OECD Studies on SMEs and Entrepreneurship: Italy

Chapter 1

SME and entrepreneurship issues and policies in Italy: Assessment and recommendations

SME and entrepreneurship performance

Italy is a small business economy

SMEs and entrepreneurs are the backbone of the Italian economy. With nearly 100 enterprises per thousand people its business density is one of the highest among OECD countries. One-quarter of the working population is self-employed, the second-highest rate in the European Union (EU). Italian SMEs contribute 80% of national employment and 67% of value added, the third and fifth highest shares in the OECD area respectively. SMEs are also at the core of Italy's export and innovation performance, accounting for over 50% of the total volume of exports and 22% of business R&D investment. The share of firms that are young, with less than three years of age (14% of Italian enterprises), is in line with the most entrepreneurial OECD economies.

Signs of fragility in start-up and self-employment activity and in business survival rates

However, the overall business start-up rate in Italy is not particularly high. Data from the Global Entrepreneurship Monitor (GEM) indicate that the total entrepreneurship activity rate (the proportion of adults starting a nascent or young business less than three and a half years old) is below the OECD average. The proportion of gazelle firms (i.e. young fast-growing firms) is also lower in Italy than in many OECD economies, pointing to a paucity of high-impact entrepreneurship. Italy's business survival rate is relatively low, especially in the services sector where many firms start up in low value-added sectors where competition is driven by prices.

Furthermore, although the self-employment rate is high, this may be signalling a lack of alternative labour market opportunities; GEM data suggest that the proportion of Italians starting a business through necessity rather than opportunity is quite high (42% compared with an EU average of 27% in 2012). And a non-trivial share of self-employed people in Italy work full-time for only one employer, in what may frequently be a form of disguised employment rather than genuine entrepreneurship and favoured by incentives to employers to avoid a high tax wedge on labour. There is also evidence of untapped entrepreneurial potential. According to the Eurobarometer survey, while 44% of Italians say that they would prefer to be self-employed, only 27% consider self-employment to be a feasible career option, mainly because of lack of financial resources and adverse economic conditions. The gap between "preference for" and "feasibility of" self-employment is one of the highest across the EU.

A weighting of SMEs towards less productive micro- and small enterprises

The structure of the Italian business economy is also weighted towards less productive size bands. Approximately 95% of Italian SMEs are micro-firms with less than 10 employees, among the highest values in the OECD area, and another 4.5% are small firms with less than 50 employees. However, the productivity of Italian small and micro firms is both lower than firms in larger size bands and lower than their peers in several other key OECD economies. Aggregate productivity levels in the Italian economy are therefore penalised by under-performance in its micro- and small-sized enterprise sector, and a relative weighting of its enterprises to these smaller size bands. By contrast, Italian medium-sized companies (with 50-249 employees) perform extremely well on average in exports, innovation and productivity, but there are not enough of them; they make up only 0.5% of the total SME population.

Significant levels of informality

While measuring informality is difficult, the most optimistic estimates gauge the size of Italy's shadow economy at 16% of national GDP and 10% of employment, which are high by international standards. Large swathes of economic informality pose problems of an economic and social nature. Informal enterprises may seek to stay small in order to conceal parts of production from tax and labour inspection authorities and have relatively little incentive to invest in the modernisation of production. They thus tend to drag down employment and productivity growth. Furthermore, tax evasion implies unfair competition for other SMEs and entrepreneurs and foregone government revenues. Informality also engenders a segmented labour market where the rights of workers are unprotected.

Business ownership is common among all segments of the population, although business quality varies

Business ownership is relatively inclusive in Italy, as shown by comparatively high self-employment rates among youth, women, seniors and immigrants compared with other countries. For example, Italy's youth self-employment rate is twice as high as in the United Kingdom or the United States, and it has recently risen further in response to the dramatic increase in youth unemployment. To some extent this reflects difficult labour market conditions. However, it would be misleading to interpret self-employment by traditionally under-represented groups as only driven by the necessity to avoid unemployment. Italy's opportunity-driven Total Entrepreneurial Activity rate for women is one of the highest across the GEM-observed countries and reveals the desire of Italian women for greater flexibility in combining family and work time.

At the same time, women, youth and migrants run enterprises that are weaker in some respects than enterprises in general. For example, there is some evidence that Italy's women-owned enterprises are undercapitalised, partly due to discrimination in credit markets. Female entrepreneurs in Italy find it more difficult than male entrepreneurs to receive a bank loan and must deal with poorer loan terms and conditions when they obtain credit, even if their risk profile is the same as that of men. Foreign-born entrepreneurs are disadvantaged for other reasons. Immigrant entrepreneurs in Italy have lower levels of education than in many other OECD countries and tend to start low-impact firms generating little value and few jobs.

Key policy recommendations: SME and entrepreneurship performance

- Develop policies to increase the business start-up rate, the rate of high-impact entrepreneurship, and growth of the high-productivity medium-sized firm sector in Italy.
- Implement reforms to reduce the scale of informal economy activity.

- Ensure that people who are disadvantaged in the labour market (youth, women, seniors and migrants) are adequately represented among the recipients of mainstream government-funded entrepreneurship and SME support programmes, or develop bespoke programmes for these groups.

Business environment and framework conditions

Macroeconomic conditions have been difficult causing business closures and a credit crunch for SMEs

The 2008 global financial crisis and the 2011 sovereign debt crisis led to a double-dip recession in Italy which created adverse macroeconomic conditions for SMEs and entrepreneurship. Public debt ballooned, reaching 130% of GDP in 2013, and the interest rate spread between long-term Italian and German government bonds, an indicator of the relative ease of government borrowing underlain by perceptions of economic vulnerability, climbed to above 500 basis points in mid-2012, before dropping to under 200 basis points at the start of 2014.

