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**FROM OFFSHORING TO RESHORING.
FOCUS ON THE *BACKSHORING* PHENOMENON IN
ITALY**

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ABSTRACT

The expansion of the physical dimension of enterprises across national boundaries, through direct control exercised over other production units, has shown to have not negligible effects on the commercial flows. International trade, therefore, represents the engine driving the global economy.

In a difficult time like what is going through the global economy, business strategy decisions have a key role in the international economies of each country.

Offshoring is the process of overseas relocation of certain business activities in order to gain greater benefits, such as labor supply at a lower cost of labor. In recent decades, this phenomenon has become increasingly important, as there are many companies that have adopted this type of strategy, thanks to the many economic benefits it brings. However, this type of choice entails certain disadvantages. The attention of the international press is increasingly attracted by the growing instances of *reshoring*: the relocation. The objective of the following work is to analyze the *backshoring*, the return of companies' previously relocated activities to home country. United States and Italy, respectively, are the two countries that have had the largest number of reshoring cases. More than half of back/near-shoring manoeuvres result from a return action from China (especially US companies). In addition, the phenomenon of backshoring has played an important role in industrial policy in overcoming the economic crisis.

This theses investigates the phenomenon of production relocation, and in particular the backshoring, and therefore the return to the country of origin. The theoretical approaches adopted for this research are the classical theories of internationalization, organizational theories and theories on business strategy, in particular the perspective of the psychic distance to be included among the hidden costs taken into consideration by the Schulte model. The work, therefore, intends to offer a look at the phenomenon from within the company, focusing on the key processes of perceiving distance (geographical, cultural and psychic) that influence localization choices.

KEYWORD: FDI, offshoring, backshoring, psychic distance, cultural distance

JEL CODE: F230, H50, H76

INTRODUCTION

Globalization affects society in all its components, whether marginal or substantial, and overwhelms each

its constituent. The economy, the way of life and thinking, which are simultaneously reflection and generators of this globalization, can no longer reappear as they were in the past, as they underwent the inexorable law of transformation and evolution.

In 2017, internationalization can no longer be felt as a strategic option, but it has inevitably become a necessity for survival, which is even more amplified in Italy where the domestic market shows weak signs of recovery.

From the second half of the twentieth century, business evolution has taken place increasingly in the context of the globalization of economic and productive systems. Value chain activities that were once more concentrated in the country of origin have been increasingly reorganized on a global scale (Caroli, 2012). The huge development of new technologies in the ICT sector, facilitation the transfer of people, goods, capital, the creation of free trade areas and the emergence of the global scenarios of developing countries, such as India and China, are just some of the factors that contributed to the explosion of internationalization.

These changes have prompted companies to adopt governance models that allow for high organizational flexibility in order to be more efficient and responsive to changes in world demand and local needs. In this perspective, in the last decades, the so-called *offshoring* phenomenon has exploded: the shift of various value chain activities across national boundaries in order to find more favourable economic conditions, such as lower cost of labor. Since the 1990s the companies that, regardless of country of origin, are strongly present on international markets and have adopted offshoring strategies dominate the world scenario. These activities are characterized by the high degree of flexibility and coordination capacity of the various dispersed resources in the various countries. They are very efficient globally and at the same time they are very careful to local needs.

Most of the literature has focused on studying the benefits of this phenomenon, however, since the 1990s a group of intellectuals has been opposed. These scholars have focused on the analysis of the risks and the criticalities associated with such organizational practices (Frattocchi *et al.*, 2014).

In fact, the conditions change, and in recent years there have been numerous cases of reshoring, the relocation of production activities previously transferred abroad and numerous cases of backshoring, the return to home country. Factors, such as rising labor costs in emerging countries, loss of quality, long shipping times and minimum order quantities, are just some of the factors that led to this trend reversal. The control and coordination of internationally dispersed supply chains is not easy. In addition, frequent political instability, which has occurred in many developing countries, is a risk factor not to be underestimated. This phenomenon has attracted the attention of the press, which increasingly focuses on articles dealing with returning companies. It should be emphasized that backshoring involves more decisively the activities of the manufacturing sector, as almost all of the observed cases refer to the return to production activities at home.

United States and Italy, are respectively the two countries that have had the largest number of backshoring cases, followed by Germany, France and the United Kingdom. The US government has actively supported the companies intent on bringing productive activity back into the country through tax incentives. Large multinationals, such as General Electric, Boeing, Starbucks, have started return operations, driven by a more favourable environment in the country of origin. At national level, there is some sort of internal competition to try to encourage companies to return. For example, the US government has invested heavily in order to offer businesses low-cost energy. Differently, in Italy, companies have come back spontaneously, driven by a change in international demand, which calls for a broader offer of "Made in Italy" products. Many fashion industry companies, such as And Camicie, Piquadro, Diadora, have started backshoring strategies in order to obtain higher-quality products that enable the benefits of the "Made in Italy" brand. Consumers, in fact, are willing to pay a premium price for this kind of goods. The Italian government has not invested enough resources to support this phenomenon, and companies returning, receive no support from the state.

In this context, the analysis of cultural differences is of great importance in the study of this phenomenon because from them can derive the choice of the entry or exit strategy implemented by the company, market segments management, and identification of consumer perceived value.

The *liability of foreignness* (Johanson and Valhne, 1977, 1990, 2009), which means the sense of strangeness that affects a company due to the lack or partial knowledge of the foreign country and its culture, affects the company as much as it is wide cultural distance between country of origin and country of destination.

The product is not only reduced to the physical component but it is a set of tangible or intangible utilities and attributes that form the essential components, completing components and accessories (design, user functions, product platform, brand, Packaging, warranty, after sales service). Cultural adaptation now appears to be one of the deepest challenges for those who are facing a foreign perspective. It requires a non-automatic approach and tuning, but to be created between country of departure and country of arrival and sensitivity to factors and mental patterns that do not belong to the starting cultural context.

The cultural aspects that arise require cognitive needs. Through the study, experience and networks, companies can leverage specific country effects and translate intercultural learning from time to time into standardizing or adapting marketing policies.

In this thesis, the first chapter will be dedicated to the study of globalization on literature: the cultural aspect of the phenomenon from which internationalization is investigated through the approaches of various scholars, from Smith to Ricardo, from Hymer to the Uppsala School, will go to Vernon and Dunning, summarizing how to enter the country through exports, contract deals and direct investments. Then the attention will go to the analysis of the phenomenon of offshoring in order to try to understand its evolution and what were the main motivations that pushed companies to relocate certain activities. The second chapter will be devoted to the phenomenon of backshoring, where an overview of current literature will be used to define and describe this type of business relocation.

