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The Italian Footwear Industry: an Empirical Analysis

Regular Paper

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Abstract This paper aims to provide readers with a deep empirical analysis on the Italian footwear industry in order to investigate the evolution of its structure (trends in sales and production, number of firms and employees, main markets, etc.), together with the identification of the main drivers of competitiveness in order to explain the strategies implemented by local actors.

Keywords Footwear Industry, Business Models, Competitive Strategies

1. Introduction

Growth in the Italian footwear market has fluctuated in recent years, with two periods of decline seen in 2009 and 2012. At present, it counts for a gross value of 4,646 million US Dollars, representing a compound annual rate of change of 0.7% between 2008 and 2012. In comparison, the German market grew with a compound annual rate of 2.2% and the French with a rate of 0.5%, reaching, respectively, a value of 13.3 billion and 11.2 billion US Dollars in 2012. Nevertheless, in 2017, the Italian market is forecast to have a value of 4,672 million US Dollars, representing an increase of 0.6% since 2012 (Datamonitor, 2013). These data reflect a turbulent context in which competitive forces seem to shape the industry continuously. Taking these considerations as its starting point, this paper aims to investigate the Italian footwear industry, explore its recent evolution and identify the main drivers affecting the degree of competitiveness among firms.

With these aims in mind, we chose to use a quantitative approach, developing a survey which was carried out among the management of a number of Italian firms active in the industry. Specifically, our research involved the creation of a questionnaire which took into consideration the main features and characteristics of the footwear industry, such as the degree of vertical integration inside the production chain (D'Amico et al., 2013) and the distinction between "processing on one's own account" and "work on behalf of third parties", which constitutes one of the main variables of segmentation in the industry.

Furthermore, in order to identify the firms to be interviewed, we used the database system developed by the Italian Chambers of Commerce. Starting from a

gross number of more than 3,000 firms, we created a stratified sample based on three different variables: 1) a firm's size, based on its number of employees; 2) a firm's localization, covering the entire Italian state; 3) a firm's activity, according to the national statistical classification.

Table 1 provides a list of these variables with the sub-segmentation used on each level.

Variable	Items
Firm's size	Number of employees between 10 and 49
	Number of employees between 50 and 249
	Over 250 employees
Firm's localization	North-east Italy
	North-west Italy
	Central Italy
	Southern Italy
Firm's activity	Leather tanning
	Shoe manufacturing

Table 1. Variables and items used to construct the sample of analysis

Acting along this methodology, we selected 1,283 firms (approximately 40% of the total) which were integrated into the research through a CATI survey, conducted in 2012. The redemption rate was 9 per cent, meaning that the final number of firms interviewed in the analysis was 115.

The questionnaire has been designed using a tree methodology which develops different sequences of questions depending on the answers obtained.

Specifically, the first group of questions refers to the strategic and economic characteristics of the firms. For example:

- products-markets portfolio, with particular reference to foreign markets;
- placement and communication strategies on national and international markets;
- industrial production cost breakdown.

Working with these data, a first map of the structural characteristics and performance parameters of the operators in the sector was drawn up.

A second set of questions was developed to identify the skills acquired by companies in the course of the main activities and phases of the supply chain, as well as to determine the degree of insourcing/outsourcing of business activities. From this point of view, the questionnaire has been a useful empirical tool to design the supply chains and analyse the degree of vertical integration of the companies as well as the level of networking activity among professionals.

2. Sample analysis: structural characteristics

As previously mentioned, firms included in the sample have been clustered into two groups according to their main activity: leather tanning (NACE Code 19.1) and footwear and accessories manufacturing (NACE code 19.3). This breakdown by activity shows that a slightly larger proportion of companies are specialized in the manufacture of footwear and accessories (56%) compared to those involved in the preparation and dressing of leather (44%).

Similarly, firms are divided between production on their own, which covers 42% of the sample, and third-party production, which accounts for 53% of the sample; the remaining 5% comprises companies engaged both in production for other operators and in their own production. The importance of this segmentation lies in the strategic considerations from a competitive perspective. Specifically, production on behalf of a third party calls for an investigation into the networking activities carried out by firms with other players acting in the industry. This networking activity is relevant to the management of all the phases related to product development and innovation. By contrast, the presence of a firm's own production activity can be viewed as a proxy for a greater degree of independence from the external environment on the part of the firm.

The average number of employees per firm is 25. More specifically, while firms operating in the preparation and dressing of leather declare an average number of employees equal to 26 units, companies focused in the manufacture of footwear display a lower value (24).

Finally, the geographical distribution of the companies shows a greater localization in regions of central Italy (45%), followed by the north-east (30%), the south and the islands (17%), and finally, the north-west (8%).