The adverse conditions led to an increase in enterprise death rates and a contraction in enterprise birth rates, causing a loss of 63 000 firms between 2008 and 2010, a drop of 1.5% in Italy's total firm stock, and 610 000 job losses. Access to finance has also become more difficult. Italian banks, traditionally large holders of Italian sovereign bonds, have become more exposed to risk-rated assets, increasing their refinancing costs and making them less willing to lend to enterprises. Compared with other OECD countries, Italian SMEs are relatively under-capitalised and over-reliant on bank credit, making them particularly vulnerable to constrained bank lending.

Government anti-crisis measures to support SME finance

The government responded with a large-scale liquidity injection plan to help SMEs weather the crisis, involving four major measures:

- Italy's national credit guarantee system was enlarged and increased support provided to local SME loan guarantee associations; from 2009 to 2012, nearly 250 000 SME loans were guaranteed for a value of EUR 41.5 billion. Between 2012 and 2013, at a time when the sovereign debt crisis was at its peak, the number of firms eligible for a loan guarantee increased from 32 000 to 36 000 while the volume of guarantees increased from EUR 3.0 billion to EUR 4.3 billion.
- Rapid payment was authorised of EUR 47.2 billion of the public administration's commercial arrears to Italian businesses. By the end of November 2013, EUR 24.4 billion had been made available by the central government to debtor public institutions (nearly 90% of the total commitment) to enable them to make the repayments, of which 16.3 billion had been paid to creditors (two-thirds of the resources transferred).
- A series of debt moratoria were agreed between the Italian Banking Association, *Cofindustria* (the major Italian business association), SME associations and the Government in 2009, 2011, 2012 and 2013, enabling SMEs to postpone the repayment of their loan principals for up to a year. The most recent, signed in July 2013 and called "Agreement for Credit 2013", renews the measures of suspension of the payment of the loan principal until June 2014 for those firms that find it difficult to repay their loan due to a temporary downturn of sales caused by the recession.

- EUR 18 billion have been transferred since 2009 to the banking system through the operational arm of the *Cassa Depositi e Prestiti* (CDP) to support soft loans for SMEs.

These measures played a key role in supporting the liquidity and investment needs of SMEs and reducing the impact of the credit crunch on Italy.

Adjustments will be needed as economic recovery kicks in

Liquidity injection programmes are of exceptional nature and should be withdrawn when economic recovery is strong. The CDP-sponsored soft loans should be phased out as the SME loan market starts showing signs of vitality to prevent a flow of liquidity towards subprime loans. Similarly, the government should make an effort to implement the EU directive imposing a 30-day limit for most state payments, not only out of fairness towards business but also to avert the administrative complexities that have characterised the sudden payment of the first tranche of arrears worth EUR 20 billion in the first quarter of 2013.

The equity market remains weak

Italy's equity market is one of the smallest among the OECD economies as measured by venture capital investment as a percentage of GDP, and there are barriers on the demand as well as the supply side, reflecting a prevailing loan culture among SMEs and a reluctance of many family-owned firms to take in external ownership as well as limited numbers and values of venture and angel funds. The relative dependence on credit rather than equity affects investment and growth finance required by high-impact entrepreneurship and medium-sized firms in particular. The development of this market could be stimulated with tax measures to encourage private investors to invest in SME equity and improvements in contract enforcement procedures for SMEs and investors.

The regulatory environment is favourable to start-up

Italy has a relatively easy regulatory environment for business start-up, and performs very well compared to other OECD countries on time needed to establish a business, although the performance premium with other countries is less in terms of costs (taxes and fees) involved. Across all enterprise types, the number of days needed to set up a business activity is only 6 days compared to an OECD average of 12 days. In the case of sole proprietorships the business registration process is estimated to take only one day and EUR 35, while for limited companies the toll is two days and approximately EUR 2 000, 80% of the latter covering notary fees. The regulatory conditions for start-up have been improved for example by putting the business registration process online in 2010, and by the creation of special tax regimes for two new legal forms of business: the "Innovative Start-Up" and the "Simplified Limited Company", which both offer simplification and fiscal incentives for entrepreneurship.

Regulatory complexity and weak contract enforcement procedures hinder business growth

On the other hand, the regulatory environment surrounding enterprise expansion is less friendly. A complex system of tax breaks (e.g. differences across different categories of investment), tax penalties (e.g. differences across different types of work contracts) and tax deadlines (scattered throughout the year) render it difficult for businesses to unravel the tax code and anticipate how much will need to be paid at the end of the year. Such complexity represents a greater proportionate burden for SMEs than larger firms. In addition, although the overall corporate tax burden in Italy is in line with or below other large OECD countries, the social contributions paid by employers on labour costs are very high, representing 24% of labour costs in Italy, compared with an OECD average of 14%. High non-wage labour costs are likely to cramp SME expansion and favour the informal economy. Furthermore, limited competition in public utilities and significant regulatory and fee restrictions in some professional activities increase the operating costs faced by SMEs.

