euro.[13]

Nevertheless, based on our empirical findings and confirmed by key informers such as some members of the US National Shoe Retailers Association, Brenta's penetration in the US market is still very much dependent on volatile events, such as a favourable exchange rate. The strong potential of the largest market in the world is not thoroughly exploited by Brenta's enterprises. In our sample, only seven firms have some relationships with US buyers and none of them is trading a significant share of production through this channel of distribution. A more promising market is represented by the independent shoe retailers[14] and hoping to increase their market share principally in this segment, some Brenta' enterprises have recently opened a collective show room in New York (see section 9). However, small Brenta firms are running into difficulties in their recent attempt to build up strong and stable relationships with their US customers: first of all there is a linguistic barrier (about which US retailers strongly complain) and besides the opportunities of direct interaction are rare. On the other hand, US independent retailers, interviewed on occasion of an organised business trip to Brenta, expressed both their satisfaction with the high quality of *Riviera*'s shoes and their concerns that they would have to change suppliers if prices went up, in other words, if the dollar-Euro exchange rate became less favourable.

Even more volatile is Brenta's presence in the Far East, the Middle East and Russia, where local firms mainly sell to large buyers or export agents. A potentially important market is Japan, where however protectionism still represents an obstacle to further development.[15] Furthermore, the demand from other Asian countries, such as Hong Kong, is slowly recovering after the financial crisis in 1997, while Russia remains a very unpredictable market. Overall, none of the sample firms maintains really stable relationships with customers in these distant markets; many firms see them as opportunities to diversify their sales but none of them systematically invests in marketing.

Thus, it appears that sample firms are able to maintain many exit options, selling in many different geographical markets and to a large variety customers, such as independent retailers, department stores

[13] Personal communication with the director of the local entrepreneurial association (ACRIB).

[14] Total retail footwear sales in the USA in 1999 were $ 38.4 billion. The market share of the retail category is about 10 per cent of total sales (NSRA 2000).

[15] In Japan the tariff on imported shoes goes from 23.6 per cent to 41.3 per cent for leather footwear. In the EU it goes from 4.6 per cent to a maximum of 8 per cent.

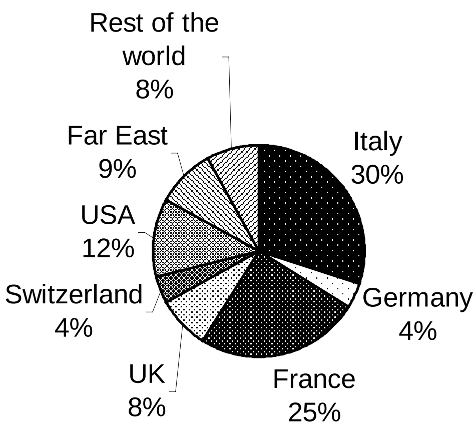
and large buyers. The only exceptions are 8 firms selling more than 50 per cent of their production to large buyers in the European market (7 in Europe and 1 in Italy). The ability to combine many customers is also confirmed by the limited amount of production sold by each firm to its two main customers (to whom on average sample firms sell only 16 per cent of their production)[16].

The above analysis of the main markets of Brenta has neglected a category of increasingly important customers for the district: the high fashion companies. Many firms in Brenta have recently begun to work as subcontractors to some leading global fashion firms. The next section analyses this value chain characterised by high fashion and global reach.

## 5 The top brand chain

The world market of luxury goods is estimated at about US $ 42 billion in 1999, 60 per cent of which corresponds to clothing and 8 per cent to footwear. In this rich and rapidly increasing market, the Italian market share is 30 per cent, followed by France with 25 per cent (Graphs 5.1 and 5.2).

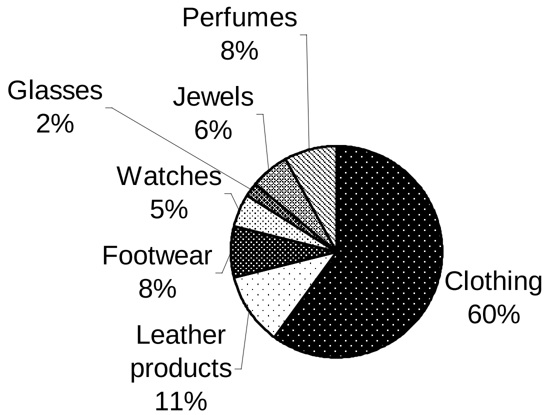
**Graph 5.1 The luxury-fashion world market (42 billion US $): main companies (%)**




Source: Pambianco estimates available at www.pambianco.com

[16] The origin of main customers is in 66 per cent of the sample firms Europe, in 11 per cent the USA, in 6 per cent Italy and in the remaining 17 per cent the rest of the world.

**Graph 5.2 The luxury-fashion world market (42 billion US $): main products (%)**




Source: Pambianco estimates available at www.pambianco.com

In recent years, the luxury fashion system went through important changes, turning it into an oligopoly dominated by a few multi-product giants. The growth strategy of many companies has been characterised by a similar pattern: first of all successful firms established their brand names in specific product lines (for example three among the most important and largest companies in the industry, LVMH, Gucci and Prada began producing and selling leather goods), then they capitalised on their brand names and diversified to other segments (in the cases named above, they entered into clothing, footwear, glasses, perfumes, wines) and finally, more recently, they have also begun to grow through the acquisitions of other well known existing brands.[17] During the last four years, mergers and acquisitions in the fashion industry have increased from 31 in 1997 to 59 in 1998, 122 in 1999, 158 in 2000 and 123 in the first 9 months of 2001, a total of 493 operations (Pambianco 2000).