The last chapter, instead, through an exploratory analysis on 59 backshoring operations in Italy, shows that the time elapsed between the choice of offshoring and

backshoring, and the distance (cultural and psychic) between the country of origin and the foreign country from which the reentry takes place are two significant variables to explain the variety of cases. The distance represents the organizational key to be considered as a proxy for the risk of missing or insufficient computation of hidden costs associated with the management of delocalized activities. For this reason it is reasonable to include the psychic distance between the hidden costs taken into account by the Schulte model. In particular, it emerges that the psychic distance, as well as the geographical and cultural distance, influences the decision of the backshoring even if the managers still have a low perception of those factors at a geographical but also cultural level that disturb the flow of information between the company and the target market.

CHAPTER 1. FROM OFFSHORING TO RESHORING

1.1 Internationalization, a linear consequence of globalization. Theoretical perspectives.

Globalization is thus a social phenomenon that originates, expands and enhances the interdependencies and the exchanges around the world and, at the same time, promotes people's awareness of the deep connections between local and global by realizing a metamorphosis in terms of intensity, extension, rapidity.

Technologies applied to transport and communications have cancelled time and space distances, accelerating economic processes characterized by fuzziness of the modes and the rapid obsolescence of production processes and products. In every context, however, the individual is bound to evaluate the distance intrinsically, with a subjective perspective, he does not usually associate a spatial unit of measurement, but a temporal horizon or even more of a journey time.

But the geographic or temporal distance is just one of the facets that can meet the term "distance", infact very important concepts such as cultural distance and psychic distance exist and will be thoroughly analyzed in the following. Various scholarly authors of internationalization processes have become aware of the centrality of these concepts for strategic management decisions and have left abundant literature. This multidimensionality of the distance idea allows for a deeper analysis of the trade of goods, people and ideas that definitively sanction the hybridization between various internationalization strategies.

Business engagement horizons have widened, boundaries between markets are getting less and less clear, and two-way interdependence has increased. These transformations are the linear consequence of the globalization phenomenon that necessarily leads to the internationalization of markets (Valdani, Bertoli, 2006), a phenomenon that has changed the relationship between enterprise and markets, its

planning and management. In this context, the concepts of globalization and internationalization tend to fade, partly overlap.

Giddens (1994, p. 64) defines the globalization as *an «increase in intensity, in world social relations, that connect individuals and distant locations, so that local circumstances are shaped by events that occur thousands of miles away and vice versa»*.

So, people inevitably find themselves in a mix of economic, technological, cultural relationships that characterize the twenty-first century.

Internationalization is not simply an export activity, much less that kind of export that merely delivers the final product to foreign importers in order to place it at local retail outlets with their organization and under their control. Internationalization is thus the process through which companies can increase their sales on foreign markets and from these markets or others they can draw for the supply of raw materials, financial resources, equipment, plants, technology and workforce (Dematté 2003).

The choice of internationalization is a strategic choice because it changes the structure of the company and entails a transformation of its structure. Internationalization does not just look for new outlet markets, or supply spaces, or where to set up production or research and development, or even trace financial squares from which to take risk or credit capital because these are the applications of an upstream decision in which the firm chooses to revise its strategic axis by opening its value chain beyond the state where it is located. It is for this reason that the decision to internationalize is never a fully-fledged and systemic approach, because it is characterized by limited rationality and a high degree of uncertainty. The mass of necessary information would be too high and the time and money to plan it at would be too expensive. Instead, it is a "homeostatic learning" (Demattè, Perretti, 2003) that raises or abandons previous hypotheses. Internationalization of businesses is therefore an extremely articulated process that involves "the degree of connection that the cognitive circuit of the single enterprise has in the major global networks, where it is acquired to know codified, whether it is contained in machines, technology materials, components, finished products, services, software licenses, or other cognitive artefacts (Rullani, 1994).

For companies, the process of internationalization is therefore a prerogative for the challenge played in the fields of innovation, production networks and skilled skills.

The prolonged economic crisis has led to a downsizing of the Italian production system, with a significant reduction in the number of companies, employees and added value in all segments of activity. At the same time, these dynamics favoured a general consolidation of the economic and financial conditions of the system as a result of a selection process that has produced a recompose of firm fabric to the more financially solid. Starting in 2011, there was also a large gap between domestic and foreign demand that still shows no signs of closure. In the years of sharp decline in domestic demand, therefore, the ability to sell on foreign markets has been a key factor both for the survival and competitiveness of Italian companies. With the persistence of the crisis, however, in addition to the ability to export, it has become crucial for businesses to intensify foreign trade (a high share of exported turnover and indicative of less dependence on the internal market) and, above all, to stimulate an evolution in forms of participation in international markets. With regard to this last circumstance, in particular, the adoption of more complex forms of internationalization - such as for example broad geographic diversification of their markets or for export and import activities - was accompanied by performance generally better in terms of job creation and added value (Istat, 2017).

On the basis of these considerations, the set of stresses that the economic cycle has exerted on the productive fabric makes it appropriate to analyze the links between the economic and financial conditions of enterprises, their forms of internationalization and performance on international markets during the cyclical recovery period of 2014-2016.

As previously stated, international trade has always existed, even before the borders, the cities and the states. Hymer (1960) began to talk about the internationalization of businesses since the '60s. In previous years, researchers focused on the factors of production or interest rate differentials. Theories of international trade are classified by Perretti (Demattè, Perretti, 2003) in three lines:

- Pre-hymer theory;
- Hymer;
- Post Hymer Theories.

1.1.1 The Pre-Hymer Theories

Adam Smith proposes the "Theory of Absolute Advancement" in the *Wealth of Nations* (1776). The theory of absolute advantage shows that two countries benefit from the exchange when the first is more efficient because it has an absolute advantage in the production of goods and services, but at the same time is not in the same position in a second good production that it needs. The second country is in this position. On this occasion the market opportunity for the two countries arises. International trade, therefore, allows each country to specialize in productions where it is more efficient.

This theory is refined by Ricardo with the exhibition of "Theory of Comparative Advantage" in the *Principles of Political Economy and Taxation* (1817). Comparative advantage theory identifies a comparative advantage situation when a country has a lower cost opportunity in producing than other countries. It is therefore a relative advantage because the country should not only produce goods where it has an absolute advantage, but also those where they are the best in comparison to other countries. In this case, opportunity cost represents the sacrifice that the economic operator accepts when it makes a decision, that is, the value of the best avoided alternative.