Weak contract enforcement procedures are also a barrier to SME investments and collaborations; it takes an average of over 1 200 days and 30% of the disputed amount to resolve a commercial dispute in Italy, compared with OECD averages of 510 days and 20%. This has been improving. For example, in 2012, steps were taken to streamline the civil justice system in order to facilitate the resolution of conflicts involving business contracts, including a geographical aggregation of courts, thematic specialisation of judges, and stricter rules on filing appeals. Since March 2011, a dispute between two companies or between a company and a consumer can also be settled outside of over-burdened courts through an administrative procedure called "mediation" managed by administrative bodies such as the chambers of commerce. In two-and-a-half years of operation, 220 000 disputes have been settled in this way, speeding up resolution and generating savings worth EUR 420 million for the companies involved. Furthermore, Italy has made encouraging strides in the area of intellectual property through the reform of its patent code in 2005 and introduction of a rapid conciliation procedure for firms wishing to enforce a trademark.

The outstanding regulatory issues affect inward foreign direct investors as well as domestic SMEs in a context of relatively low stocks of inward foreign direct investment (FDI) in Italy compared with other economies of similar (e.g. France) or even of smaller size (e.g. Spain and Sweden). This should be addressed in order to exploit the potential of SME participation in global value chains for accessing foreign markets and technologies. A "fast-track" lane and simplified regulations for foreign investors in relationships with Italian public administration would be helpful, as announced in the *Destinazione Italia* campaign.

Skills and training problems are affecting SMEs and entrepreneurship

Start-up activity and SME innovation in Italy are constrained by gaps in workforce and management skills. In terms of recruitment, the rate of hiring of university graduates into Italian SMEs is low, even though young higher education graduates in Italy are more likely to be unemployed than young people with only upper secondary education. This reflects both a mismatch between the university educational offer and labour market needs and a labour market in which many companies are locked into low-skill sectors and technologies. Recent data point to some moderate improvements – 17% of private sector recruitment is projected to concern high-skilled jobs, while university graduates are expected to fill 11.4% of anticipated new jobs – but employers continue to report difficulties filling high-skilled positions such as in engineering and software development. Training is not filling the gaps. Only 29% of Italian SMEs offer continuous vocational training, one of the lowest rates in the European Union. Only 5% of employees in microenterprises receive training in the workplace in Italy.

More investment and collaboration is needed in business innovation

Business innovation activity is relatively limited in Italy. For example, Italian manufacturing firms invest three times less in research and development (R&D) than their peers in Germany, France or the United States. Industry-university collaboration is also low, highlighted for example by a low proportion of industry-financed public R&D in Italy. An innovation culture needs to be built in Italian SMEs, and more incentives are needed for universities to engage with entrepreneurship, including increased emphasis on university spin-offs and consultancy to complement licensing and contract research.

Key policy recommendations: Business environment and framework conditions

- Phase out anti-crisis financial support to small businesses (e.g. the expanded Central Loan Guarantee Fund) when the economy is back on the path of full recovery, but do not allow late payments to accumulate.
- Introduce additional liberalisation and privatisation reforms, for example by reducing the size and scope of state-owned enterprises, including in public utilities, and the number of trades where entry is regulated by the grant of expensive licenses.
- Implement ongoing reforms aimed at streamlining the civil justice system in order to reduce contract enforcement costs and delays and simplify business taxation procedures, including alternative dispute resolution mechanisms for informal intellectual property protection.
- Reduce the tax wedge on labour and carry forward current labour market reforms to reduce the scale of informal business activity and ensure that self-employment is not used by employers to avoid a higher tax wedge on wage employment.
- Expand the SME equity market through tax concessions to equity investors and to firms that open themselves to external co-ownership and improving the legal system for resolving commercial conflicts involving external investors.
- Strengthen the link between formal education and the labour market by increasing employer engagement in the national vocational training system and improving the tertiary education offer for the skills most in demand by employers.
- Strengthen the incentives of universities to stimulate start-up enterprises and support SME innovation.
- Improve the attractiveness of Italy to FDI through special agreements and administrative "fast-track" lanes such as those foreseen in the *Destinazione Italia* initiative and making the business environment more friendly to foreign direct investors.

The strategic framework and delivery system for policy

The Statute of Enterprises and Annual SME Law provide a basis for prioritising policy actions

In Italy, entrepreneurship and SME policies are generally implemented by passing a specific law for each policy measure and establishing a related fund to be managed by the relevant Ministry. In 2011, the integration and coherence of this policy setting process was strengthened by the enactment of a Statute of Enterprises; a document that prioritises the ten principles of the EU Small Business Act (SBA) in terms of those that are the most relevant to Italy. It has set forward as major objectives a streamlined and transparent public administration, innovation, fair access to finance, and stimulation of formal inter-firm networks. To complement the Statute of Enterprises, it is proposed to pass an SME Law each year that will propose a series of programme actions for the year. It is important to ensure that the Annual Law is passed in practice. In addition, to favour implementation and help with prioritisation, indicative budgets should be established for the full set of actions implied by the Statute of Enterprises and the Annual SME Law.

The SME Envoy plays a key role in policy formulation

As in other European Union countries, the Italian government has appointed an SME Envoy who sits at the centre of a network of SME Envoys in each Italian region and maintains very close relations with chambers of commerce and business associations. The Envoy makes an important contribution to policy development by gathering of intelligence on policy requirements from the SME and entrepreneur perspectives, advocating the role of SMEs in the economy, encouraging impact evaluation of major programmes, and supporting co-ordination between national and regional actions. Increased emphasis on policy evaluation would nevertheless help strengthen the policy design process.

