

**The long-term outlook for the Italian
economy/structural reforms**

The role of equity finance for firms' growth

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Italy's challenges in the midst of the euro-crisis, May 8th 2013
Bruegel and Dipartimento del Tesoro

A model that worked well until the mid nineties

- SMEs prevalent *in all sectors*
- Particularly fit in traditional sectors with medium-low technological content
 - Scale economies not very important
 - High productive efficiency, also thanks to localization externalities (industrial districts)
 - Exports; role for competitive devaluations

What has changed?

- Context, not endowments
 1. Globalization
 - New producers with low marginal costs
 2. Euro
 - End of competitive devaluations
 3. ICT
 - Lean manufacturing, global value chains:
codified knowledge

The “tertiarization” of manufacturing

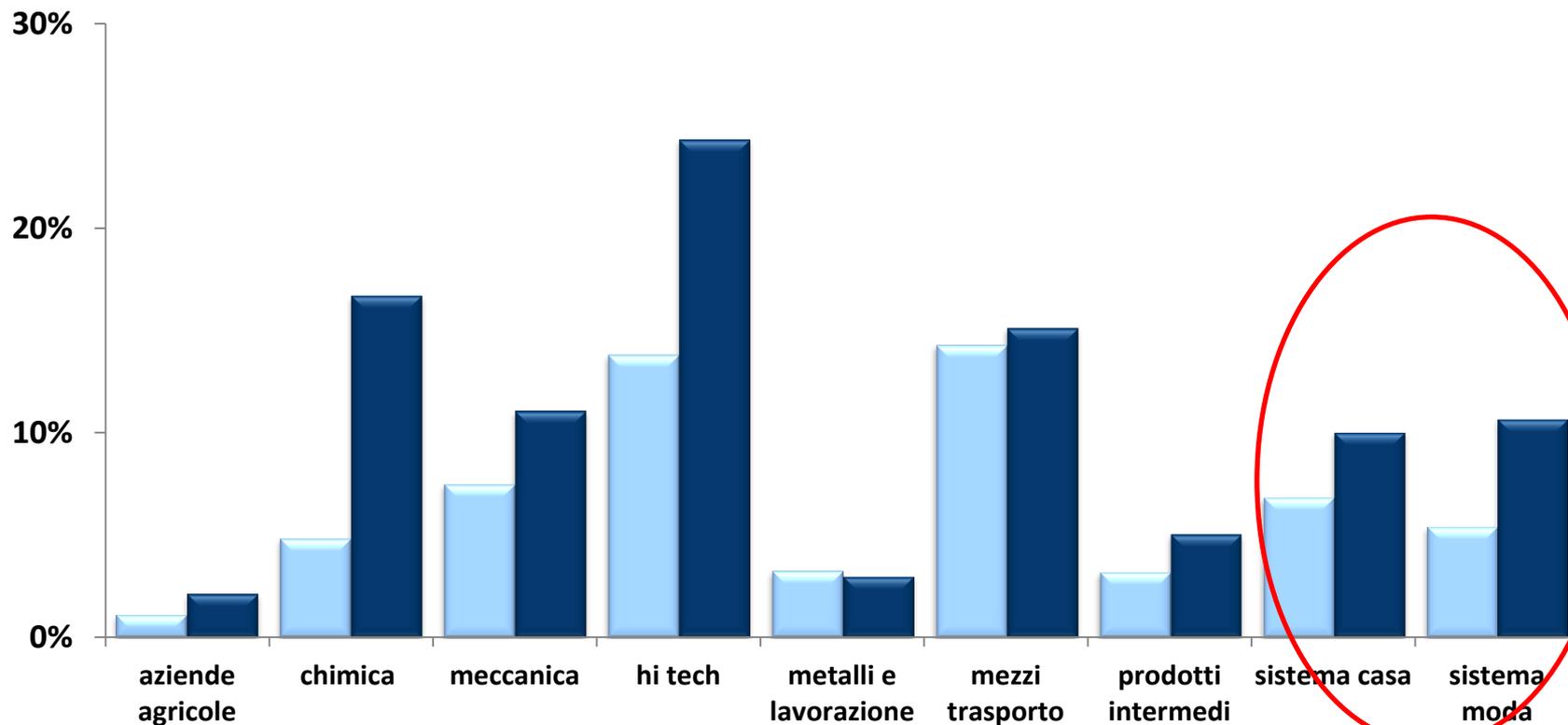
- Successful firms become more “services-like”:
 - Focus on phases before and after production: design, trademark, innovation, service, distribution network
 - This leads to differentiation of the product which reduce the elasticity of demand and allows firms to withstand the competition in international markets
- Role of **intangibles** – not only technological innovation