Finally, Ricardian theory is resumed and modified by Heckscher and Ohlin in the "Theory of Factoring Facilities" outlined in *The Effects of Foreign Trade on Heckscher's Income Distribution* (1919) and Ohlin's *Interregional and International Trade* (1933). The authors insert the concept of inequalities into the productive factors. The theory of factories provides that a country import a good when to produce it is low on productive factor or this is very expensive, while exporting the good for which production requires the intensive use of a relatively generous production factor and low expensive in the origin country.

1.1.2 The Hymer theory. The theory of market imperfections and monopolistic advantages

After World War II, theories of Adam Smith, Ricardo, Heckscher and Ohlin, respectively, become inadequate to identify those economic phenomena that were taking off as trade and foreign direct investments. These phenomena were not attributable only

to macroeconomic variables or to the production factors or interest rate differentials, but also they were indissolubly tied to the international expansion process of companies.

Stephen Hymer in the "Theory of Monopolistic Benefits and Market Blemishes" (1960) sanctions the transition from a macro vision (referring to the nation) to a micro vision (referred to the company). Hymer's theory proposes the concept of *liability of foreignness*, that is, "an enterprise established in a foreign country that is subject to all the disadvantages associated with its condition of non-national society." In fact, foreign companies have to overcome the barriers to entry, which are consciously or unknowingly established by foreign countries such as laws, political and economic system, language and culture. Usually, the advantage that a company enjoys in its country of origin is superior because it is not attenuated by over-exposed barriers. On other occasions, the benefits of internationalization may be higher because competitors in the host country may not have the same foreign technology or expertise as the technology, skills and knowledge of the foreign enterprise or supply channels so that they can compensate for the limiting effects of entry barriers. The market imperfections and the monopoly benefits that companies enjoy in their own country, but which can be re-launched in the international dimension, are the motivations that drive businesses to enter the international system (Demattè, Perretti, 2003). Internationalization of businesses can therefore be attributed to some advantages (Bain, 1956). The result is a revolution due to the change of perspective (replacing the nation with the enterprise), but the author remains bound to the previous settings because both the membership to a specific nation (resulting in uneven capacity distributions and presence or a lack of natural resources, elements that derive from casual historical events or development contexts) both the interpretative category of the benefit concept continue to be fundamental.

1.1.3 The Post-Hymer Theories

1.1.3.1 The Theory of the Eclectic Paradigm

Until the second half of the 20th century, most of the mainstream theories regarding FDI explained only partial aspects of the internationalisation process of production. Some theories focused on the countries' characteristics (factor endowments)

and others concentrated only on the role of firms (neoclassical approach). Approximately twenty years after Hymer's studies, John H. Dunning (OLI paradigm, 1988, 1998), the New Trade Theory (Markusen *et al.*, 1995, 1999, and 2001) and other approaches to consider both the theory of firms and the international trade theory that explains the determinants of FDI and the role of multinational enterprises.

Dunning (1981) conceptualises Hymer's thinking in a model, also known as "eclectic theory": "Ownership - Location - Internalization" (OLI), which summarizes the reasons which lead the enterprise to become a multinational enterprise. This approach assumes that three conditions are met for an enterprise to decide to make FDI.

1. *ownership advantages* of competition and experience (therefore of intangible assets), from a technological and organizational point of view, through which the company, which wants to become multinational, would have a competitive position over the competitors of the market in which it operates (Federico, 2006). Intangible capital held has two characteristics:

- transferability, as it can be transferred from country to country without shipping costs¹;

- *not rivalry*², can be used simultaneously in multiple businesses and in multiple plants without ever having to. With regard to this, literature subsequently, assuming that the company is a multinational company, clarifies the types of benefits that derive from productive factors that can be used in multiple plants, even at the same time, that give rise to the *Enterprise-wide scale economies* (managerial and organizational skills, exclusive technological know-how, good brand reputation) that enable the multinational enterprise to cut costs due to duplication of production units and, in the presence of FDI, the related ones on the acquisition of information on institutions, on organization, on local business practices and on linguistic and cultural barriers (Federico, 2006)³.

¹An example might be that of the chemical formula of a medicine that can be forwarded via email from one plant to another

²*Non-rivalry* is a feature of public goods, since the use of a subject does not preclude another from being able to use it in the same time.

³It is clear that it is assumed to be in a context characterized by asymmetry and incompleteness of information, under oligopoly or imperfect competition and unavailability of good technology where financial wealth and physical capital count less than *knowledge capital* and *invisible assets* (Federico, 2006).

2. Depending on the ability to achieve benefits when the company is located in a foreign country (availability of raw materials, quality and labor costs and energy, availability and quality of infrastructure, product transport cost) the company evaluates the convenience to delocate the production abroad (*location advantage*). This advantage exists where the company acquires a foreign firm that already operates in the outbound market by cancelling transaction costs (De Arcangelis, 2009). In this case, the benefits are those that derive both from horizontal foreign direct investment and from vertical foreign direct investment (Federico, 2006).

3. Choose to keep some productive activities within the company by internalizing the exploitation of the proprietary benefits instead of assigning licenses or subcontracting agreements with independent foreign patents, then outsourcing business lines: *make or buy*. Choice depends on the characteristics of both the host country and the industry in which the company is part. The convenience of making FDI exists when the enterprise belongs to areas characterized by a high risk of appropriation because intangible assets and the technology factor are particularly relevant or operate in highly capital-intensive sectors where the purpose is to preserve investments made by opportunistic conduct by local producers. On the contrary, it is more convenient to use the subcontractor when it comes to labor-intensive sectors (Federico, 2006).

The variables on which the OLI model is based are a combination of the characteristics of an enterprise, a sector and a country, but which are often not easily perceptible and therefore verifiable at the empirical level (Onida, 2004).

In an effort to make eclectic theory confirmable, Dunning (1981) proposes to group *ownership advantages*, *internalization advantages* and *localization advantages* of multinational companies, taking three sets of explanatory variables that reflect the trade-off in investment decisions abroad for companies: *firm-specific determinants*, *country-specific determinants*, *industry-specific determinants*.