Business services are provided through a dense network of business associations, but gaps should be filled for start-up and under-represented entrepreneurs

The delivery of policies and programmes benefits from a dense system of well-funded chambers of commerce and business associations operating right across the country with large memberships and close links to SMEs and entrepreneurs. However, it is important to reach out in the delivery of business development services to enterprises and entrepreneurs that are not so well covered by existing services and business associations, in particular start-up entrepreneurs and people from social groups that are under-represented in entrepreneurship including women, youth, ethnic minorities and seniors.

Co-ordination, competition and capacity building should be strengthened in policy delivery

Further steps could also be taken to co-ordinate programmes and ensure some competition in service delivery by encouraging new suppliers to bid for training. Furthermore, new measures with respect to improving regulatory processes for SMEs imply training needs for those government officers and civil servants required to take on additional responsibilities.

A public agency or financial institution for SMEs and entrepreneurship could make an important contribution

Many countries have established a national SME agency or public financial institution to manage and co-ordinate public investments and support programmes for SMEs and entrepreneurs, involving recent institutions, such as the British Business Bank and BPI France as well as longer established institutions such as the US and Japanese SME agencies. Such an agency or financial institution could potentially play an important role in Italy by co-ordinating investments in and support for growth-oriented start-ups and SMEs.

Key policy recommendations: Strategic framework and delivery arrangements for policy

- Ensure that the proposed Annual SME Law is instituted and introduce a parallel budget allocation process to fund the implementation of policy actions advanced in the Annual SME Law and the Statute of Enterprises.
- Strengthen the evaluation of SME and entrepreneurship policies and programmes as an input into policy formulation.
- Consider the establishment of an SME agency or public financial institution responsible for co-ordinating investment and innovation support for medium-sized SMEs and high-impact entrepreneurship.

- Reach out to nascent entrepreneurs and entrepreneurs from under-represented populations, including firms of very small size and entrepreneurs that are not members of any specific business association, by communicating through appropriate channels on regulations and available programme support and by developing accessible programmes tailored to these groups.
- Develop a training programme to support public officials charged with implementation of foreseen regulatory simplification measures for SMEs.
- Strengthen co-ordination in the delivery of SME and entrepreneurship policy, drawing on the institutional role of the SME Envoy.
- Increase competition in the delivery of business support services by encouraging new suppliers to bid for contracts to deliver public programmes.

National SME and entrepreneurship programmes

Italy has a well -functioning central credit guarantee system

Italy has one of the largest credit guarantee systems among OECD countries, resting on a very strong Central Guarantee Fund (CGF). As well as the counter-cyclical role it took on in the crisis the CGF plays a long-term structural role in the economy enabling many SMEs and new firms to obtain credit that they could not otherwise obtain because of lack of collateral. In future, the Government proposes to create special sections in the CGF that will target specific categories of entrepreneurs or investment projects (i.e. SME internationalisation, innovative start-ups and women entrepreneurs), and this will be very helpful in the sorts of start-up entrepreneurship, high impact entrepreneurship and development of medium-sized enterprises that are required to strengthen Italy's SME economy.

The local loan guarantee associations network shows signs of fragility

Italy also has a broad network of local loan guarantee associations (*Confidi*), which are generally endorsed by the local branches of national business associations and sometimes supported by the CGF. The system is well adapted to the strength and tradition of the Italian banking sector and the importance of local co-operation amongst entrepreneurs at local level, and has been instrumental in enabling SMEs with limited relationships with banks to obtain credit at better terms and conditions than would otherwise be possible. However, approximately one-half of *Confidi* registered losses in 2011 and requires shoring up. The system could be strengthened by encouraging the merger of the smallest *Confidi,* or their aggregation in consortia (offering the advantages of more professional management, cross-subsidisation strategies and reduced exposure to sector or local slowdowns), and by providing training to their managers. It would also be sensible to keep a sizeable proportion of CGF support to *Confidi* in the form of direct guarantees to banks rather than weighting the Fund overly towards counter-guarantees to the local associations, which would require them to take more of the risk.

New programmes are encouraging the equity market, but they lack scale

Certain national programme measures have been taken to boost Italy's equity market. The Italian Stock Market's Elite programme is an investment-readiness initiative that prepares firms with growth potential to receive equity finance in the near future and be ready for an Initial Public Offering (IPO). The Italian Investment Fund (*Fondo Italiano*), endowed with EUR 1.2 billion, targets growth-oriented medium-sized Italian firms either directly or indirectly through participation in funds of funds. These initiatives are noteworthy but of small scale. A common approach to buttressing equity markets in many countries is the concession of tax breaks to investors and there is a good case to relax Italy's rules on tax breaks for equity investment, including business angel investment. Managed funds listed on the public stock market could also be promoted, through which informal investors could buy and sell shares in unlisted SMEs, stimulated by tax incentives such as exemptions from capital gain tax on disposal of shares.

Italy has introduced measures to support R&D

Italy has established a range of innovation funds which give a combination of tax breaks, grants and soft loans for business R&D and university applied research. Examples include the Concessional Research Fund (*Fondo Agevolazioni Ricerca*), which provides tax breaks to firms contracting university research, and the National Innovation Fund, which finances projects based on the exploitation of industrial designs. Business R&D has also been favoured by the new Innovative Start-Ups programme. This scheme provides a favourable treatment in terms of taxation and employment relations to young R&D-based firms, which become eligible if they meet one of the following three conditions: i) at least 20% of turnover is re-invested in R&D; ii) at least one-third of staff members hold a Ph.D. degree; iii) they hold or have licensed a patent. By the end of September 2013, nearly 1 200 new businesses had registered as innovative start-ups.