3. Sample analysis: strategic and economic characteristics

In order to conduct an analysis of the main strategic and economic features of the firms included in the sample, we must turn our attention to business models so that all management aspects can be considered simultaneously.

In current literature and practice, there are various ways in which business models are defined and used. Traditionally, a business model describes the external

organization of commercial transactions between firms. Transactions include the exchange of information, goods, services, money, contracts and knowledge. In sum, a business model defines the potential benefits for various business actors, the sources of revenues and the cost drivers (Timmers, 1998). Moreover, it describes the architecture for a product or service and the related information flows, including a description of the various business activities and roles (Osterwalder et al., 2005). This conceptualization is consistent with the approach described by Amit and Zott (2008), which proposes a relational view of business models, defined as "the structure, content, and governance of transactions" (Amit and Zott, 2008).

In our work, we have chosen the Amit and Zott perspective because it is useful for the analysis of the relationships chain, which involves manufacturers, distributors and consumers. Specifically, we look at the different models of production, which can be placed along a continuum of organizational forms. At one end of this continuum is so-called "scheduled-based production" (which follows the traditional, seasonal cycle of sales) and, at the other end, the "ready fashion" model, based on: i) a short production time combined with a brief delivery time and ii) low-quality final products. Finally, the mid-point can be identified as the semi-planned production model (or "fast fashion"), characterized by a combination of fast lead times and high stylistic contents.

The use of business model methodology to interpret the survey results in the field allowed us to read the evidence in an integrated manner, with particular reference to the analysis of the activities and skills acquired by companies.

Taking these considerations as our starting point, we focused our strategic and economic analysis on the main elements which form the basis of the business model concept, namely: market performance (measured in terms of total turnover), customers (viewed as geographic target markets), placement strategies to reach these markets and costs borne by firms.

The distribution of firms by size (measured in terms of total turnover) shows different performances in the two productive sectors identified above (Figure 1). Specifically, in the preparation and tanning of leather, the most-represented class of turnover is between 2.5 and 5 million Euros, which suggests greater revenue potential in this sector. By contrast, specialization in footwear manufacturing activities has different values: we can note the absence of firms with a turnover of over 10 million Euros, while the most-represented class of turnover is between 1 and 1.5 million Euros. Even the lower classes (up to 0.5 million, and between 0.5 and 1 million) have values higher than those indicated by the upstream supply chain. To summarize, on the basis of information gathered in the study sample, the companies operating in the early stages of the production process record higher values.

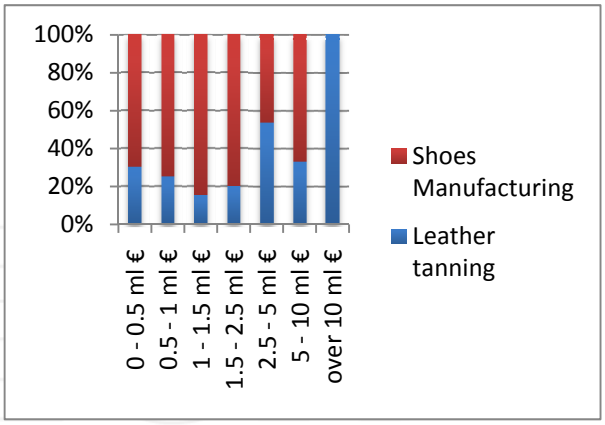

Figure 1. Distribution of firms by class of turnover

With regards to trends in turnover, on the basis of subjective evaluations expressed by the firms interviewed, these values seem to be sufficiently stable over time. More than half (55%) of the companies reported a stable trend in revenues over the last three years, while 20% of the sample demonstrated a gradual increase. The remaining 25%, however, faced a decrease in sales in terms of revenue, essentially due to the economic crisis and competition from so-called emerging countries.

Breaking down the data according to the stage in the production chain, there is greater stability in the performance of upstream players in the supply chain (i.e., those involved in the preparation and dressing of leather), with just over 70% of companies declaring a stable or positive trend active in this area. Among downstream companies, i.e., those involved in manufacturing footwear or accessories, a majority of operators also registered a positive trend, along with a substantial proportion reporting a downward trend.

The analysis of turnover by size and the comments made about the trend in the last three years require an interpretation based on the geographical perspective, aimed at highlighting the locations in which these revenue streams are generated. With this aim, our survey focused on the geographical areas in which most turnover has been generated (Figure 2). European countries constitute 54% of total turnover, followed by Asian countries (excluding China) with 18%, the countries of NAFTA (14%) and, finally, South America (12%).