Firm-specific determinants (business-level determinants: whether to invest abroad or not) consist of business size, productivity, inventory of acquired skills (industrial secrets, age, experience, R&D, patents) and market power. These variables are analyzed through discrete models, observing the likelihood that an enterprise will make an FDI, regardless of its amount. In different literature, studies are carried out on each of these

characteristics: according to a study conducted by Infante *et al.* (2000), the *size* of the enterprise is an element that strongly influences the choice of investing abroad or not . Instead from Helpman, Melitz and Yeaple (2004) study emerge that the *degree of productivity* of an enterprise is also a decisive factor in choosing to invest abroad. In fact, less productive businesses choose to export or even continue to operate in their home country rather than investing across borders, as they are not in a position to manage the fixed costs that they need for FDI. This is also demonstrated by microeconomic evidence, as multinationals have a higher average labor productivity than the export companies, and in particular households (Federico, 2006).

Country-specific determinants (how to invest in that particular country) relate to quantifying the amount based on data derived from a number of not only economic aspects (such as market size, cost and quality labor costs, purchasing power, energy costs, distance from other outlet markets, transport costs, raw material costs, *external economies* related to the availability and quality of local suppliers), but also institutional (taxation, linguistic-cultural distance, degree of customs protection, local legislation and patent regimes, investment flows or other indicators of productive activity abroad such as turnover, added value of affiliates or employment) (Onida, 2004).

These types of variables have an equal impact on the different types of FDI. In horizontal investments, companies tend to locate the various stages of the production process in different countries, reducing transport and communication costs. Instead, in the case of vertical ones, the firm bases its choice by combining two factors: on the one hand it reflects a reduction in production costs that corresponds to organizational difficulties (resulting from fragmentation of production) others consider the size of the market in which it operates (if large, in fact, decides to invest) and the extent of customs barriers or other costs (so export is less costly) (Federico, 2006).

Industry-specific determinants relate to market form (among others, barriers to entry, bid concentration, complexity across the value chain, public demand, product differentiation), degree of technological opportunity (the speed of advancement of the innovative frontier), the conditions of *innovative endowment appropriateness* by the innovating firm and incidence of transport costs, dynamic scale economies and static

scale economies⁴. While dynamic scale economies (at enterprise and learning level) favour FDI, because it is convenient to increase the number of plants on which to distribute the intangible capital production cost by expanding abroad, the static economies of scale (plant and district) instead discourage them, as the average costs decrease by concentrating production on a single plant (Onida, 2004). Therefore, the distinction and the presence of scale economy at enterprise and plant level is important, as there are significant economies of scale in the case of large companies, which will try to expand their sales in many countries (BARBA NAVARETTI, VENABLES, 2004).

The criticisms that have been made to theory illustrated concern the fact that it is not based on a general equilibrium context, but merely tracks a set of conditions that make the economic environment so as to stimulate FDI but less trade or other contractual forms (Reganati, 2003).

The analysis of the choice of entry mode of multinational enterprises into a foreign market is largely based on two analytical paradigms, namely, the eclectic paradigm of Dunning, especially the internalisation approach, and the transaction cost approach. Buckley and Casson (1976) present the first comprehensive research devoted to internalisation theory as it applies to multinational enterprises, developing a theory of multinationals based on the concept of internalisation, particularly with regard to knowledge, transaction cost and market imperfections. This work differs from its antecedents which mainly explored ownership and location frameworks, and concentrates its analysis on internalisation, giving a more dynamic approach to multinational enterprises. This study has had a considerable influence on the literature on multinational

⁴When the volume of production grows, the unit cost is reduced and economies of scale are reduced. One of the key elements that contributes to determining it is the ability to distribute fixed costs to a higher number of units produced. For example, Microsoft realizes economies of scale by distributing the fixed cost of supporting a new Windows operating system on each personal computer on which it will install its new operating system (Hill, 2007). At a practical level it is difficult to measure these two types of economies of scale, in fact, various methods have been used in literature. For example, Brainard uses plant-scale economies as the number of workers in the median plant, and instead, as a measure of economies of scale at enterprise level, the number of non-production workers Media headquartered in the country of origin. Measurement could also be carried out by identifying the company's specific assets, including know-how about product design or production processes, reputation in relation to product quality or brand or brand image. Because, despite being intangible, they have significant costs. Other studies have taken into account, instead, the advertising of the brand, noting a positive relationship between FDI and the intensity of advertising. Finally, another method of measuring FDI is investment in R & D, which largely tends to generate FDI (Onida, 2004).

enterprises and particularly on international business. International business economists believe that firm-specific assets are better exploited internally (internal route, wholly-owned subsidiaries) rather than through markets by licence (arm's length, external route). In fact, although transaction costs of a foreign subsidiary are high, the cost of licensing, for example, can be higher.

The starting point of this analysis is that a multinational owns the firm's specific asset that can generate economic rents. These rents can be earned by simply exporting the product (e.g. through trade) or licensing a foreign firm (licensee) to distribute the product (examples of the so-called external route). However, these modes of entry, licensing in particular, have high costs and risks, such as opportunistic behaviour by the licensee. Opportunistic behaviour, transaction costs in the external market, lack of knowledge in a foreign market, risk and uncertainty, asymmetric information, moral hazard, adverse selection, incomplete contracting and market failures are some of the main topics analysed in internalisation theory. Hence, internalisation within a multinational is designed to reduce transaction costs and market failures by replacing imperfect 'external' markets with the hierarchy (horizontal or vertical) of the multinational enterprises. In particular, the presence of internalisation advantages induces multinationals to retain the control of their asset located abroad (wholly-owned subsidiaries) since it gives improved guarantees in terms of protecting intangible assets, particularly when the legal environment in the host country is weak (this is an example of the internal route pursued by a multinational when deciding to invest abroad). The first reason for internalisation is linked to characteristics of knowledge: the non-excludability property of new knowledge. In fact, a firm does not want to reveal, for example, product technology to potential licensees since they could reject a deal and copy the technology at lower cost. A second reason concerns information asymmetry problems related to new or complex products. For example, licensees recognise that a firm lacks incentives to reveal real product quality. In this case, it is possible to envisage the problem of incomplete contracts. Another problem is when the new knowledge transferred to a foreign subsidiary is easily learned by the new licensees, who can, in turn, start a new domestic firm in competition with the multinational enterprise. Therefore, multinational firms have strong incentives to internalise the advantages by choosing FDI, rather than giving licenses or selling firm-

specific assets, such as patents, to other firms. For this reason the internalisation theory predicts, and empirical evidence confirms, that multinationals prefer wholly-owned subsidiaries over minority ownership (i.e. joint venture) or arm's length transactions.