Complementary measures are needed for innovation

However, the existing approach to innovation support is biased towards R&D and technology, and more could be done both for commercialisation of research outputs and for non-technological innovation in firms. For example, research commercialisation could be promoted by creating co-operative research centres or consortia where staff members of universities and private sector companies work together on joint product development, or by tying part of university research grants to the commercialisation of research. For non-technological innovation, the target group of the Innovative Start-Up programme could be widened, and other forms of innovation such as marketing and organisational innovation could find better support. Consultancy could also be subsidised for innovation in services.

SME exports are promoted, but the scale has dropped

Italy offers a full range of export promotion programmes for SMEs covering export credits, export guarantees and insurances, grants and soft loans for market feasibility studies and promotional activities, coaching and matchmaking services, etc., through support organisations such as the External Trade Agency (*Istituto Commercio Estero*), technical agencies such as SACE and SIMEST and the chambers of commerce. While these programmes have tended to focus on larger SMEs, the government and chambers of commerce have also recently launched the World Pass network of one-stop shops to help the smallest SMEs to obtain information about opportunities in international markets, foreign legislation, import-export regulations, etc. Recently, Italy launched a National Export Plan for 2013-15 calling for more coordination among the export support agencies, higher prioritisation in targeted markets and sectors, greater involvement of southern Italy's firms in export activities, and the creation of a new Bank for Exports. However, although the Plan favours rationalisation its measures are likely to require more resources than those currently made available. For example, the External Trade Agency's budget was more than halved in 2012 from an average of EUR 80 million per year in the period 2008-10 to EUR 30 million in 2012, while other programmes have very small budget outlays (e.g. export consortia measures).

Entrepreneurship education should be better mainstreamed in school and college curricula

Only 30% of Italians believe they have the right set of skills and experience to be able to start a business, compared for example to 56% in the United States and 47% in the United Kingdom. In addition, a lower-than-average share of Italians has taken entrepreneurship-related courses in schools or university, 17% of Italians as against 23% on average in the EU27. Only 40% of Italians participating in the GEM survey reported that schools have helped them develop entrepreneurial attitudes; the second-lowest value across OECD countries.

Italy would benefit from stronger attention to entrepreneurship education at school, vocational training and higher education levels. A number of noteworthy initiatives already exist, either run by semi-public (e.g. the Union of the Chambers of Commerce) or not-for-profit organisations (e.g. Junior Achievement), but they are loosely coordinated and of insufficient scale to address the full population.

A clear national strategy for entrepreneurship education, which sets out objectives, indicators, incentives and rewards, would help recognise the importance of entrepreneurship education in society and create appropriate activities and infrastructures. The approach should include measures to motivate and train future entrepreneurship teachers, for example by giving special signs of financial or immaterial recognition, and to collaborate intensively with the private sector, because of the practical and experiential nature of entrepreneurship education compared to other disciplines.

SME workforce training increased dramatically with establishment of Industry Training Funds, but participation of smaller SMEs is limited

With a budget of EUR 450 million in 2012, the Industry Training Funds (ITFs), or *Fondi Paritetici Interprofessionali*, are Italy's main workforce training policy, although the European Social Fund (ESF) is also a big player by financing EUR 400 million of training activities at firm level. Established in 2004, ITFs are jointly managed by the main national business associations and trade unions. They are financed by a 0.3% compulsory levy on total wage costs, which has laid the ITFs open to the criticism of adding to non-wage labour costs. However, since their introduction the number of SMEs offering training to their workers has increased dramatically. Whereas in 2005 only 32% of enterprises with more than 10 employees offered training to their employees, the percentage had nearly doubled to 56% in 2010. Unfortunately, smaller SMEs are less than proportionally represented among ITF users and those smaller SMEs that do participate tend to choose more traditional types of training. Potential revisions to the programme should be considered to encourage greater and better participation by smaller SMEs, for example through the use of training vouchers.

The apprenticeship system needs some adjustments

The Italian apprenticeship system has been reformed on several occasions during the last 15 years. Today's approach is based on a three-year programme in which work-based training is combined with a maximum of 120 hours of theoretical training and classroom activities delivered by a private training agency. However, apprenticeship contracts have sometimes been used by SMEs as a form of cheap labour rather than as a genuine attempt to build the skills and competences of tomorrow's labour force. This abuse has been facilitated by the lack of national standards regarding the contents and quality of apprenticeship training and an insufficient system of monitoring, supervision and quality controls. In an effort to strengthen the quality of apprenticeship, the government has introduced stricter quantitative criteria on the minimum and maximum duration of apprenticeship, number of apprentices per company, and minimum retention rate of apprentices. Further national standards for the apprenticeship training system should be introduced, including arrangements for the examination and authorisation of training companies and trainers, the establishment of institutions for monitoring and supervising apprenticeship training at regional level, and the creation of a central organisation for the final examination of apprentices.

A few firms benefit from intensive support for SME management but additional low-cost programmes are needed to reach out to more firms

A wide range of effective consulting, business development services and management training programmes are offered by local chambers of commerce. However, these programmes tend to provide intensive and high-cost support to a select group of SMEs and start-ups with the greatest development potential and the number of firms that can benefit from these programmes is small given the high costs of face-to-face provision. A priority should be to expand the proportion of SMEs that benefit by complementing existing intensive support with lower-cost solutions. An online business diagnostic tool, hosted by the website of the chambers of commerce, could reach a larger number of SMEs with a free and quick analysis of their strategies and operating practices, and could offer links into further subsidised or non-subsidised management training, mentoring and consultancy support. The use of volunteer mentors could also be expanded.