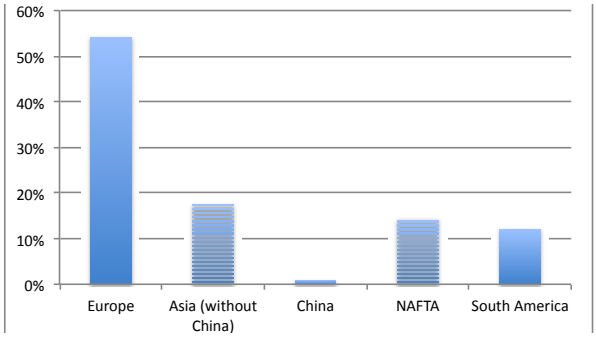

Figure 2. Market turnover breakdown

The analysis of placement policies and related business strategies was limited to companies that operate on their own. Specifically, the distribution policies adopted by the firms in the sample may be divided into two types: the creation of a private distribution network, which accounts for about 74% of the sample, and the use of intermediaries (33%). The percentage of companies that use flagship stores is very modest (3%) while the use of forms of franchise is totally absent. From a commercial strategy point of view, the mix of instruments used by companies to enable commercial transactions seems to be highly articulated and includes participation in national fairs (65%), the employment of agents and representatives (35%), the implementation of marketing activities and communication (14%) and participation in international fairs (9%).

The markets of the footwear sector are characterized by a high level of risk, not only because of the volatility of final demand, but also thanks to the growing weight of fixed costs on industrial total cost (Nenni et al., 2013). Furthermore, the cost configuration often acts as an entry barrier for new competitors, but it also represents one of the main drivers affecting industry competition and the competitive advantage of some operators. For these reasons, the survey investigated the breakdown of product cost in order to identify the key internal mechanisms of operations management.

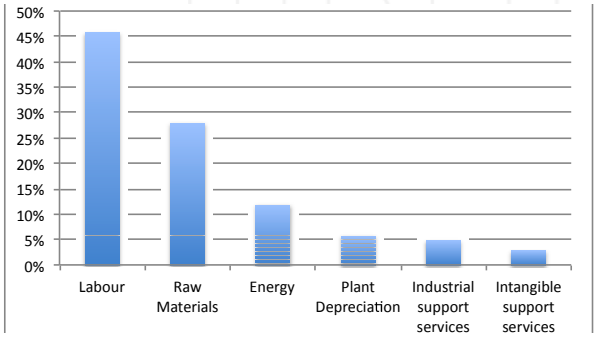

Figure 3. Industrial cost breakdown

As expected, labour and raw materials constitute the main contributors to production cost, respectively accounting for 46% and 28% of the total (Figure 3.3). Another significant source of cost is represented by the energy costs, which contribute a further 12%, while the remaining 14% is ascribable to depreciation of plant value, industrial support services (such as logistics or quality control) and intangible services (such as design, modelling or promotional and communication activities).

4. Main activities and core competencies

The final part of the empirical analysis aimed to investigate the organization of production, studying i) the degree of internalization of the main activities in the value chain; ii) the localization of productive plants and iii) the skills and competencies of the firms and the main enabling factors or constraints in the strategic development of the firms.

The analysis of the degree of internalization was conducted in order elucidate the choices of the firms in terms of vertical integration vs. outsourcing procedures.

The main evidence from the leather tanning and dressing sector shows:

- An integrated perspective in the operational management process that applies not only to the production phases, but also to distribution, through shipment to end customers. In 78% of cases, this activity is carried out directly by the firms interviewed.
- A strong focus on the initial and final phases of the manufacturing process, involving both the internalization of the purchasing of raw materials required in the production process and quality control of the outputs of this process.
- A significant degree of internalization in the first processing activities (lining) – viewed as a critical issue for competition in the industry in 53% of cases – as well as at the later stages of finishing, i.e., surface (50%) and wet finishing (48%).

By contrast, the "manufacture of footwear and accessories" level revealed the following:

- There is a strong presence of firms in the quality control phase, internalized in 76% of cases. This stage is viewed as a hygienic requirement necessary to secure the consensus of buyers in foreign markets.
- There is a high level of internalization in logistic operations, as well as all activities related to shipping products to customers (59%).

- The production of prototypes, in 57% of cases, emerged as the third activity carried out inside the company.
- The cutting and fitting of shoes are other examples of activities that, for most of the businesses, seem to be strategic, thereby excluding the possibility of outsourcing them to third parties.
- Finally, odd as it may seem, planning and design occupy only the fifth place in the ranking of the stages of the production process carried out internally by firms. It is undoubtedly true that these activities constitute a major source of competitive advantage in this sector. Despite this, only 37% of the companies in the sample have internalized this stage. This can be viewed as an indicator of the presence in the sector of specialized operators with specific competencies in design.