In Dunning's OLI paradigm (1998) the MNEs are seen as firms which internalise a specific ownership advantage that provides them with some market power. Firms are willing to exploit this through FDI instead of exports in order to benefit from some location advantage and to avoid the possible asset dissipation that may occur, for example, with licensing. Additionally, it is important to note that the distinguishing features of direct investment are both control and transfer of knowledge. Producing abroad can be accomplished through subsidiary production or licensing, franchising, or another mode of entry such as joint venture or merger and acquisition. Some modes of entry in a foreign market may be more appropriate than others under different circumstances and each is an important factor in the project's success.

The transaction cost approach argues that a rational firm chooses the alternative that minimises the cost of operations subsequent to entry. For example, the acquisition of a firm in the host country enables a multinational to retain control of its 'technology', reduces or eliminates the cost of pulling resources together to build a firm, and endows it with both business relationships and knowledge about the local markets and institutions. However, it then has to bear the cost of integrating the production structure, organisational structure and corporate culture of the acquired firm into its own.

1.1.3.2 International Product Lifecycle Theory

This model portrays trade and FDI as a dynamic adjustment mechanism for those rapidly evolving environments. It creates a correlation between the product life cycle phases and trade (Vernon, 1979).

The *first stage* of the life cycle is the original creation and the launch of a product in the market. At this stage it is crucial to identify the new product that satisfies the demand of the domestic market and then export it to a foreign market with similar preferences.

The *second stage* is maturity. The product is standardized and market demand becomes more flexible than the price. In addition, the company needs to get more cost-effectiveness and this involves locating production overseas in order to reduce production costs.

In the *third stage* of the cycle, the product reaches its maturity stage and becomes fully standardized. National demand reaches a level of saturation and, in order for businesses survival, they have to compete in terms of cost. Thus, the innovative enterprise moves production abroad, especially in countries where labor costs are lower and can export goods to the world market.

The Product Lifecycle Model has been able to identify the elements that lead to the determination of the comparative advantage that changes with the product age and the evolution of the external environment. But this model was originally designed to analyze the innovative thrust of USA multinational corporations and their expansion abroad during the 1950s and 1960s, so it does not take into account the modalities and causes of innovations in countries other than USA. The predictive capacity of the model is fragile, because it is not able to determine the times of realization of the different phases, and because its applicability is basically limited to consumer goods.

The transformations that took place in the international economic environment brought Vernon to question the validity of the product life cycle hypothesis for two reasons: several countries were reaching the United States' income and labor cost level, product cycle has been shortened since the technology diffusion process has intensified (Reganati, 2003).

1.1.3.3 The Uppsala model

The model of Uppsala theorized by Johanson and Valhne (1977, 1980, 2009) is also referred to as a "Behavioural or procedural approach" and focuses mainly on the work of Cyert and March (1963), Penrose (1966) and Aharoni (1966). The *Uppsala model* basic concepts are:

- *Experiential knowledge,*
- *Establishment chain,*

- *Psychic distance*,
- *Liability of foreignness*,
- *Business network*,
- *Trust*.

These concepts are two to two connected, because the second is almost the solution of the first.

Internationalization appears to be a process of evolutionary growth, driven by sequential and incremental involvement stages where the company moves as a limited-scale actor that through experience stores market knowledge and with adaptation responds to internal and external change. The company gradually grows its international expansion through *objective knowledge* and *experiential knowledge* that can only be acquired through *learning by doing* or personal experience.

Learning and knowledge are as connectors between the various phases, allowing to reduce the perception of risk and uncertainty, constituting one of the *driving forces* of the expansive process, learning in fact plays a strategic role (Hofstede 1980, Johanson E Vahlne, 1990).

The *chain establishment* is therefore the process of expansion abroad which envisages an initial export activity and a subsequent transition to the form of intermediation (independent agents representing the company in foreign territory and carrying out indirect export activities on its behalf). Subsequently, with the increase in sales, the company creates sales subsidiaries for direct export and, given the constant increase in demand for products, subsequently also develop subsidiaries abroad with the aim of avoiding and overcoming commercial barriers (Johanson e Vahlne, 1990, 2009).

Mobility from one previous stage to one depend on the *current variables* derived from the current situation (knowledge acquired on the market, resources and investments in the same) and the *variables of change* associated with increasing adjustments and environmental and internal evolutions. More the company engages market knowledge, lower will be the perception of the risk and greater will be the investment in the foreign country.

The process is therefore incremental because it moves towards more and more entrenched entry procedures (gradual investment in single market) and because it passes

from countries with little psychic distance (culturally closer, geographically and as a degree of economic development where opportunities and less uncertainty are seen) to more distant countries on the strategic and managerial level (grading in the choice of markets). The psychic distance, as will be amply described in the following paragraphs, is formed by all those factors, such as differences in language, culture, and political system, that disturbs the flow of information between the company and the market (Johanson and Vahlne, 1977).

Johanson and Wiedersheim-Paul (1975), Boyacigiller (1990), Evans (2000) include in this sum of factors the differences in language, culture, political systems, education, degree of industrial development and in marketing infrastructures. As a consequence, greater the psychic distance will be, greater will be the liability of foreignness (Johanson and Vahlne, 2009).

The *liability of foreignness* is a concept that emerges around the '80s by identifying the difficulties that the company faces when it comes to being in a other country than the one where it was born. The *liability of foreignness* is defined as the set of foreign management costs that are associated with the position of a company operating in a foreign market that causes a competitive disadvantage due to additional costs that would not exist for a local company (Zaheer 1995).

These *social costs* can be distinguished in three categories:

- Costs due to the company's lack of knowledge and familiarity with the environment (Johanson and Vahlne, 1990);
- Costs directly derived from physical and geographic distance: costs for transport, travel, coordination between sparsely distant areas (Eden and Miller 2004, Zaheer 1995);
- Costs to the host country: economic nationalism, lack of legitimacy for foreign companies (Eden and Miller 2004).

The experience allows to store information on markets and to open more and more to the process of internationalization. But, when the perceived risk exceeds the tolerability threshold, there is a barrier to involvement and mobility.

Internationalization at stages can be showed <<*like rings in the water*>> (Madsen and Servais, 1997) for its sequentiality due to the uncertainty of decision-making and lack of skills.