There are further opportunities for SME development through public procurement

Important steps have been taken to improve SME finance by tackling a tradition of late payments by the public sector. However, SMEs do not participate as much in public procurement contracts in Italy as would be expected from their share of sales in the economy as a whole. Various actions could be developed to address this such as subdivision of contracts into smaller lots, an online tool to publicise procurement opportunities and provision of guidance and training to SMEs in successful tendering.

Support for social target groups could be scaled up

Italy is a leader in public programmes for women entrepreneurs although there are some opportunities for renewal of the institutional framework of support for this under-represented group of entrepreneurs. At the same time there is considerable scope to upscale existing rather rare and fragmented support for other social target groups, in particular youth, immigrants and ethnic minorities and seniors. Many of the finance and training barriers faced by social enterprises are not yet adequately addressed by public programmes implying the opportunity for a comprehensive national programme for social enterprises promotion to complement recent reforms of the legal status of social enterprises.

Italy's corporate social responsibility strategy is also a force for SME upgrading

Italy's National Action Plan on Corporate Social Responsibility (CSR) 2012-14 stresses the importance of CSR processes within the business strategies of all sizes of enterprises, including SMEs, and especially internationalised SMEs with foreign operations or roles in global value chains. With a common approach at national and regional levels, the plan includes fiscal incentives for employment of people from disadvantaged groups, reduction of negative environmental impacts, and improvement of the work-life balance of employees, together with guidance and best practice exchange measures and consultancy and training for workforces and management in CSR processes. The focus is not only on individual SMEs but also on SME networks and SMEs in supply chains. The CSR strategy is therefore helping to improve the competitiveness of SMEs as well as their social impacts, and does not just concern large firms. Many policy initiatives are underway in this area at national and regional levels and those that prove the most effective may usefully be extended.

Key policy recommendations: National programmes

- Increase value for money from the Credit Guarantee Fund by capping lender default payments, allowing borrowers to post personal guarantees, and permitting larger firms to participate in the scheme. Set limits to the total volume of counter-guarantees to local mutual guarantee associations to reduce potential moral hazard and systemic risk problems.
- Strengthen the viability of the *Confidi* by encouraging mergers and the creation of consortia and offering training and good practice exchange to increase management capabilities.
- Broaden the financial instruments for high-impact entrepreneurship and medium-sized firms by opening up the mini-bond market to non-professional investors, expanding tax breaks for mini-bond and business angel investors, supporting a dedicated small caps or accelerator programme, considering an initiative to facilitate indirect investment by informal investors in SME equity on the Italian stock market through managed funds, and offering financial education programmes for entrepreneurs and SME managers.
- Introduce new initiatives to favour collaboration between universities, SMEs and entrepreneurs, for example through mentoring of potential academic entrepreneurs, dedicated seed funding for early-stage commercialisation of research, funding for co-operative research centres for staff of universities and enterprises, and a major national programme for joint research between universities and small collections of related SMEs.
- Develop information, education and training programmes to support entrepreneurs and SME owners to manage their intellectual assets, and extend current innovation policy support to promote other types of intellectual property in addition to patenting.
- Amend the criteria for obtaining tax breaks under the "innovative start-up legislation" to reward firms generating innovation outputs, rather than using technology inputs (R&D, PhD staff and patents), and including non-technological innovation.
- Streamline and prioritise the system of support for SME exports based on comprehensive review of existing initiatives, ensuring that adequate resources are provided to the most effective actions. Favour the development of networks of SMEs for the purposes of collaboration on exporting to new markets. Offer advice and training to SME managers and workers aimed at better exploiting export opportunities in areas such as foreign language skills and supply chain and operations management, including by encouraging banks to play a more proactive role in assisting entrepreneurs and SMEs with exports. Develop infrastructure, awareness and training programmes to promote e-commerce among SMEs.

- Develop a national strategy and action plan to promote entrepreneurship education at all levels (schools, vocational training, and higher education institutions) and to incentivise education institutions to offer entrepreneurship support. Accompany this with a promotional campaign to create awareness towards entrepreneurship and new business creation in the general population.
- Integrate components of a dual apprenticeship system into vocational education. This includes industry- and nation-wide standards for training, formal labour contracts with apprentices, formal centralised examinations, and proper quality assurance mechanisms.
- Expand company-based apprenticeship training schemes by increasing their quality, and hence their attractiveness to businesses and young people, by further development of national standards on the contents and methods of training and improved arrangements for authorisation of training companies and tutors, monitoring and supervising the training, and central organisation of apprentices' final examinations.
- Revamp existing workforce training measures, including the Industry Training Funds, so that they can better respond to the relatively limited organisational capabilities and budgets of SMEs with respect to training by increasing SME awareness of available public training programmes, introducing a simplified procedure for SME applications to ITF courses, encouraging training for networks of SMEs, and making more use of training vouchers for SMEs.
- Introduce a national programme to encourage the recruitment of graduates by SMEs, such as through specific goal-oriented internships for university students in SMEs supervised by university teachers and researchers as part of their degrees, which may lead to subsequent hiring at the same time as promoting SME innovation directly.
- Expand the reach of public management support to more SMEs by developing low cost solutions including a comprehensive system of enterprise diagnostic self-assessment health checks, the use of retired professionals as mentors and advisors, and peer-to-peer learning activities such as a national company visit programme to discuss best management practices.
- Create an online portal providing signposting to all public management support measures available at different levels of government and across different public institutions, together with tailored search facilities which allow SMEs to easily identify appropriate support across different stages of the life-cycle of a company.
- Increase the participation of SMEs in public procurement contracts by increasing the subdivision of contracts into lots, increasing the visibility of public contracts to SMEs, for example with an online search tool, offering basic online guidance and training to SMEs in winning contracts, and organising "meet the buyer" events to match SMEs with public agencies with potential contracts.
- Pilot test and scale up promising new initiatives for female, youth, ethnic minority and senior entrepreneurship. Broaden the support by placing a stronger accent on business training and coaching in addition to offering financing, encourage programme participants to develop more growth and innovation-oriented business projects, and facilitate and support intergenerational business succession.
- Increase programme support for social enterprises by increasing awareness of the economic and social contribution of the sector, adapting the fiscal regime to provide suitable incentives to social enterprise activity, developing new measures for social