The economic logic behind these growth strategies is a search for scale and scope economies in activities, over than manufacturing, such as branding, marketing, advertising, opening of mono-brand shops in the most exclusive and expensive streets in the world. The increasing concentration of fashion enterprises in the intangible phases of the value chain may be explained by the growing concentration of rents in these activities (Kaplinsky 2000). According to Kaplinsky (2000), in the past decade the barriers to entry in manufacturing have begun to fall and consequently the rent going to production activities has shrunk in favour of rents accruing to activities outside the area of production.

This explains the growing concentration of investments in areas like branding, advertising, marketing and sales where capital cost barriers to entry are high. Creating and maintaining a global brand is very

[17] An example, regarding acquisition of brand names, is Prada which recently acquired Church, a well known British footwear enterprise. The French group LVMH owns more than 50 brands in different industries: for example in the fashion industry names like Louis Vuitton, Dior, Kenzo, in the wine industry Moët, Krug, Dom Pérignon and in the distribution industry Le Bon Marché and E-luxury (e-commerce).

expensive and only those with access to international financial markets are able to afford it. Leading firms are therefore expanding through mergers and acquisitions, capitalising on their core competencies such as design, advertising, marketing, brand naming, which are no longer sector specific. This implies that we can consider the footwear or clothing industries as sub-systems of the global fashion system.

The rapid growth of the leading enterprises in the luxury industry is confirmed by the following examples: the second largest Italian firm in the top brand industry, Prada, has augmented the value of sales from about US $ 550 million in 1997 to 1 billion in 1999, an increase of 82 per cent in two years; Gucci, the largest one, has seen in the same period a more modest increase of 30 per cent. The net profits gained in the industry are also quite remarkable: in 1999 in Prada they reached 27 per cent of the value of sales, 16 per cent in Gucci and 10 per cent in LMVH (Table 5.1). Considering the top ten Italian enterprises in the top brand value chain, the results are slightly less astonishing but still very positive: the average rate of growth of the sale value from 1998 to 1999 was 35 per cent and in 1998 the average net profit was 14 per cent of total sales (Pambianco 2000).[18]

**Table 5.1 The performance of some top luxury-fashion companies operating in the footwear industry**

| | Value of sales (US $ million) | Share of world market % | Net profits (US $ million) | Net profits as % of sale value |
|---|---|---|---|---|
| LVMH (France) | 7900 | 13.2* | 790 | 10 |
| Gucci (Italy) | 1200 | 2.6 | 324 | 27 |
| Prada (Italy) | 1000 | 2.3 | 160 | 16 |
| Tod's (Italy) | 202 | 0.5 | 20 | 10 |

*From US $ 7.9 billion, the total value of sales of LVMH, wine, champagne and spirit sales have been deducted for a total of US $ 2.2 billion, to obtain LVMH share of world market in the luxury-fashion goods.

Source: Pambianco estimates available at www.pambianco.com

Connecting the top brand value chain with the literature we may refer back to Gereffi (1999) defining it as a sub-type of the 'buyer-driven' chain in which the lead firms are the owner of top global brands, controlling activities connected with intangible characteristics of the products such as design, brand name, marketing and distribution. Nevertheless, Gereffi's work is more focused on 'buyer-driven' chains '*in which large retailers, branded marketers, and branded manufacturers play the pivotal roles in setting up decentralized production networks in a variety of exporting countries, typically located in the Third World*' (Gereffi 1999: 41–42). Therefore, Gereffi also discusses the importance of the creation of brands but he is more concerned with global brands in mass markets, such as Liz Claiborne, Nike and Reebok. Dealing with top brands, barriers to

[18] According to an analysis of balance sheets of a sample of 60 Italian footwear enterprises from 1997 to 1998 the value of sales recorded a negative 3.5 per cent rate of growth and in 1998 the average net profit was a mere 1.6 per cent of total sales. The clothing sector (a sample of 285 firms) recorded better results, although not comparable with the leading enterprises in the luxury value chain: the rate of growth of sale value was 5.9 per cent and net profits in 1998 4 per cent (Pambianco 1999).

entry are higher, given the scarcity of world-known brand names and the high returns to branding and marketing in global markets. Therefore economic rents in this chain may supposed to be higher than in other types of chains (Kaplinsky 1998 and 2000).

Besides, our empirical findings presented in the next section show that, in the top brand chain, developed country producers (and not only developing countries as in many Gereffi studies) are affected by increasing power concentration. In the next section we analyse the rapid expansion of the top brand chain in Brenta, investigating the uneven relationship between local footwear producers and top global brand leaders.

## 6 Brenta in the top brand chain

In recent times the high and medium-high segments of the footwear industry have increasingly attracted the interest and the financial capital of well-known top brands and luxury multi-product oligopolies, mainly coming from outside the shoe world.[19] Some world top luxury companies looking for highly skilled manufacturing capabilities to begin footwear production, identified the *Riviera del Brenta* as a preferred area in which to find subcontractors. The beginning of this trend corresponded with a difficult time in Brenta, because local firms were facing the end of the positive impact on exports of the 1992 devaluation of the Lira.

Among our sample firms, 17 enterprises (corresponding to 42.5 per cent of the sample) work as subcontractors to high fashion companies, producing shoes sold with globally known top brands. In 5 cases (12.5 per cent), they work exclusively as subcontractors, while 4 of them (10 per cent) make between 50 and 89 per cent of their total production for high fashion companies and the remaining 8 (20 per cent) less than 50 per cent (Table 6.1).[20] According to our interviews, it appears that in many cases the amount of production made as subcontractors is still rather changeable, depending on seasons. Furthermore, some firms do not have direct contact with high fashion companies but rather they are subcontractors to other local enterprises, who are the direct subcontractors.