Consistent with the geographic distribution of the sample across the national territory, firms' factories are located mainly in central and northern Italy. Production activities are mainly established in firms' area of origin, often close to or within industry clusters. The percentage of firms with production facilities located across national borders was very low and was observed in only two cases.

In order to understand the principal drivers which explain choice of plant location, we asked firms to indicate the three main variables which influence their strategy in this regard.

According to the data collected through the survey, proximity to suppliers is the main determinant of the choice of plant location (named in 67% of cases). Suppliers are often present in the same province (in 47% of cases) or region (in 41% of cases) as the manufacturer. Sometimes they are located outside the local region, but nonetheless within the national territory (36%). In fact, only a low percentage (equal to just 13%) of suppliers is located abroad.

Similarly, proximity to final markets is a significant factor in guiding a firm's choices (named in 34% of cases), as well as the possibility of obtaining the benefits resulting from the dissemination of knowledge on a local basis (24%). Other factors include the likelihood of signing commercial agreements (11%) with local players or developing basic and applied research projects with other firms (i.e., competitors or suppliers) (3%).

Clearly, these findings reflect the Italian industrial context. In Italy, the prevailing model developed inside the industrial districts (Beccattini, 1979; Beccattini and Rullani, 1993) is based on the integration of all activities related to the supply chain in a network of firms located close to each other. Compared to a traditional, integrated supply chain, this model preserves flexibility of production while maintaining the advantages of integration resulting from the coordination of the information flow and the reduction of costs associated with the purchase of raw materials. Thanks to these characteristics, the network model is well suited to the volatility of the market for fashion products and, specifically, to the footwear industry.

Finally, the analysis of firms' competencies was conducted using a self-assessment process: each company evaluated its own capability in planning and design activities compared to direct competitors. More specifically, we asked firms to assess themselves on the main business skills of technological innovation, within a range of scores from 1 ("we do not have this competency") to 7 ("we have a strong competency in this area").

Ratings show firms in the sample have a greater propensity to manage incremental (rather than product) innovation (5.6 vs. 5.3) and a significant (average score: 5.5) ability to collaborate with suppliers of machinery for the customization of plants and final products.

In order to study interviewees' perceptions of the constraints and problems that hinder business growth, it was necessary to specify the main obstacles encountered in the development of the enterprise. Consistent with our expectations, the factor that most adversely affects the growth of operators in the footwear industry is the cost of labour, named by 68% of respondents. It should not be forgotten that this factor is also one of the main causes of business delocalization across national borders in the fashion and footwear industries (Cutini, 2011).

Regarding competitive pressure from emerging countries (in which the problem of labour is less challenging), the second constraint factor is represented by international competition, which accounts for 63%. Additionally, financial resources play a significant role in limiting the growth of firms: in fact, 40% of operators interviewed identified the reduced availability of financial resources as the third factor constraining the firm's development.

Finally, with rates substantially similar, other limits can be identified as internal factors (such as a low qualification of technical employees and sales staff, wrong or inappropriate technological innovation policies, lack of marketing competencies and skills) and as relating to the external environment (e.g., poor logistics and transport infrastructures).

5. Conclusion

This article described the Italian footwear industry using data gathered through an empirical survey of a sample of firms operating in the sector. The firms interviewed were highly heterogeneous in their endowment of resources and capacity to cope with the forces currently shaping the competitive environment. Nevertheless, some general considerations can be identified as guidelines for business modelling in the footwear industry. Regarding the cost side of business models, the main drivers are:

- the degree of vertical integration in the value chain, indicating a preference towards the "make" option for both upstream activities (initial phase of production) and downstream activities (e.g., shipment and delivery phases);
- the location of plants and activities, guided by the opportunity to have strong contact with suppliers and/or final markets, in order to benefit from innovation and knowledge sharing processes.

At the same time, firms must succeed in developing a value proposition according to their competencies and know-how. From this perspective, quality control, logistics, and product innovation in prototyping activities seem to be the main sources of competitive advantage. Consequently, in order to cope with the turbulent nature of competition in the industry, firms must improve their skills, resources and capability in these areas, leading to a continuous process of internal renewal.

Various limitations characterize our research. Firstly, although the sample was created according to proper statistic methodologies, it does not necessarily reflect the characteristics of the whole industry. A larger sample could provide readers with more reliable findings.

Secondly, the sample includes only Italian firms, while an analysis of competition across the national territory should also take into consideration foreign players.

Finally, the findings of quantitative research could be compared with data and information collected through qualitative studies. The development of a number of case studies which thoroughly investigate the business models of specific firms could complete the framework of research.

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