Theoretical developments, changes in business practices, and criticisms to the model (faster internationalization due to greater homogenization of markets, lower transaction costs, developed overseas managers experience, etc.) led to a revision of the model of Uppsala in 2009. The market no longer appears like a sum of independent suppliers and customers; instead, they are the business network, a network of people who exchange information each other, in the medium and long term relationships; the industrial network expects that a company's relationships can be used as bridges with other networks (Johanson and Vahlne, 2009). From the encounter between retailers and customers, inevitably comes an exchange that brings knowledge to one another, raising both for their own cultural baggage. Prerequisites for the intersection of these subjects and for the creation of networks is the trust that arises from being part of the same entity. Trust is an important ingredient for successful learning and knowledge development. Confidence can also replace knowledge; for example, when a company lacks a necessary knowledge of the market, it allows, through a trusted mediator, to conduct foreign affairs (Johanson and Vahlne, 2009).

The Uppsala model, revisited in 2009, adds a further new central concept: the problems and opportunities faced by a company facing the international horizon are less dependent on the country and increasingly a matter of relationships and networks. The *liability of foreignness* is the biggest problem in entering a new country, but the *liability of outsidership* is a difficulty that can also occur in the domestic market. The liability of foreignness can be overcome through organizational learning: the perception of distance contracts and becomes the liability of outsidership, or complexity resulting from extinction from a corporate network. The challenge that every company has to overcome is to become an insider in every business network in which it has a business. Being part of a network is indispensable for the success of internationalization because relationships between people and companies give the opportunity to learn and build trust and commitment, a prerequisite for internationalization. The process of learning, building estimates and assuming liability allows you to pass from an outsider to an insider.

1.1.3.4 The new theory of international trade

The likelihood that exploitation of economies of scale by companies could have significant implications on international trade was the starting point for the new international trade theory developed at the end of the 1970s. This theory provides two important contributions:

- through economies of scale, international trade can offer to consumers a wide range of products while lowering the average cost of production;
- when companies need to produce by satisfying a large proportion of world demand in order to obtain economies of scale, the market is able to manage with a small number of businesses.

Therefore, international trade in certain products can be controlled by some countries whose businesses have been able to produce those products before all the others (Hill, 2007).

Much of the New Classical and New Trade Theory (NTT) provides support for the increase in the importance of trade between industrialized countries and the prevalence of specialization (horizontal and vertical models) (Markusen and Venables, 1998, Markusen, 1999). Usually, a multinational company creates new business in other countries (host or recipient country). As a result, production is geographically divided between different countries. As described by Markusen (1999), there are two ways in which a company can divide its production and become multinational. The first is to duplicate some of its activities by building a plant in a foreign country (the *host economy*) in addition to that installed in the home country (*domestic economy*).

Some studies (Markusen and Markus, 2001, Markusen and Venables, 1999) argue that FDI are among the wealthiest countries. Therefore, multinational companies install production facilities in similarly high-wage countries, which is reliable with the prospect that foreign direct investment is more driven by market access than wage differentials.

Moreover, according to the *convergence hypothesis* (Markusen and Venables, 1999), countries converge on the relative size, factor allocations and production costs. Markusen (1999, 2001) explains why the largest and most profitable developing countries, such as Brazil and China are the countries that attract more FDI. The

motivation for this approach is that developing countries have the ability to export a large part of their production to the mother country of the multinational company that invested there. Multinational companies need skilled local labor and reasonable infrastructure to build a final product and these requirements are only found in high-income developing countries. The size of a country is important because not all final production has to be shipped to the mother country and is instead consumed by the local market.

1.2 Entry mode. The gradual process of internationalization

The *Stage Model* (Johanson and Vahlne 1977, 1990, 2009) shows the concept of graduation both focusing first in countries closer to the source, in order to open later on more markets, and in the growth of complexity of entry mode in the country, starting from exports to joint ventures.

Each mode of entry into the market has a different degree of risk depending on the investment needed and the level of control that the company holds. The various forms of internationalization will be analyzed in the paragraph.

This graduality is frequently observed in the processes of internationalization of enterprises and reflect the essence of investment planning and risk management (Shenkar and Luo, 2008). Demonstrating elements of the company's degree of engagement arise from different entry modes:

- *strategic control*: linked to the ability to influence systems, the choices of foreign subjects which determines the future of a business;

- *assuming liability*: it sets the degree of interdependence that the foreign company will connect to the home country enterprise, the more control it will hold, the more investments will be in economic and temporal terms, thus exposing itself to an higher risk;

- *the degree of flexibility*: decreases if the complexity of the chosen mode increases. It will be difficult to recover the investments in a short time and without considerable losses to get well.

The causes that drive companies to internationalization are associated with external stimuli (domestic market stagnation, foreign market develop higher than

domestic one, foreign customers shifting) and internally (holding a competitive advantage, excess production capacity, cyclical or seasonal productions, participation in fairs or international events, unexpected foreign orders, business agent maneuvers).

The plan of an internationalization often, especially in the Italian reality of small and medium-sized businesses, remains a theoretical exercise defeated by a practice that is interwoven between attempts, highly dependent on the case and the coincidences. The strategy will plan the company's goals in terms of the resources and time horizon in which the company decides to engage.

Demattè (2003) classifies the foreign presence in:

- Contractual presence arrangements for outlet markets;
- Export-based presence modes;
- Direct presence with investment.

1.2.1 Contractual presence arrangements for outlet markets

Contractual terms are equivalent to long-term partnerships between the company and a local counterpart, so as to share the risks of the asset while simultaneously enjoying the mutual benefits. The main contractual terms are:

- The *International Licensing* (productive and/or commercial) or *contractual franchising*. The first is a contract whereby a subject (licensor or licensor) transfers to a foreign subject (licensee or licensee) the right to exploit, in a specific geographical area, a particular product or tangible or intangible asset of its own (brand, logo, technology, codified knowledge) by paying royalties to the licensor. Then, it will be the licensee to invest in the business, by taking on business risk, but also the risks associated with the company's position are remarkable. In fact, for the duration of the contract, the licensee enjoys decision-making autonomy in the marketing and distribution plan, and once the collaboration is concluded, the know-how transmitted may have contributed to creating a local competitor. *Contractual franchising* is a form of contractual agreement in which the franchisor gives the local entrepreneur, the franchisee, the right to use the commercial formula, the know-how, the organizational and marketing competencies for a fee of access and royalties. It represents a win-win game where the franchisor expands its

business with a restrained degree of risk and the franchisee uses a well known and appreciated brand. There are other types of contracts that characterize entry modes: *piggy back* ('bring weight on the shoulders') provides that the *rider* (company) introduces his products to the distribution of another carrier (carrier) that presents a complementary assortment;