In most of the cases investigated, fashion companies provide the design and Brenta manufacturers take care of all production phases, including product development[21] and purchase of raw materials and components. After that, shoes are sold by fashion companies with their brand names. In our sample, design is totally in the hand of fashion companies in 65 per cent of the firms working as subcontractors, while 35 per cent of them contribute to design, often meaning that fashion companies give producers

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19 In Italy among the top ten companies in the luxury industry there is only one footwear firm: Tod's, ranking at the 9th position with a value of sales of US $ 202 million (Table 5.1), originated in Marche, the largest Italian footwear cluster and was recently listed at the Milan Stock Exchange.

20 According to the local entrepreneurial association, in 2000 the amount of production made by Brenta's enterprises as subcontractors to high fashion companies has reached 50 per cent of total production in the area (personal communication with the director of ACRIB). If these estimates are correct, in our sample subcontractors are underrepresented.

21 There is a distinction between creative and technical design; in the paper the former is simply called design while technical design, including size developing, is named product development.

some ideas and sketches to be transformed into a shoe.[22] Sales are undertaken by fashion companies in 82 per cent of the cases (Table 6.2) while product development and purchase of inputs are carried out in most of the cases by the subcontracting firms. Nevertheless, according to many firms interviewed, there is a trend of increasing involvement of fashion companies in these activities: increasingly they are directly selecting suppliers, sometimes even through acquisitions of firms, and extending their control on quality and delivery conditions backwards along the chain.

**Table 6.1 Production for high fashion companies among sample firms (%)**

| % on total production | No of enterprises | % on total sample |
|---|---|---|
| 0 | 23 | 57.5 |
| 1–49 | 8 | 20.0 |
| 50–89 | 4 | 10.0 |
| ≥90 | 5 | 12.5 |
| **Total** | **40** | **100.0** |

Source: author's survey

**Table 6.2 Internal functions in sample firms working as subcontractors to high fashion companies**

| No of sample firms* | Not undertaken | Partially undertaken | Totally internal |
|---|---|---|---|
| Design | 11 (65 %) | 4 (23 %) | 2 (12 %) |
| Product development | 2 (12 %) | 2 (12 %) | 13 (76 %) |
| Purchase of components | 1 (6 %) | 3 (18 %) | 13 (76 %) |
| Sale | 14 (82 %) | 2 (12 %) | 1 (6 %) |

*The total number of sample firms working as subcontractors is 17. In parenthesis there is the ratio on the total number of subcontracting enterprises in the sample.

Source: author's survey

From what has been said so far, it appears that Brenta has been undergoing a process of functional *downgrading*: traditionally the design and acquisition of inputs was controlled locally, and carried out inside the firms or inside the district; more recently, with the advent of the luxury fashion companies local enterprises are moving out of design and sale. There are also signs of luxury fashion companies extending their control backwards along the chain.

Integration in the luxury fashion value chain is thus causing a process of functional *downgrading* at district level in those activities, which are the typical core cross-sector competencies of luxury fashion companies, namely design, branding and sales.

22 In the rest of this section, the proportion of sample firms is intended as ratio of the 17 enterprises which work as subcontractors to high fashion companies.

Nevertheless, although Brenta is showing a trajectory of functional *downgrading* resulting from the integration in top brand chains, it has to be underlined that many of the leading companies in those chains are Italian. Therefore, moving from a narrow district perspective to take into consideration the evolution of the Italian fashion system as a whole, our conclusions may be very different. The Italian luxury goods industry is definitely undergoing a process of functional upgrading and concentration in rent-rich activities, being able to exploit cross-sector its core competencies in design, branding, marketing. This is very different from what is often occurring in developing countries. Small Brenta producers are abandoning some key activities which are moved to the headquarters of the chains' leaders in Milan, while in the case of the producers taking part in global chains in the developing world, these activities are never carried out within the country but rather they are set in New York, London or other cities in the developed world.

Apart from design, the functional downgrading occurring in Brenta concerns activities in which local enterprises, probably including most of the small Italian footwear firms, have traditionally been rather weak such as branding, marketing and sales strategy. In our sample, 60 per cent of firms do not perform any marketing at all and the existing brand names are sometimes recognised at national level (mainly in Germany) but never globally. A reason for the very limited local investments in these activities is the average size: firms are too small to afford very expensive strategies in marketing or advertising and to impose a brand name in the global market.

Local entrepreneurs are aware of their weaknesses and are beginning to accept that in the global market high production skills are no longer enough to sell their products; brand names and aggressive marketing strategies have become unavoidable competitive factors. Therefore, many of them agree that becoming subcontractors to luxury fashion companies is a way to face the challenge of globalisation, paying the cost of functional *downgrading*.

Nevertheless and quite unexpectedly, our empirical analysis shows that this choice is not at all an impoverishing strategy. In fact, Table 6.3 shows a statistically significant positive relationship between performance[23] and the share of production sold to high fashion companies. Furthermore, Table 6.4 confirms that during the last five years the share of firms mainly working as subcontractors and recording an increase in any of the observed performance indicators is higher than in rest of the sample. There is, of course, a problem of causality in interpreting these findings because it is impossible to know a priori whether positive performance is caused by participation in the luxury value chain or quite the reverse, high fashion companies select their subcontractors among better performing enterprises.

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[23] The index of performance is generated by attaching equal weights to each performance variable (see question 2 in the questionnaire to shoe enterprises in Appendix). The five possible values – from strong increase to strong decrease – were coded on a range of +2 to -2 respectively, with no change coded 0. The index for each firm was then constructed by adding up the actual values and dividing them by the number of variables. To test the robustness of this indicator, an alternative performance indicator was also obtained with a principal component analysis, estimated as a linear combination of the original variables. The correlation coefficient between the two indicators is 0.9 (significant at .01 level).