enterprise finance, such as fiscal incentives for investors, adapting existing business development services to facilitate access by social enterprises to regular support and offer certain tailored services such as training, mentoring and social enterprise incubators, and making public procurement contracts more open to social enterprises through better use of social clauses.

- Set up a comprehensive evaluation framework for regular and rigorous evaluations of SME and entrepreneurship support programmes to determine their effectiveness and ways they can be improved, including guidance on the regularity, scope and methods of evaluation to be used.

The local dimension of SME and entrepreneurship policy

Entrepreneurship and SME performance is weaker in the lagging South

Italy is one of the OECD countries with the largest income inequalities across regions, twice as high as countries such as Spain, Germany, Japan and the United Kingdom. Regional disparities are also a feature of entrepreneurship and SME performance. Both business density (number of enterprises per thousand population) and business demography indicators (enterprise birth and death rates) are typically lower in the south than in the north. On average, southern firms are also smaller, less profitable, less export-oriented and less technology-based than those in the north. However, southern regions are not homogenous and some do better than others, as shown for example by the presence of strong export-oriented industrial clusters in Puglia and Campania.

Convergence policies place insufficient emphasis on SME and entrepreneurship development

Policies aimed at the convergence of the south are underpinned by programmes set out in the annual National Plan for the Development of the South, which is backed by national resources and the European Union Structural Funds. Both have increased attention to local enterprise development in recent years. For example, among the measures of the National Plan are extensive business development incentives and a small automatic voucher as an entry point for entrepreneurs seeking public support. Overall, however, business support plays a relatively small role in the National Plan for the Development of the South, which focuses more strongly on improving framework conditions in the areas of infrastructure, education, innovation, the rule of law, and local public financing. Furthermore, the share of European Regional Development Fund resources for 2007-13 that were allocated to research and technology development, innovation and entrepreneurship was only 29.5% in the southern regions of Italy, compared with average shares of 58.0% in the United Kingdom, 46.9% in Germany, 36.9% in France and 30.1% in Spain, and only 7% of EU Structural Fund resources for the programme period 2007-13 had been spent by the end of 2011. There is therefore scope to fund a broader set of actions for SME competitiveness and entrepreneurship such as measures for training, advice, mentoring, consultancy and innovation. This would require some re-direction of the resources of existing funds to SME and entrepreneurship resources from less productive uses, as established by evaluations, complemented by actions to build capacities of local policy makers to design and implement SME and entrepreneurship programmes that can draw down unused funds in time.

Italy's decentralised governance system calls for strong national-regional coordination in SME and entrepreneurship actions

Italy has a governance structure in which regions share important economic development powers with the central government. This principle is embedded in the Constitutional Law; Article 117 giving concurrent competences to the state and regions in a range of areas such as scientific and technological research, innovation support for productive sectors, and regional credit institutions. The decentralisation process was advanced further in 2009 by a delegated law for the introduction of fiscal federalism. The joint responsibilities across levels of government make policy coordination an important issue for SME and entrepreneurship policies and programmes in Italy.

One of the main government bodies responsible for policy coordination is the State-Region Conference (*Conferenza Stato-Regioni*), a forum in which regions give their opinions on national government legal and administrative decisions relevant to them, and where the priorities of EU-funded regional development programmes are co-ordinated. This structure has proved useful in setting programmes that are coherent among each other and, at the same time, tailored to the different development needs of regions. However, there are two main priorities to improve co-ordination further. One is greater synergies between regional and national initiatives that target the same type of company (e.g. growth-oriented firms). The other is the introduction of mechanisms to better match the distribution of national programme resources to the size of the target firm base. The loan guarantee programme is a case in point, with 20% of operations and value concentrated in the single region of Piedmont.

Policy co-ordination will also be instrumental to the success of regional smart specialisation strategies in the context of the 2014-20 EU programming period. Smart specialisation involves a process of identifying competitive advantage and setting strategic priorities at regional level, to maximise the knowledge-based potential of each region. Without a national approach that coordinates regional smart specialisation strategies, there is a danger that regions enter in competition with each other in choosing the same generic specialisations, and lose the development potential stemming from larger-scale cross-regional initiatives (e.g. inter-regional supply chains). For example, it is important to identify clusters of national relevance and providing national steering and support when these clusters cross local administrative boundaries.

Regulatory simplification should be rolled out further at regional level

There is a wide regional variation in administrative efficiency. For example, while the Lombardy region has only 600 business regulations, there are more than 2 000 in Lazio, Sardinia, and Sicily. There are also important differences in the coherence of regulations and the way in which they are implemented. There is a clear scope for an exchange of best practices in regulatory and administrative reform so that lagging regions can learn from those forging ahead in the field of improving business regulations. Priorities include reducing the number of regional business regulations and introducing e-government measures more widely.

