

Interview with Matt Hancock on the Emilia Romagna Model
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*The Winter 2005-06 issue of **Owners at Work** published an extended article on the employee-owned sector in Emilia Romagna in Northern Italy.*

In March, Emilia Romagna expert Matt Hancock visited Kent to speak. We asked him to put the employee-owned sector in the context of the region's economic development policy.

OaW: Matt, give us an overview of the cooperative sector in Emilia Romagna.

Hancock: There are four million people in Emilia Romagna and 300,000 businesses, or about one business for every ten people. The numbers are a bit hard to get a handle on, but it's safe to say that there are 4,000 active co-ops in the region. Two-thirds of those co-ops are worker owned. Those range from heavy industry to precision equipment, from gigantic ceramic presses to service co-ops. There are also a number of very important agricultural co-ops, housing co-ops and, increasingly, social co-ops.

Social services are increasingly provided through co-ops, often using a multi-stakeholder model so you actually have, in some cases, people who are receiving a service who are also members and are elected to the board of directors of the co-op.

OaW: How does the multi-stakeholder co-op work? Do they have different classes of co-op members?

Hancock: No, the law in a Type-B social co-op – which is essentially a sheltered workshop – stipulates that if you want to be considered a co-op and enjoy the tax benefits that come with that, then a minimum of 30% of your members and a minimum of 30% of your board members need to be people who are benefitting from your service. So, if it's a sheltered workshop and is employing young people with Down Syndrome, the members in that co-op will be the children's parents, specialists working at the co-op, and 30% minimum have to be these kids with Down Syndrome and they will also be on the board of directors. The same is true if you are doing a social co-op that works with felons, drug addicts, or whatever the need is.

OaW: What portion of the economy in Emilia Romagna is cooperative?

Hancock: In terms of GDP, it is reported to be around 9%. If you take a company like Ducati Motorcycles, they have a thousand employees, 90% . . .

OaW: Is Ducati a co-op?

** Hancock: Ducati is not a co-op, but let me step back. The co-ops generally tend to be large. The largest businesses in Emilia Romagna are co-ops. That's true for retail, agriculture, and worker-owned co-ops. You do have some co-ops that are small with only 10 to 20 members but if you look at the biggest firms in Emilia Romagna, they are generally co-ops. Of those firms,

99% of them have less than 250 employees. The average manufacturing firm in Emilia Romagna has only 10 employees. Only 1% of firms have 250 or more employees.

** The big firms use a flexible network model to produce the majority of the product. Ducati is a good example. They make motorcycles but 90% of the motorcycle is made outside of Ducati by this network of sub-suppliers. So there is a lot of value being produced before the motorcycle gets assembled by Ducati.

OaW: How does this flexible manufacturing system work?

Hancock: It developed as a response to the market for the development of an economy that was based on micro and small enterprises. None of these small enterprises alone would be able to compete in the market. So what the market dictated was that you need to have a mix of competition and cooperation. I'm not going to get very far alone making a cylindrical metal component that will eventually go on to a packaging machine.

We do better when a group of firms work together. Let's say, Nestle needs to have machinery to package chocolate. Nestle would come to one firm and they would get that one firm to take the order. Then that firm would organize other small firms which specialize in a particular phase of production to produce the other pieces of the packaging machine.

The development of these flexible manufacturing networks, on one hand, was dictated by the market because small firms acting alone aren't going to be able to compete effectively. On the other, it was also aided by regional policy, which tended to concentrate businesses in a particular area and to provide a lot of support to business development, in terms of infrastructure and in terms of loans, and then later on in terms of business development services and then in terms of more advanced things like marketing and research and development, which encourage groups of firms to get together and meet their needs collectively.

OaW: I read that this is changing...

Hancock: Emilia Romagna's flexible manufacturing networks are now moving from an informal arrangement to something more formalized. There are two models.