### Table 6.3 Kendall correlation coefficients [(a)]

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Performance | 1.000 | | | | | | |
| Product innovation | 0.104 | 1.000 | | | | | |
| Process innovation | 0.042 | 0.461** | 1.000 | | | | |
| Number of employees | 0.051 | 0.028 | 0.213 | 1.000 | | | |
| Ex-factory price | 0.319** | 0.142 | 0.068 | 0.126 | 1.000 | | |
| % of production as subcontrac-tor | 0.229* | 0.256* | 0.092 | 0.161 | 0.447** | 1.000 | |
| % of production sold to European buyers | -0.036 | -0.022 | -0.037 | -0.030 | -0.204 | 0.080 | 1.000 |
| | Perform-ance | Product innovation | Process innovation | Number of employees | Ex-factory price | % of production as subcontrac-tor | % of production sold to European buyers |

** correlation is significant at the .01 level; * correlation is significant at .05 level
[(a)] Some of the variables in this study (process and product innovation) are ordinal variables which can be ordered qualitatively in a limited number of ordered classes. Therefore, to analyse correlation we calculate Kendall coefficient which is the more appropriate for ordinal variables. However, alternative correlation measures, such as Spearman and Pearson coefficients, were also calculated and no differences in terms of statistically significant associations were found.

Source: author's survey

### Table 6.4 Performance among sample firms (number and % of firms recording an increase of performance indicators during the last five years)

| | Number of pairs | Value of sales | Exports | Profits | Average price | Quality of product | Number of employ-ees | Total |
|---|---|---|---|---|---|---|---|---|
| Firms mainly working as subcontractors* | 6<br>66.7% | 7<br>77.8% | 4<br>44.4% | 5<br>55.6% | 8<br>88.9% | 6<br>66.7% | 4<br>44.4% | 9<br>100% |
| Firms mainly selling to buyers** | 2<br>28.6% | 1<br>14.3% | 1<br>14.3% | 1<br>14.3% | 2<br>28.6% | 2<br>28.6% | 1<br>14.3% | 7<br>100% |
| Rest of the sample | 6<br>25.0% | 8<br>33.3% | 4<br>16.7% | 4<br>16.7% | 18<br>74.0% | 13<br>54.2% | 7<br>29.2% | 24<br>100% |

* Firms producing more than 50 % of their production as subcontractors to high fashion companies
** Firms selling more than 50 % of their production to buyers

Source: author's survey

In order to address the causality problem we tested the relationship between performance and production as subcontractors to top brand companies with OLS (ordinary least squares) regression analysis. Among the independent variables included (indicators of process and product innovation and number of employees) the amount of production as subcontractors is the only statistically significant variable explaining performance. Nevertheless, the cause-effect relationship remains unclear given that if the amount of production as subcontractors becomes the dependent variable, then the Beta coefficient of performance is the only statistically significant among regressors.

On the other hand, although our sample survey does not provide an empirical test of the hypothesis that performance is positively influenced by the participation in the luxury value chain, we may corroborate our argument looking into the economic theory of rent.[24] In fact, the extent of subcontracting shoes is derived from the demand of luxury shoes and given that final consumers are ready to pay a high price then top brand companies are also willing to pay a relatively high price to their high quality subcontractors, sharing with them (a small) part of their rent. In other words, our argument is that top brand companies are exploiting final consumers' willingness to pay very high prices for luxury goods earning a rent or a super-normal profit, above production costs. This rent is to some extent shared within the chain in order to guarantee high and consistent quality and respect of delivery conditions.

Moving on to upgrading, Table 6.3 shows that there is a positive and statistically significant relationship between the amount of production made for high fashion companies and the degree of product upgrading. This finding is confirmed in Table 6.5, showing that subcontracting firms introduce more product innovation than the rest of the sample. The role played by top brand companies in product innovation is confirmed by the fact that 60 per cent of sample firms stress the importance of their assistance in this field.

However, high fashion companies, which do not have specific skills in shoe production, are not assisting their subcontractors in process innovation, although their degree of upgrading is still better than the rest of the sample (Table 6.5).

Sample firms identify a number of advantages coming from their activity as subcontractors, among them the most important are: the size of orders (all firms except one), their regularity (all firms except two) and for 70 per cent of them the prestige of working for a world known top brand. A further advantage, very much emphasised by the interviewed firms, is the reduction of costs because they no longer have to produce a sample set. Among the disadvantages, imposition of delivery conditions and timing, lack of direct market access and the loss of independence are stressed by 75 per cent of sample firms.

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24 A summary of rent theory in the history of economic thought, with a particular focus on land, is presented in Camagni (1992).

**Table 6.5 Process and product innovations among sample firms**

| | Process | Innovation | | Product | Innovation | | |
|---|---|---|---|---|---|---|---|
| | **No innovation** | **Little innovation** | **A lot of innovation** | **No innovation** | **Little innovation** | **A lot of innovation** | **Total** |
| Firms mainly working as subcontrac-tors* | 1<br>11.1% | 1<br>11.1% | 7<br>77.8% | 1<br>11.1% | 2<br>22.2% | 6<br>66.7% | 9<br>100% |
| Firms mainly selling to buyers** | 1<br>14.3% | 4<br>57.1% | 2<br>28.6% | 1<br>14.3% | 5<br>71.4% | 1<br>14.3% | 7<br>100% |
| Rest of the sample | 0 | 12<br>50.0% | 12<br>50.0% | 1<br>4.2% | 14<br>58.3% | 9<br>37.5% | 24<br>100% |

* Firms producing more than 50% of their production as subcontractors to high fashion companies
** Firms selling more than 50% of their production to buyers

Source: author's survey

These disadvantages are strongly related to the issue of governance within the chain. Coordination of the value chain is clearly in the hands of top brand companies, keeping their control on *rent-rich* activities such as design, branding, marketing and also becoming directly involved in shoe and component production. Nevertheless, only two sample firms have clearly defined their relationship with high fashion companies as quasi-hierarchical, while the remaining ones reported that there is some degree of cooperation.