- *Management Contract*. The owner of a chain of stores grants it to a foreign firm with experience in the industry;

- *Turnkey Contracts*. The foreign company creates a sales point or a manufacturing factory and once it is launched it gives it to the local investor. This takes advantage of the knowledge of the foreign company which, in turn, has the opportunity to sell its products and create relationships in the market;

- *Contract manufacturing*. Contracts concerning the production dimension, through which the company delegates the production of the product or some of its components to a foreign company. The reasons may be the exploitation of the low labor cost, the reduction of transport costs and duties when it is decided to sell in the same market where it has been delocalized;

- *Assembly Agreement*. The company transfers the parts of the product abroad which will be assembled and then re-inserted into the national territory for marketing;

- *Original Equipment Manufacturer (OEM) Contract*. The company acquires a foreign product from a foreign counterpart and then retracts and sells it as its own.

1.2.2 Export-based presence modes

Export is the transfer of goods and services across national boundaries using direct or indirect channels (Young, Hamill, Wheeler and Davies, 1989). Exports are characterized by a very limited risk, the objective should be of a cognitive nature: to understand whether or not there is a market opportunity; if it there is, use it with a more complex planning, if it there isn't to exit the market deteriorating an almost.

Export methods may be direct or indirect.

Direct exports occur when intermediaries operate on behalf of the enterprise, on this the export risk is affected. The company will be able to leverage control over the distribution, the price and the contribution of the bilateral exchange of information.

Direct export channels are:

- *Dealer*. Tasks and roles are similar to the distributor but are simultaneously wholesaler and retailer.

- *Distributor*. Wholesaler who buys the ownership of the products and has the exclusive sale in a specific geographic area. It manages the logistical aspects, the promotion activities and may indicate revisions and new versions of the product given its proximity to the foreign target;

- *Importer*. This is a figure similar to the distributor, but it does not have the sales exclusivity while simultaneously representing competing companies;

In *indirect exports*, the company does not transfer any value chain activities, in fact an intermediary (aware of the local market) carries out export activities on its own behalf or on behalf of third parties. In this way the company has a null market control and a very limited knowledge of the same. The main types of intermediaries in indirect exports are:

- *Trading Companies*. Large-scale operators managing simultaneously export and import by offering the company's marketing, financial and logistics services specific to the foreign context;

- *Brokers*. Links between the producer and the foreign customer potential that facilitate the operation, for this distinctive feature their commitment is temporary and short-term;

- *Buying offices or buyers*. Commercial brokers who buy for third parties and support the business with suggestions for the product to be more compatible with the foreign target by also providing logistical facilities;

- *Export Companies*. Businesses conducting export activities for companies belonging to the same compartment and not competing among them;

- *Export consortia*. Associations between several companies to jointly carry out the necessary activities, divided into single-sector or multi-sectoral, and promotional or sales.

1.2.3 Entry Mode with Direct Investment

Direct presence arrangements are made up of investments made in a foreign country so as to obtain lasting interest and control. They involve the purchase of a production plant or the creation of a new plant that can be owned or shared by more than one market participant. Foreign direct investment (FDI) is the most risky mode, but it ensures full control over the activities. Alternative types of investment are:

- *Contractual Joint Ventures*: are strategic alliances created to carry out marketing, technology or production projects without the creation of a new company;
- *Equity Joint Ventures*: are mixed capital companies originating from parent companies with capital, tangible or intangible assets;
- *Wholly foreign-owned companies*: they need adaptation skills, long-term perseverance and experience. We can distinguish Greenfield investments that provide for the creation of a new company and Brownfield investments by purchasing an existing company.

These input types combine the high risk and use of investments with total control of each stage of the production and marketing process, often translating into a very effective entry mode.

1.2.3.1 Foreign Direct Investment (FDI) and multinational companies

There are several definitions that have been attributed to the concept of foreign direct investment.

The International Monetary Fund in 1993, the fifth edition of the Balance of payments manual, the Organization for Economic Cooperation and Development (OECD) in 1996, the third edition of the Detailed benchmark definition of foreign direct investment and the United Nations Congress on Trade and Development (UNCTAD) are agreed to define that “*Direct investment is the category of international investment that reflects the objective of a resident entity in one economy obtaining a lasting interest in an enterprise resident in another economy. (The resident entity is the direct investor and the enterprise is the direct investment enterprise.) The lasting interest implies the existence of*

a long-term relationship between the direct investor and the enterprise and a significant degree of influence by the investor on the management of the enterprise. Direct investment comprises not only the initial transaction establishing the relationship between the investor and the enterprise but also all subsequent transactions between them and among affiliated enterprises, both incorporated and unincorporated". In this definition the item "interest" takes on particular importance. First, the desire to "acquire a lasting interest of an enterprise resident in another economy" is the crucial goal of foreign direct investment and not a short-term objective, but a lasting interest, as there is a real relationship between the direct investor and the foreign company. Secondly, interest is not confined solely to the financial aspect, but also to the managerial aspect (*a significant degree of influence of the investor on the management of the enterprise*), as the direct investor acquires the right to significantly influence the management of the company on which it decided to invest⁵.

In addition, the International Monetary Fund in 1993, in the fifth edition of the Balance of Payments Manual, coincides with the concept of foreign direct investment with the concept of a multinational enterprise: *«an incorporated or unincorporated enterprise in which a direct investor, who is resident in another economy, owns 10 percent or more of the ordinary shares or voting power (for an incorporated enterprise) or the equivalent (for an unincorporated enterprise)», but "(...) some countries may choose to allow for two qualifications (...). First, if the direct investor owns less than 10 percent (or none) of the ordinary shares or voting power of the enterprise but has an effective voice in management, the enterprise may be included. Second, if the investor owns 10 percent or more but does not have an effective voice in management, the enterprise may be excluded».*

In addition, for direct investment firms are meant: *"those entities that are:*

- *subsidiaries (a non resident investor owns more than 50 percent);*
- *associates (an investor owns 50 percent or less);*

⁵Significant influence on company management is a key factor to not confuse the concept of foreign direct investment with portfolio investment. In fact, portfolio investment is a mere financial investment by individuals not involved in business management, and unlike foreign direct investment, they can be easily de-invested.