In the first model, a lead firm emerges and coordinates the network. That's one of the firms that used to be small but has gotten a little bit bigger and maybe has 250 to 500 employees. It is now beginning to assemble the equipment or entire assembly lines, a turn-key kind of model. A customer from Germany or China or the United States, instead of going directly to one of the small firms that is a component manufacturer now goes directly to one of the larger firms who is actually producing the final product. There are now a small number of larger firms emerging at the interface between the market and this network of suppliers. This means you are getting increased vertical integration, more formal relationships, experience of real co-design and co-production, rather than this sort of informal network.

The other model that is emerging is what you would call a virtual firm where these smaller private firms are setting up their own virtual company, almost like a second tier co-op. They are

creating their own customer that will interface with the market for them. This will allow them to collectively bid on jobs, which will allow them to source things collectively. The most advanced one is a company called Deco Service. Deco is made up of 17 small firms that are in a formal network. They have their own brand. They do about \$17 million in sales a year and that is expanding. They have customers in Rochester, NY, Germany, and throughout Italy. This has been made possible because they have created their business that represents this network.

OaW: If you are a small business with 10 employees and you are in a flexible manufacturing network is everything you are producing within that network or do you produce components for other networks, or sell products directly to outside customers? How does this work from the point of view of the individual firm?

Hancock: I know one of these firms very well, it's called LACO, which is a combination of the two names of the founders of the firm. They specialize in the production of cylindrical components. They can make anything that is cylindrical in shape and they are very good at making it.

LACO is a typical story. The founder graduated from a technical vocational high school, which is unique in that it gives its students a very firm grounding in theory so you are able to design. You're able to use machinery **and** you are also able to design pieces. He went on to become an entrepreneur, left the company he was working for which was called IMA. IMA produces packaging materials like Lipton Tea bags. The boxes are packaged by their machinery. They make pill bottles. The pharmaceutical industry will use their packaging machinery. After doing this a few years at IMA, he was encouraged by IMA to spin off into his own firm. They guaranteed him some orders so he would have some money coming in at the beginning, so initially his main client was IMA. As he began to expand his capacity he continued to supply to IMA but then also began to supply IMA's competitors. IMA is perfectly comfortable with this. In fact, they encourage it because it guarantees them flexibility. IMA doesn't have to guarantee him a market because they know that he has enough other customers to stay in business but also that he is flexible enough to be able to meet the demands of IMA when they need it.

LACO is also part of this network I just talked about, Deco Service. So he's supplying and he is an owner in that virtual firm. He is also supplying IMA directly with the products, but sometimes, too, he's part of the project that is organized by this virtual firm who may be supplying assemblies to IMA. He has now set up a relationship with a group of firms in Romania because he realized that being competitive requires that he supply assemblies as well as high value-added components so he is adding to his capacity to meet the customer's needs. He specializes in cylindrical components, but he is also saying that he can offer an integrated solution because he has suppliers in Romania and we can provide you with an assembly, rather than just the single component.

OaW: Why do you think this works so well?

Hancock: You have people who are technically very competent: They know how to work machinery but also have theoretical backgrounds that allow them to become a designer of components. They have the skills needed to run a business and they have a genuine passion for

producing quality things. Another key is that they are overwhelmingly geared toward export, not just out of their region but throughout Europe. They are producing for the Chinese market, they are producing for the Brazilian market, they are producing in Eastern Europe for markets there. There is a real demand for the products that they are making. Everyone is so specialized that there is enough work to go around.

One of the trends you do see is that the small firms that used to have only two or three employees are now getting bigger. The average firm now has 10 employees. They are beginning to introduce more sophisticated management techniques but everyone that I have spoken with in the flexible manufacturing network says that the key is flexibility; the key is their specialization. If a new division or specialization develops within a firm and they get beyond three or four employees they spin them off into a new company.

OaW: What role does public policy play in all this?