A clear assessment of how hierarchical these relationships are is a difficult task. There are mixed signs: in many cases firms are not fully dependent on the top brand value chain, producing less than 50 per cent of total production as subcontractors and in some cases they even contribute to design but, on the other hand, most of them suffer from functional *downgrading* and are loosing their direct link with the market; furthermore 75 per cent complain about dependence on high fashion companies.

We may conclude that the most common type of governance within this chain is somewhere in between network and quasi-hierarchy. The clear leaders in the chain are the top brand companies; definitely they are setting the rules that the rest of the actors have to comply with but in many cases they are also co-operating with their highly qualified partners to obtain top quality products and besides, very importantly, they are willing to share with them part of their rent in order to acquire their production skills.

The local entrepreneurial association is pushing Brenta firms to increase co-operation with high fashion companies, making themselves unavoidable partners and eventually acquiring licences.[25] The

[25] According to some sector experts, an alternative strategy to get into the luxury value chains could be to acquire licenses. This strategy was adopted in the 1970s by one of the leading Brenta firms and has been rather successful in the past. This firms owns seven licences of globally known brand names such as Yves Saint Laurent and Calvin Klein and it takes full care of their design and distribution. Nevertheless, there is a recent trend among fashion leaders to reacquire licences and for example it happened to this named firm that one of its licences was not renewed after many years. Furthermore, in 2001 45 per cent of the shares of this same enterprise were bought by the French group LVMH.

question is how long this strategy will be successful for because some high fashion companies are already setting up their own production facilities and others are beginning to decentralise production of more standardised shoes to Romania and other low-wage countries. Probably, for a long time they will need Brenta firms as subcontractors of top quality shoes but competition is tough within the district and Italy more generally. Following this strategy, Brenta firms may seek to build up a cooperative relationship with the chain's leaders, capitalising on their excellence in production but they may progressively lose their design capability and the direct market access.

To conclude, it is useful to summarise our main empirical findings in connection with our reference point on value chains (Gereffi 1999): first of all the top brand value chain confirms Gereffi's trend toward 'buyer-driven' chains. But there are also some novelties: producers from developed countries are involved in the chain and, their participation, far from having an upgrading effect, much stressed in Gereffi's work, has a functional downgrading effect. Nevertheless, although firms have abandoned some key functions, their performance is still very positive because they have the prospect of sharing with the chain's leaders, most of which are Italian, the high rents of the luxury industry.

## 7 Buying groups in Germany

Almost half of our sample sell more than 50 per cent of its total production to Europe, mainly to Germany. In Germany the shoe market is dominated by independent retailers, concentrating 74 per cent of total sales according to some estimates of the National German Shoe Retailers Association. However, most German retailers are organised in big buying groups, some of them associating more than one thousand shops and extending to other European countries, mainly Switzerland, Belgium and the Netherlands.[26]

At first sight therefore the German market seems to be dominated by buyer-driven chains but as we show in the rest of this section the buying groups' main purpose is not at all to drive the chains and establish 'quasi hierarchy' relationships with their suppliers but on the contrary to (a) facilitate market based relationships by reducing transaction costs (providing institution-based trust) (Zucker 1986) and (b) facilitate networks in which ties are information-rich.

Buying groups offer financial assistance to their members (the retailers): providing long and short-term credit for the retailers and guaranteeing their payments to suppliers. Furthermore, buying groups maintain direct contacts with shoe producers through their specialised buyers for different market segments visiting them at least twice a year, corresponding with the summer and winter sample sets.

There are usually two different forms of relationships with shoe producers: there is a network of authorised suppliers from whom retailers can purchase at agreed payment conditions, obtaining credit from the group and there are some footwear producers selling directly to the group, offering their own sample set to members. Therefore, retailers can choose to buy directly from producers or purchase from

[26] For instance among the buying groups we interviewed, one has a membership of more than 3000 shops in Europe (1500 in Germany) and another around 1900 shops.

the group and in both cases they receive credit if needed. Furthermore, the groups organise several events, outside official trade fairs, to present suppliers' sample sets and arrange meetings between retailers and producers. These events usually take place in different parts of Germany or neighbouring countries and are specialised for market segments and the producers' country of origin, for example there are specific exhibitions to present Italian shoes.

The largest buying groups have local branches in Italy, usually in Veneto or Tuscany, taking care of logistics and maintaining more frequent contacts with suppliers, sometimes implying quality controls during the production cycle and more often on finished products. Moreover, local branches deal with problems of returned products and after-sales service.

Among the buying groups interviewed, the largest ones operate in a variety of market segments, while two smaller groups are more specialised in the high and medium high ones.[27] In this segment, Italian producers are the main suppliers of all interviewed buying groups, although all of them said that German producers are recently regaining market shares. The increasing competition of German producers is explained by buyers in terms of improved design and better sales and after-sales services. In most cases, German shoe enterprises are very large firms, domestically manufacturing only a minor share of what they sell with their brand name and outsourcing the rest to producers outside Germany. They focus on design, branding, advertising and sale, offering a very varied sample set to satisfy different types of customers: from youngster and sport to classic and formal shoes. According to the buyers interviewed, they offer very good service, which means reliability in delivery timing and quality, rapidity in reassortment and after-sales assistance. As shown in the next section, these are areas in which Brenta producers are rather weak. Moreover, German producers have become very good at interpreting domestic tastes, maintaining intensive and fruitful contacts with their customers. According to Brenta producers, they also have a strong price advantage, because the distribution mark up on German shoes is half that on Italian shoes.