Role of intangibles in SMEs

Attivo immateriali su totale attivo, imprese con fatturato fra 2 e 50 milioni di euro

no crescita crescita

(2010 vs 2007)



Intangibles and firm size

- Intangibles: Fixed costs are increasingly important
- Companies with sufficient scale to invest in intangible capital
- “Enough with the "small is beautiful", we should realize that we must grow, be larger to withstand global competition, in order to make investments in technology, to enter new markets and afford to make mistakes, try again, wait ...”

Andrea Guerra, La Stampa, July 2° 2012

Corporate governance, finance and management

- Investments in intangibles:
 1. Are risky
 - Family entrepreneurs little diversified
 - Require equity
 2. Require specific managerial skills
 - Need for managerial contributions from outside the family
 3. Require significant financial resources
 - Size and capitalization
- Features too little present in our firms, still too centered on family-bank

Size

Quota di imprese che esportano per classe dimensionale

<i>Size Class</i>	AUT	FRA	GER	HUN	ITA	SPA	UK
10-19	69.8	44.7	45.7	58.0	65.4	51.2	54.9
20-49	63.8	59.1	65.4	64.7	73.3	63.5	62.8
50-249	88.6	75.4	78.2	79.3	86.6	76.2	76.8
more than 249	90.8	87.6	84.0	97.4	92.6	88.0	80.7
Total	72.6	57.9	63.4	67.3	72.2	61.1	64.0

Fonte: The Global Operations of European Firms, Navaretti Bugamelli Schivardi

- Exports would grow by 37% with German firm size distribution

Ownership and finance

Ownership and financial structure in 7 European countries, 2008

	AUT	FRA	GER	HUN	ITA	SPA	UK
Share of firms:							
<i>Foreign owned</i>	12.8	10.3	6.3	19.8	4.1	4.5	12.2
<i>With Venture capital in equity</i>	2.2	1.9	1.3	0.9	0.5	1.0	5.7
Share of bank debt over total liabilities	87.0	78.7	83.9	82.9	87.5	86.4	65.2

Source: The Global Operations of European Firms, Navaretti Bugamelli Schivardi

Ownership and control

Tavola 8 –Quota di imprese a proprietà e gestione familiare
(in percentuale)

	imprese di proprietà familiare	<i>solo imprese familiari:</i>	
		CEO di famiglia	management di famiglia
Francia	80,0	62,2	25,8
Germania	89,8	84,5	28,0
Italia	85,6	83,9	66,3
Spagna	83,0	79,6	35,5
Regno Unito	80,5	70,8	10,4

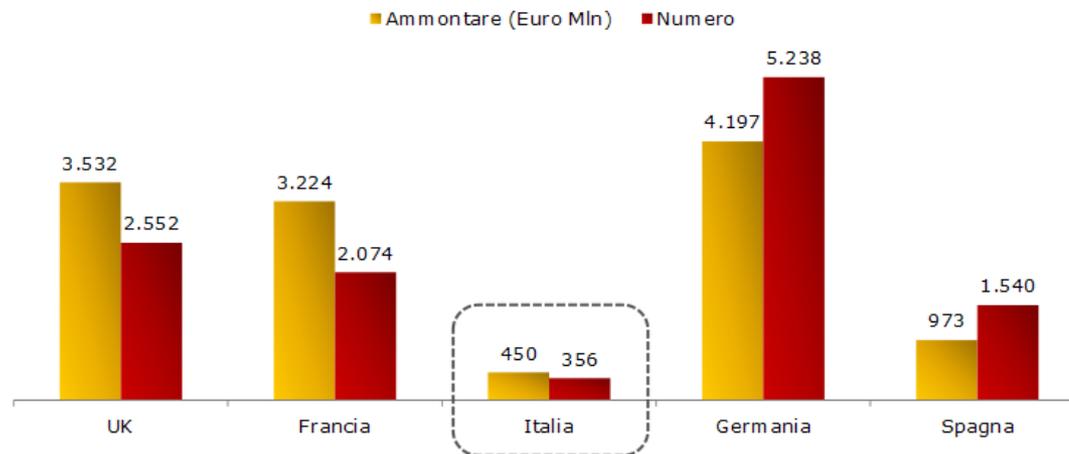
Fonte: Bugamelli et al, Banca d'Italia, su dati EFIGE