Hancock: A decisive role. It goes from things as simple but fundamental as making sure that the infrastructure in the region is the best that it could possibly be. That means roads, public transportation to get people to work comfortably and effectively. Emilia Romagna built a very advanced highway system when nobody had yet seen the need for it, but policy makers anticipated that need for 10 years down the road. They knew that if they didn't have an advanced highway system they were going to be in trouble in the future.

Public policy has made it possible, particularly coming out of World War II, for people with no money but with a lot of skills to become business owners. Cities used eminent domain to take over unused land and would use public money into developing it and the kind of infrastructure that industry depends on. They would then selling it at cost, below market prices, to small business owners and co-ops.

In the 1970 and 1980's you had an economy that was competitive but it was mostly first generation owners who were technically very competent but who did not have the management skills for the global market. Individually they didn't have the ability to bring in new automation that the market was demanding so what they did was to set up a series of sectoral service centers.

The service centers were born out of the dialogue with businesses and the regional government and the needs that grew out this dialogue were the people saying that they could really use some help in quality control, quality certification, management, automation and R&D. The service centers worked with a cluster of businesses on . . . The best way I heard it described was as a literacy program for small businesses and to put them into a position to be able to deal with the universities and foreign markets more effectively.

OaW: Do the service centers provide support for exports?

Hancock: Not generally. That's provided by the business associations instead.

OaW: And the business associations are based on an industrial sector or are they broader?

Hancock: They are based on business size, not sector. There are two small business associations in Emilia Romagna. The largest one is associated with the left wing political parties. The second largest one is associated with the Christian Democratic party. You have one association for mid-size businesses and you have one association for larger industrial businesses.

What they will do is to work with a group of firms in a particular cluster of a district. They will use public money to bring the textile producers to Eastern Europe or China to develop relationships with suppliers or clients there. They will use public money to take a group of fashion designers from Emilia Romagna to important fashion shows around the world.

OaW: When you say public money, is that money from the central government in Rome or is that money from the regional government in Bologna?

Hancock: What is important to understand when looking at Italian policy is that Italy is not a federal system. There is a central government in Rome that collects taxes. The city government has a limited ability to collect taxes based on property but it is very low. There is a regional tax but it is essentially collected by the federal government and then sent back to the region so the region doesn't really have its own tax base but they do have funds that come through Rome. It's money that is raised regionally, then goes to Rome, and then gets sent back to the region. The majority of the regional budget goes to health care because that is managed at the regional level.

The money for economic development comes from the tax that is collected nationally for regional use and from European Union funds. Emilia Romagna has been particularly skillful in making use of the structural funds of the European Union. A lot of the policy they are doing now is with money that essentially comes from the European Union and is filtered through Rome.

OaW: What about availability of capital for the Emilian businesses?

Hancock: Small businesses used to be essentially started with sweat equity. That's no longer feasible because buying a CNC machine is a lot more difficult than buying an old manual lathe. So more and more banks are stepping in to provide small business loans. The business associations, in cooperation with the regional government, create loan guarantee consortiums to reduce the interest rates that small businesses are paying. A member of the CNA, which is the small business association, for example, gets a preferred interest rate with banks that are in the Network.

OaW: And that is because of the fact that the business association is providing the loan guarantee?

Hancock: Exactly. Your collateral is the good faith of the regional government and the business association.

OaW: So the loan guarantee is provided by the regional government in cooperation with the business association?

Hancock: Precisely.

The regional government also has a range of other policy tools. For example, if the regional government, in cooperation with labor and businesses, has identified certain priority areas for automation you can apply for a grant to purchase a new piece of equipment because it is a collective competition; it is not proprietary. If the businesses in this cluster need to introduce a type of automation to be competitive, they will provide grants to them. There are all sorts of unique financing mechanisms that help small firms upgrade their equipment. Some of these are not always outright grants. Sometimes it is just reducing interest rates for loans on equipment.

OaW: So what you are depicting here is a kind of regional industrial policy.