In conclusion, it may be useful to recall that in recent years demand for shoes in Germany and neighbouring countries has stagnated, which seems to have penalised the top market segments. In these segments, Italian producers have also encountered increasing competition from German firms. Therefore, Brenta's producers, traditionally exporting a very large share of their production to Germany, have been particularly hit by this situation. The next section analyses their relationships with German buying groups in more detail.

[27] In Germany, women's leather footwear of high and medium high price (more than US $ 80) represent less than 12 per cent of total sales (data presented by the German Shoe Retail Trade Association at press conference in GDS – International Shoe Fair – Düsseldorf, September 2000).

# 8 Brenta producers in the German value chain

In the medium-high and high segment of the German market, most imports come from Italy and particularly from *Riviera del Brenta* and Tuscany. The interviews showed that German buying groups are the key players operating in Brenta.[28] All of them have a large number of enterprises (an average of 200 firms) included in their list of approved suppliers, but stable relationships exist only with a minority of producers. On average each buyer interviewed maintains continuous relationships with around 20 firms located in Brenta.

The connection with the large majority of approved suppliers is a market based relationship with producers proposing their sample set and retailers buying directly from them on the basis of a standardised contract, agreed by manufacturers with the buying group.

Each buying group has preferred suppliers with whom competencies are shared. First of all, this includes information exchange, given that producers, retailers and buyers have many opportunities for meeting at special events organised by the buying groups; besides, buyers and some retailers often visit firms. In some cases there is collaboration between producers, buyers and retailers on design. Occasionally, shoes are sold with a brand name of the buying group or of an important retailer.

Nevertheless, German buyers complain because Brenta producers are not learning quickly how to take advantage of all information they could receive via communication networks. Most of the buying groups have in fact recently set up information networks linking some suppliers and shops which collect and provide instant sale information. Most of the German suppliers are connected and use this information to speed up delivery and offer reassortment. One of the buyers interviewed said that, among their 20 stable suppliers in Brenta, only one is connected to their network.

Low propensity to innovate among buying groups' suppliers in Brenta is confirmed by our empirical findings: sample firms selling more than 50 per cent to buyers appear in fact to be less innovative than the rest of the sample (Table 6.5). With regard to performance, results are also less positive than for the rest of the sample (Table 6.4).[29] Moreover, there is also a negative, although not statically significant, correlation, between price and the amount of production sold to buyers (Table 6.3). Indeed in Brenta firms strongly complain that they are unable to pass on increases in costs.

In our interviews we also asked buyers to evaluate the performance of their Brenta suppliers regarding product quality, innovative design, response time, punctual delivery and service.[30] As expected, firms in *Riviera* excel in design and are doing rather well in product quality; although, many buyers stressed that quality has recently been decreasing. This seems to be due to the relocation of production to other countries. In effect, given their average small size, firms are running into difficulties with quality control on the production made abroad.

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28 The buying groups interviewed were selected from a list provided by the local entrepreneurial association. Only one group of this list was not interviewed. The questionnaire used for interviews is presented in the Appendix.

29 Table 6.3 shows a negative, although not statistically significant, correlation coefficient between the performance indicator and the share of production sold to European buyers.

30 None of the buyers interviewed attributed any importance to quality standards, such as ISO 9000, as a factor of market competitiveness.

Increasingly, Brenta enterprises are using their internal production capacity to make shoes as subcontractors to high fashion companies and outsourcing abroad the rest of their production. Decentralisation to Romania and other neighbouring countries is a necessity for reducing costs, given that price competition is severe even in the high quality German market. In this respect, outsourcing may be interpreted as a strategy of functional upgrading of Brenta firms: moving low value added activities abroad and at home focusing on production for the rent-rich luxury market.

German buyers do not rate highly the reliability of delivery of their Brenta suppliers. They complain about delays and a too long response time from order to delivery.[31] In Brenta, the entrepreneurs interviewed give the responsibility of delays to their suppliers of components and raw materials who satisfy first their high fashion customers. According to our survey, this privilege is due to the different timing of production, with the luxury value chain anticipating the rest of the market and also, inevitably, to the stronger bargaining power of the top brand oligopolists in imposing their delivery conditions. This is therefore an area of potential conflict within the district between production for the luxury value chain and for the rest of the market.

The other weakness according to the German buyers is Brenta's service or rather the lack of it, meaning for instance after-sales service, reassortment and substitution of defective goods. On these aspects, Brenta enterprises are unable to compete with German producers, who invest many resources in these activities.

In light of the above, it appears that within the German value chain there are in most cases market transactions, but often with some cooperation between more or less equal partners sharing their competencies. Brenta enterprises maintain a high degree of independence because they may sell to several buying groups and within them to many retailers; in other words they maintain many exit options. Furthermore, there is no conflict on functional specialisation. Brenta manufacturers take care of the entire cycle from design to production and the buying groups of distribution and marketing. Cooperation is mainly aimed at improving product quality and some of the buyers want to intensify this cooperation. However, Brenta manufacturers sometimes see this desire of increasing cooperation in product development as a sort of intrusion on their creativity. This is very much in line with the findings by Schmitz and Knorringa (1999: 14): '… *the Italians are considered unwilling to learn from foreigners. A telling example was the reaction of an Italian company to a Brazilian consultant who had been asked by a buyer to investigate logistical and quality problems: the Italians were offended.*'

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31 This confirms empirical findings obtained by Schmitz and Knorringa (1999) who interviewed buyers from US, UK, The Netherlands and Denmark. According to their survey, Italian footwear producers in comparison with Brazilian ones were not performing very well in 'reliable product quality', 'speed of response', and 'punctual delivery'.

# 9 Local governance in Brenta

While Brenta never lived up to the romantic view of the Third Italy, much advertised in the past literature on industrial districts, it has nevertheless been traditionally characterised by strong local linkages at both a vertical and a horizontal level. As documented in a previous survey carried out in Brenta in 1992 (Rabellotti 1997), local shoe producers had intensive and co-operative linkages with their local suppliers and subcontractors and frequent informal contacts with other shoe firms in the district. Compared with Marche, another major footwear district analysed at that time, entrepreneurs in Brenta showed a more co-operative attitude, also attributing more importance to these informal relationships.