Challenge: Increase the supply of equity

- Italian firms still too dependent on bank debt
- Italy lags behind in the development of financial intermediaries specialized in offering equity-and external competences
- Forum «*idee per la crescita*»: a series of proposals to foster the development of such operators

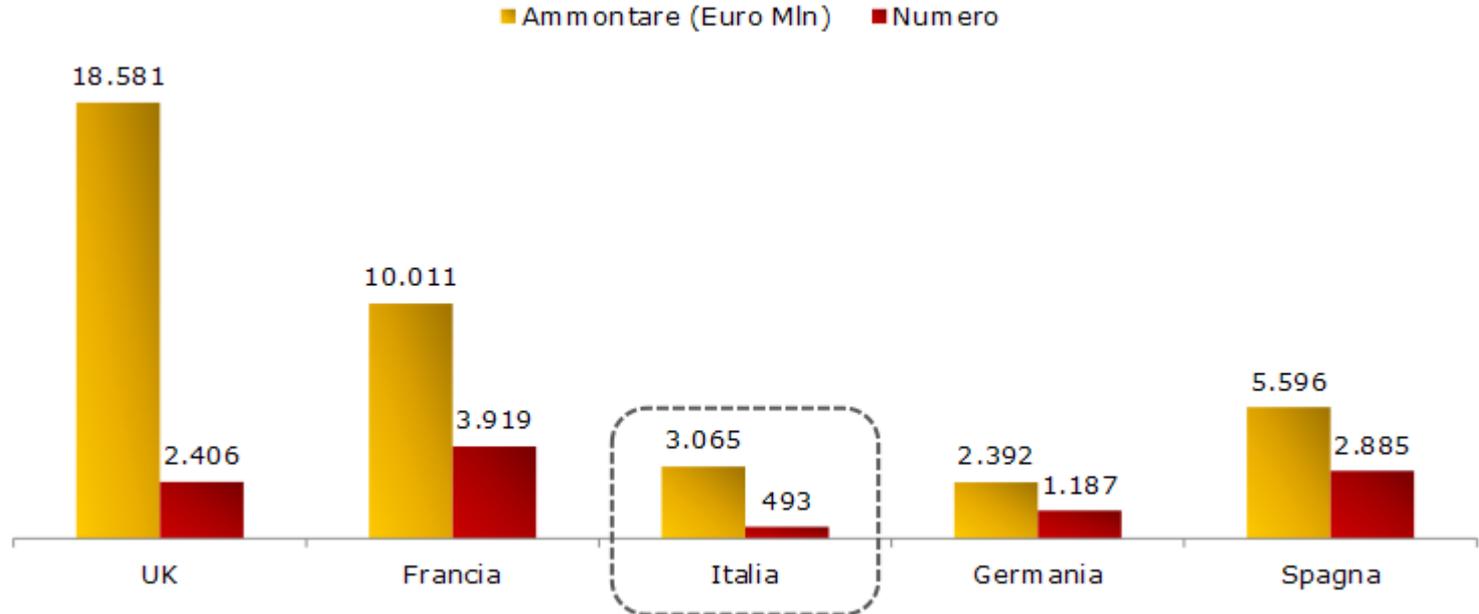
Early stage-VC

Early Stage Investments, 2007-2011

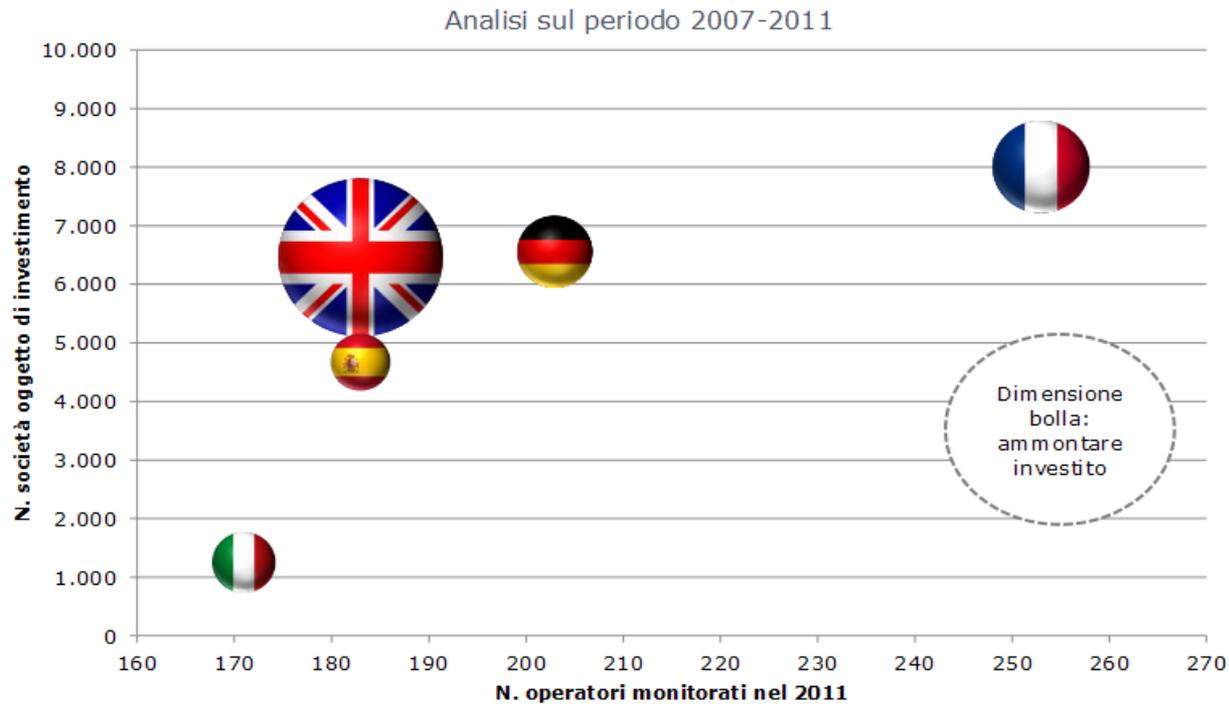


Espansions (small PE)

Expansions Investments, 2007-2011



LBO-Large PE deals



Problems of the «equity industry»

1. Fundraising
 2. Regulation
 3. Way out
 - Different relevance according to development stage
- Coordination failures
 - Room for intervention

1: Funds of funds for VC

- Coordination failures barrier to development of the industry
- Externalities in R&D, particularly for SMEs
- Funds also problematic
- Our proposal built around:
 - Investors and size – 100-150 m
 - Investment strategy: indirect
 - Professional management
- Similar to *Fondo Italiano Investimento*, different from *Fondo Strategico Italiano*
- Key: selection of projects made by VCs

2. Complete the reform for startups of Decreto Sviluppo 2.0

- Implementing decrees
- Further areas of intervention
 1. Eliminate tax discrimination between investors;
 2. Stimulate demand for innovation through acquisition of startups by large companies;
 3. Generate demand for innovation through the digitization of the Public Administration

3. Proportional regulation: European legislation

- Mid-market particularly important in Italy