Hancock: Absolutely. The regional industrial policy is usually done on a 3-year plan. There is an annual conference on the economy. It's convened by the regional government and the labor unions and business associations attend and discuss economic policy. The regional government presents research to them in a plan and then it is discussed and debated with what they call their "social partners."

OaW: Social partners?

Hancock: Labor, the business associations, and agriculture. Agriculture is overwhelmingly cooperative. There are some private meat processors but the majority of farmers organize their co-ops and they are represented by the cooperative business association, which would be one of the social partners.

OaW: Let's talk about transferability. NE Ohio has a population that is virtual identical to that of Emilia Romagna so if we wanted to introduce some of Emilia Romagna's characteristics, what do you see as most transferable?

Hancock: The experience shows that focusing policy on a sub-national level can be very effective. I think that the real lesson that it is most effective when it is local and when it is regional. National policy can be effective in that it is leveraging local and regional efforts.

They have done some amazing things and they continue to do some very advanced things in terms of industrial policy and, now, around innovation, and linking high-tech advanced research with manufacturing but they have very limited resources. Our state, city and county governments all have greater ability to raise revenue. They have much larger budgets and they have control over the money that they are raising. In terms of resources, we are at a greater advantage.

OaW: If we take a single industry, for example ceramics, where Emilia Romagna seems to be very successful, is this because it has targeted by the regional government and other areas in Italy don't target ceramics or what keeps neighboring regions from targeting the same industries?

Hancock: There is nothing keeping them from targeting it but they are not doing it effectively. If you look at the clusters there is a spontaneous base there. There is no planning, the region doesn't pick winners, they don't say "This year we want to start the ceramics industry in Emilia Romagna." They did it since the research identified existing industrial clusters and they began to look at what the needs of these clusters are. How could policy increase the competitiveness of

the cluster as a whole? They did that based on regional cooperation with the business associations. Nothing was imposed on the cluster. The best cases it comes out it dialogue.

OaW: So you have a left-wing government collaborating with business organizations to provide infrastructures, subsidizes, grants, loans, and loan guarantees to capitalist businesses?

Hancock: Well, I don't know. Is a worker-owned co-op a capitalist business? Or is a network of small firms, such as Deco Service "capitalist"? There are 150 employees and 30 of those employees are also owners of the businesses and they are all working in those businesses.

OaW: None of them look much like ENRON, Aldelphia or GM.

Hancock: The common trait among even the larger companies that are clearly capitalist businesses is that they are committed to competing based on innovation and quality. They are not interested in competing in with low wage countries on wages.

OaW: Do you see individual policy tools like these loan guarantees provided through the Chamber of Commerce or the Ohio Manufacturers' Association and the State or the City of Cleveland? Is this a tool has something that could be used here?

Hancock: Absolutely. I think it is important to look at what the underlying structure that is making this successful not just the particular loan guarantee policy.

OaW: So what is the underlying structure?

Hancock: It is the same as what you guys are doing here. The OEOC's Advisory Board brings together labor, business, government and members of the ESOP community and so that kind of dialogue is fundamental in getting these different social partners to sit around a table is fundamental but then building a common vision that the different social partners can all fine tune and advance is key.

What might come out of that? A service center would be appropriate, or maybe a loan guarantee consortium is important. Who knows what could come out of it.

Another key thing about Emilia Romagna -- and there are all sorts of cultural factors that could never be replicated -- is an overwhelming degree consensus around long term vision that ties economic development to social development very explicitly. That is a commitment to maintaining and expanding the manufacturing economy as the key to having a healthy service center economy. This is a vision that is shared by all the social partners. I think that is key.

Finally, the government in every level of Emilia Romagna has been recognized as being one of the most, if not the most efficient, honest and transparent governments in Italy. That makes doing business very easy. They have tried to cut through as much red tape as possible because that is a deterrent to starting a business or expanding a business.

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