In addition to co-operative vertical and horizontal links among firms, Brenta is also characterised by the existence of several collective institutions: ACRIB, the local entrepreneurial association established more than 30 years ago; an export consortium (Consorzio Maestri Calzaturieri del Brenta), created in 1967 and a technological and training institute, named Consorzio Centro Veneto Calzaturiero, set up in 1986.[32]

Among many initiatives organised by these bodies, a significant example is the collective organisation at international fairs, managed by the Consorzio Maestri Calzaturieri, which has been held for many years. For example, at the September 2000 international shoe fair in Düsseldorf, 81 exhibiting producers from Brenta participated in a space collectively organised, with a common look and identified by the logo of the consortium.

Comparing local governance in the early 1990s with that at the turn of the century a significant change can be noted: links within the cluster have become less important and links with outside actors have become more important. In 2000, among the sample firms, only 25 per cent think that relationships with other local shoe enterprises are important, while the remaining 70 per cent attach no importance to them at all. Furthermore, during the most recent years, according to 30 per cent of sample firms, cooperation among shoe enterprises has decreased within the district. A better, but far from good, evaluation is given to the relationship with the local entrepreneurial association ACRIB, which is considered very important by 15 per cent of the enterprises, important by 37.5 per cent and unimportant by 40 per cent. Among local links, only relationships with suppliers[33] assume a real importance. They are very important for 65 per cent of sample firms and important for 15 per cent (Table 9.1).

Regarding the importance attributed to the reputation of the district, most of the sample firms believe that their main buyers and high fashion companies do not attach much importance to this aspect. This is confirmed by the interviews with German buyers, who did not select '*Made in Brenta*' nor '*Made in Italy*' among the main factors of competitiveness. As a matter of fact, the cluster has never made a real effort to promote its collective image, apart from joint participation at the fairs, and the '*Made in Italy*' factor is progressively losing its impact on the market because customers are looking more for individual

32 A detailed description of their main activities can be find in Rabellotti (1997).

33 Most of the suppliers of components are located in Brenta. Raw materials' suppliers are instead typically located in other clusters specialised in leather production. Finally with regard to machinery, production is concentrated in Vigevano, an old footwear cluster transformed in a mechanical district, but in Brenta there are usually local dealers with whom shoe firms interact (Rabellotti 1997).

top brands and because in many cases shoes are no longer made in Italy but in nearby low-wage countries.

In contrast, links with actors external to the cluster are considered increasingly crucial; particularly, relationships with main customers are regarded as very important by 65 per cent of the sample firms and important by 15 per cent and those with high fashion companies are very important for 70 per cent of the sample firms working as subcontractors and important for 13 per cent (Table 9.1).

**Table 9.1 Importance of linkages according to sample firms**

| | Very important (no of firms) | % of sample firms | Important (no of firms) | % of sample firms | Unimportant (no of firms) | % of sample firms | Missing no of firms |
|---|---|---|---|---|---|---|---|
| Suppliers | 26 | 65.0 | 12 | 30.0 | 2 | 5.0 | 0 |
| Shoe enterprises | 3 | 7.5 | 7 | 17.5 | 28 | 70.0 | 2 |
| ACRIB | 6 | 15.0 | 15 | 37.5 | 16 | 40.0 | 3 |
| Main customers | 26 | 65.0 | 6 | 15.0 | 4 | 10.0 | 4 |
| High fashion companies* | 12 | 70.0 | 2 | 13.0 | 3 | 17.0 | 0 |

*Sample firms working as subcontractors for high fashion companies are 17. The percentage is calculated on the 17 firms which answered the questionnaire.

Source: author's survey

In summary, external linkages have recently assumed a greater importance while relationships within the cluster have become less important, except for links with suppliers which remain crucial. Among the entrepreneurs interviewed there is a diffused feeling of disillusionment regarding local cooperation and the possibility of repositioning themselves in the world market through joint initiatives.[34]

Nevertheless, there are a few recent joint projects, among them the opening of a show room for 13 firms in New York, sponsored by ACRIB and funded at 50 per cent of its costs by public subsidies, is particularly successful. Boosted by the recent Euro devaluation, this initiative has been a real success for at least seven partners with more than 200 thousand pairs sold by the show room in its first year of activity, compared to an initial objective of 50 thousand. Following this successful experience there is now a new project to set up a trading company in joint venture with a local partner in Shanghai, to sell in the top segment of the Chinese market. This project should also receive a financial support from the Veneto regional government and from the Italian Ministry of External Trade.

[34] A similar result was found by Schmitz (1999) in the largest Brazilian shoe cluster, the Sinos Valley, where producers with the closest ties to global buyers were least interested in collective local initiatives.

Another project sponsored by ACRIB is the setting up of an electronic information network connecting shoe enterprises, suppliers of components, retailers and some local branches of banks. The e-commerce initiative, which is in a pilot phase, will be aimed at supplying business-to-business and business-to-consumer services. By 2002, ACRIB expects to be able to interact with its members mainly through this dedicated network.

Furthermore, there is a project[35] of the regional government, involving ACRIB and other local institutions to train immigrants from outside Europe, providing them also the essential services (i.e. housing, residence permits visas for their families) needed to facilitate their integration into the local community. This initiative addresses a crucial issue in Brenta where there is a structural shortage of skilled labour given that the district is located in a region characterised by full employment[36] and the footwear industry is not considered very appealing in terms of pay and working conditions. Easy availability of highly qualified workers was traditionally one of the main advantages of firms located in industrial districts like Brenta. Therefore, the difficulty in finding skilled workers is having a negative impact on the district, by increasing labour costs, decreasing flexibility and becoming an obstacle to further expansion. This is why local initiatives addressing this constraint are particularly important for the future of Brenta.