- But regulation heavy for small operators
- Moreover, if not regulated, no access to subsidies
- Exploit European legislation:
 - EuVECA regulation (European venture capital funds)
 - Directive 2011/61/EC Alternative Investment Fund Managers
- Key not to increase the burden of regulation

4 Provide certainty on the tax treatment of LBO

- LBOs recognized by *civil code*, Art. 2501-bis, but their fiscal treatment still uncertain
- Serious problem for international operators
- Proposal: bidder can ask for a clearance from a civil court
- Fiscal authority can still question, but only after the ok from an ad hoc commission

5 Stimulate the demand for equity by companies

- Ace: make sure it is permanent
- Stock market: implement the suggestions of the working group on «*Semplificazione regolamentare del mercato finanziario*»
- Last, arguably more important but hard for policy: entrepreneurs must realize that it is in their interest to increase capitalization and to open up control and management

Redesigning the architecture of the financial system

- In general, still too based on banks
- Emerging consensus (even among bankers) that the system would benefit from being more balanced
- The crisis offers an opportunity to redesign
- We need operators that buy the new instruments

Redesign the architecture of the financial system

1. Pension funds – increase both the propensity to invest in equity and the size of subscriptions – inform citizens
2. Mutual funds – separate them from banks
3. Ownership structure of banks
 - Foundations should give up banks control