Key policy recommendations: The local dimension

- Increase the emphasis on SME and entrepreneurship programmes in the annual National Plan for the Development of the South and in the use of 2014-20 EU Structural Fund resources for regional development, by reweighting support towards programmes for training, consultancy, finance and innovation in SMEs and start-ups, and building local capacities to manage programme actions for SMEs and entrepreneurship.

- Introduce tailoring and monitoring mechanisms for key national SME and entrepreneurship programmes in order to ensure that southern SMEs are proportionally represented among recipients and that they are effective for supporting economic development in the South as well as the North.
- Ensure that the rules of business incentives for the South are clear and consistent over time.
- Strengthen coordination between national and regional government programmes where they target the same types of company, including a written agreement stating clearly how competences are divided and co-funding organised between national and regional levels with regard to entrepreneurship and SME policy.
- Widen the remit of the national one-stop shops network to include business development services offered by the regional level as well as national government, perhaps through individual agreements with the regions and co-financing to ensure that there is a base level of service across the whole country.
- Identify clusters of national importance and establish a mechanism for support when the clusters operate in multiple regions, considering the use of national competitions as a way of targeting resources.
- Consolidate regional business laws and regulations and provide better information and contact points, including through e-government platforms at regional level. Support regional administrative simplification through formulation of a set of national guiding principles, publication of comparisons of administrative efficiency between regions, evaluation of the impact of various regional administrative simplification initiatives, and exchange of information on good practices.

Industrial clusters

The Italian 'cluster effect' has weakened in recent years

Italian industrial clusters are a celebrated strength of the economy, accounting in 2011 for 30% of total national manufacturing exports. They refer to local labour market areas that are specialised in a particular manufacturing industry and are made up of a number of SMEs rather than one or more dominant large firms. They occur in a range of traditional manufacturing sectors such as textiles, furniture, white goods and footwear. Their success has been based on the close co-operation of their component SMEs in tightly-bound local subcontracting networks and their flexibility to adapt rapidly to changes in market requirements.

However, the cluster effect has weakened during the last two decades. From 1991-2010 the number of clusters meeting the criteria for inclusion in national statistics declined from 199 to 156, the number of cluster employees fell from 5.2 million to 4.4 million, and the share of Italy's employment in clusters fell from 29% to 26%. This was accompanied by a near disappearance of the performance advantage of cluster firms compared with non-cluster firms with respect to returns on investment and equity, value added per worker and product and process innovation rates.

Italian industrial clusters must adapt to profound structural change

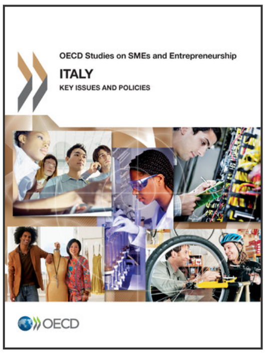
Italian industrial clusters have been exposed to substantial structural changes in the past two decades as a result of increased international competition from low cost producers. This is forcing cluster firms to avoid direct competition with traditional goods from emerging economies by competing on quality and innovation and shifting into high-end niche products for international markets. As in the Italian economy as a whole, medium-sized firms are doing better at this than small firms, which have been hit hard by an increasing tendency of cluster firms to source from abroad to cut costs. The medium-sized firms in Italian clusters must be allowed to innovate and internationalise to secure anchor points for continued cluster presence.

A shift in the traditional Italian cluster policy approach is required

Traditional cluster policies in Italy have focused on the establishment and support of networks of firms within the geographical boundaries of the clusters and investments in training and technology within clear sector specialisations. However, today the key cluster players are seeking to innovate, diversify and internationalise. Rather than seeking to preserve the traditional structure and specialisations of clusters, policy should be seeking to support cluster upgrading to new activities and technologies. Tying subsidies to local interactions is no longer appropriate since the best innovation and market partners may be national and international. Neither are policies that constrain the most dynamic cluster firms in their attempts to develop new activities outside of the traditional sector definitions. Instead the emphasis should be placed on promoting innovation and internationalisation among cluster actors and favouring the evolution of clusters towards related specialisations.

Key policy recommendations: Industrial clusters

- Permit strong flexibility in partner selection in network support programmes, enabling firms to collaborate with capable partners outside cluster boundaries.
- Promote the diversification of clusters into related industries and high-end activities. This may be facilitated by shifting existing subsidies and incentives onto "new" activities with diversification potential, such as support for strategic research projects, innovation collaboration networks involving companies and/or researchers that belong to different sectors and/or fields of specialisation, and labour mobility between related industries.
- Strengthen the external knowledge and innovation connections of clusters by promoting inward and outward foreign direct investment in clusters, the participation of cluster firms in global value chains, including by helping them meet the necessary quality and certification requirements and identify new market opportunities, and reinforcing links between cluster firms and capable public technology and research centres.
- Tailor policy to different types of cluster firms, focusing on rapidly increasing the productivity of small inefficient enterprises, maintaining the engagement of medium-sized firms with their clusters, and supporting the knowledge gatekeeper role of leading cluster firms within their supply chains. Offer selective support targeted at those cluster firms that demonstrate the strongest potential to grow in domestic and international markets.
- Promote the competitive award of incentives for the adoption of socially and environmentally sustainable standards and certifications, and other formal corporate social responsibility policies in clusters.
- Develop long-term strategies for clusters with the participation of expert working groups at the local level to guide policy support by national and regional governments.



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