To conclude, there has been a change in the relative importance of local and global linkages. Vertically, there is the weakening of local linkages: backwards with subcontractors due to increasing decentralisation of production to Romania and other nearby countries and forwards due to increasing presence in the district of high fashion companies. Horizontally, there are a few collective initiatives promoted by ACRIB but, compared with the past, Brenta enterprises are investing more in their external linkages with buyers or high fashion companies than in local relationships.

## 10 Conclusions

This paper studies the impact of global transformations occurring in the fashion system on local competitiveness in one of the most important Italian shoe districts. This is done integrating the typical industrial district approach with the global value chain literature. Based on our empirical findings we address these main questions: Is globalisation pushing Brenta towards new value chains? What types of governance characterise the relationships between local and outside actors? Do the chains' leaders come from inside or outside the districts? Does the integration of industrial clusters in global value chains enhance or weaken local upgrading strategies? In this section we present the main conclusions.

1) In Brenta most of the shoe enterprises feed into a variety of chains. If we exclude from our sample, firms producing more than 50 per cent of their production as subcontractors of high fashion companies (22.5 per cent of the sample) and enterprises which sell more than 50 per cent of their

[35] This project is part of a local agreement ('*patto territoriale*'), an instrument of industrial and infrastructural policy at local level recently introduced in Italy and much implemented in the Southern regions.

[36] According to the last available population census (1991), in Brenta 96 per cent of the working population is employed.

production to large buyers (17.5 per cent) we are left with 60 per cent of firms combining several different chains. Therefore, our first conclusion is that in Brenta shoe enterprises often face several exit options, dependence on one value chain is limited to a reduced number of cases. This is likely to be a main difference between clusters in developed and developing countries (Humphrey and Schmitz 2000).

2) There are two main value chains operating in Brenta: the German and the top brand value chains. The former one has been working in Brenta for a long time, with Germany the main market of the district. The relationships within this chain are mainly market based linkages with some sharing of competencies between producers and their customers. Referring to Gereffi's definition of chains, the German chain cannot be defined as a buyer driven because buying groups are not 'setting the parameters' for manufacturers in the chain. The peculiarity of this chain is that buying groups, gathering together large numbers of independent retailers, are helping them to reduce transaction costs and risks and to improve information access.

3) The top brand value chain is a new comer in Brenta. Its increasing importance follows a global boom of luxury, branded goods in clothing, leather accessories, shoes, perfumes, etc. This is a cross-sector global value chain, characterised by very high entry barriers, given the costs of creating and maintaining a global brand. It can be defined as a sub-type of Gereffi's buyer-driven value chain, with some peculiarities.

4) To be part of the chain, Brenta's shoe producers accept a functional '*downgrading*', abandoning design and sales, which are the key competencies of the leaders of the chain, and focusing on production. Their relationships with top brand companies can be defined as somewhere in between network and quasi-hierarchy but it is clear that the leaders of the chain are not located in Brenta. This story draws attention to at least two new insights: not only upgrading but also downgrading can occur within global value chains and this may happen even to leading producers of developed countries.

5) An unexpected, very important finding is that subcontracting firms perform well, better than the rest of the sample and they are also upgrading more in terms of product and, somehow, also of process. This is explained by the availability of top brand companies to share some of their high rents with their skilful subcontractors.

6) Furthermore, although at district level a process of functional downgrading is clearly occurring, taking a more systemic perspective our conclusions are different. In fact, the Italian high fashion luxury industry as a whole is undergoing a process of functional upgrading and concentration of investments in rent-rich activities linked with intangible characteristics of the products. The global leaders in the chain exploit cross-industry economies of scale and scope in branding, marketing and advertising. Most of the global leaders of this value chain are Italian companies. Therefore, if Brenta as a district is experiencing functional downgrading, in the Italian fashion system there is, instead, occurring functional upgrading.

7) The integration of Brenta into the top brand value chain is causing conflicts within the district. First of all some producers use their internal production capacity to satisfy the demand of shoes coming

from high fashion companies and outsource, often to Romania, the production of their own sample set with a decrease in quality and secondly, suppliers of components first fulfil orders coming from the top brand chain, generating delays for the remaining firms in the cluster. Nonetheless, these changes occurring in the district can be also interpreted as a form of functional upgrading with Brenta enterprises moving the less profitable production for the German market abroad in order to use their internal capacity to satisfy the demand from the rent-rich top brand chain.

8) There are also conflicts arising between linkages within the district and outside it: comparing our findings with a previous survey in the early 1990s it is clear that Brenta enterprises are now attributing less importance to relationships with other local firms than before. Backward and forward local linkages are weakening while external linkages with buyers and top brand companies have recently assumed a major role.

9) The conclusion that can be drawn is that intangible activities are increasingly becoming the major assets in the top brand industry. In the past Italian industrial districts, such as Brenta, have built their excellence on a mix of skills in design, fashion and production but the small size of firms has limited their capability to face the massive investments required to control intangibles in the global market. These intangible activities have become the core competencies of a few large cross-industry companies dominating the top brand value chain, which is assuming a leading role in Brenta. Its expansion allows local footwear firms to continue exploiting their traditional comparative advantages of highly skilled producers, maintaining a good performance. Nevertheless, the top brand oligopolies with their huge profits and large financial capital availability are the global leaders of this segment of market. To date, it is not clear what this would mean for the future of Brenta. Local firms are winning a place in the rent-rich global top brand market but focusing only on their production skills they offer capabilities which can also be found in other clusters in the world and this may slowly erode their competitiveness and independence.

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