- *branches (wholly or jointly owned unincorporated enterprises) either directly or indirectly owned by the direct investor.*

«*Subsidiaries in this connotation also may be identified as majority owned affiliates. Foreign-controlled enterprises include subsidiaries and branches, but associates may be included or excluded by individual countries according to their qualitative assessments of foreign control*»(IMF, 1993)⁶:

Thus, a multinational enterprise is that company that differs from a simple enterprise and which carries on international trade through imports and exports since it carries out its productive activity as well as its distribution and marketing function in at least two countries (Onida, 2004). For this reason, it will be constituted by a parent undertaking and one or more affiliated companies owned or controlled by it (Reganati, 2003).

It is the origin of capital transactions that are called direct foreign investments in the balance of payments accounts, which are distinguished by other purely financial transactions (loans, securities investments, trade credits, etc.) and portfolio investments (Onida, 2004).

1.2.3.2 Different Types of FDI

Different types of foreign direct investment can be distinguished. Depending on the *location* where the survey is conducted there are *Inward foreign direct investment* when carried out in the reporting country and *Outgoing Foreign Direct Investments* when it is made abroad by the country conducting the survey⁷.

Depending on the *sector* in which the company operates distinguishing *Horizontal Foreign Direct Investment* and *Vertical Foreign Direct Investments*.

The first is carried out abroad in the same sector where the firm operates within the domestic market, so as to meet demand for foreign goods and services and duplicating

⁶Direct investment firms are controlled by:

- a non-resident investor for more than 50%;
- by members controlling 50% or less;

- wholly or jointly owned subsidiaries of companies not incorporated in companies, either directly or indirectly owned by the direct investor.

⁷ It can also have entry and exit FDI in the same country and in the same sector.

the same stage of the production process. This type of investment has disadvantages and advantages: on the one hand, they are costly because the company has to bear the costs of transport, the realization of production facilities in a foreign country or the acquisition of a foreign company. They are also risky because of problems associated with the pursuit of economic activity in another country (such as the need to establish relationships with customers who have a different culture or have to know different legislation); on the other hand, they have the advantage of exploiting the natural resources in the host country (Hill, 2007) and pursuing strategies that will allow them to enter the foreign brand (Federico, 2006)⁸.

The second one (*Vertical Foreign Direct Investments*) consist in the acquisition of companies that carry out parts of the entire production process, therefore looking for productive factors at lower cost or higher quality. In this case the enterprise separates management from production in the sense that it maintains managerial functions in the country from which it comes and locates production in a country where, for example, the labor force has a lower cost or has special skills. They can be *upstream*, these are investments directed at foreign sectors that provide inputs for a domestic production process, or *downstream*, when a foreign sector sells outputs from domestic production processes an enterprise (Hill, 2007)⁹.

Based on the *reasons*, why the investment is undertaken, the investment can be

- Investing in *resource seeking* if the goal is the privileged access to essential production resources;
- *Cost saving* investments if the goal is to rationalize costs by locating value chain activities in countries where cost advantage can be achieved;

⁸ That said is one of the strategies of major Japanese automotive industries such as Toyota, Honda and Nissan, which have duplicated one of their production phases in the UK so that they can meet European demand by cutting costs and barriers to trade (Barba Navaretti, Venables, 2004).

⁹ The differences that can be drawn in relation to production costs and the endowment of factors have led to the conclusion that horizontal FDI are the most commonly used as they are most important quantitatively compared to vertical FDI. From some studies conducted by Markusen and Maskus (2002), based on the knowledge capital model, which integrates the motives of FDI and compares them to those horizontal and those vertical models, it has emerged that the integrated model gets the best effects of an exclusively vertical models, while the latter is the least costly of both the integrated model and the purely horizontal FDI model. Although these are the empirical evidence, it should be noted that these were derived from data referring to the decade from 1980 to 1990, which does not take into account the considerable influx of FDI that occurred since the '90s and which has an ever-growing trend in vertical FDI (Barba Navaretti, Venables, 2004).

- *Market seeking* investments in order to exploit competitive advantages over local businesses in the place where the company internationalizes by guaranteeing a direct presence of that foreign market;

- Investing in strategic asset seeking if the goal is access to strategically significant complementary inputs.

The first two types typically fall into the vertical FDI as they de-structure their value chain by delocalisation of certain activities, characterized by a greater but less qualified work intensity, in markets where labor costs are lower than the country of employment origin or in which there are favourable tax incentives.

The other two types mentioned above, however, fall within the horizontal FDI, as they tend to replicate their production structure in the foreign country and imply a generally-qualified job application.

While in the latter case the main purpose is to satisfy the outlet market more efficiently, in vertical FDI's model, however, is to minimize production costs. However, in most cases the two models coexist.

Depending on the set up production in a foreign country, you can have three types of investments:

- *Greenfield Investments* (FDI "Green Meadow") when the FDI create new plants and new production capacities (Onida, 2004). These operations are carried out more in developing countries (Hill, 2007).

- *mergers and acquisitions* occur where the pre-existing investment firm and the existing local business are engaged in acquisition or merger operations without causing an increase in the production capacity of goods and services in the receiving country (as is the case for Greenfields) (Onida, 2004). In this case, foreign companies have strategically valid business and for this reason the aim is to try to increase their efficiency. In addition, compared to Greenfield operations, they have the advantage of being executed more quickly and are prevalent in developed countries.

- in *joint ventures*, two or more companies cooperate and undertake to share profit, loss and control in a specific enterprise. Creating a joint venture is advantageous for those companies that do not want to get into a merger (Hill, 2007).

1.3 Strategic Agreements and Offshoring.

The crisis has been particularly devastating as it is the result of the coincidence of three factors: the financial crisis that began in August 2007 and the consequent collapse of financial sector models based on speculative surpluses; a recession that began in the second half of 2008 and a serious structural crisis related to the industrial system that begins in autumn 2008.

The combination of these three factors has characterized the economic landscape from 2009 to date. Scholars and international and national policy makers have been forced to review strategies for the global economy as well as for financial markets, since, unlike the past crises, «the most global crisis ever encountered in the economy» (FILIPPOV, KALOTAY, 2009).

Substantially, what started the 2007 financial crisis was a liquidity problem by the international financial system that in August 2007 affected London and New York following the rise in subprime mortgages in the United States¹⁰. Stock markets have fallen, large financial institutions have collapsed or have been bought by the state, governments around the world saw themselves forced to devise immediate rescue plans for their financial systems. In addition, historic private financial institutions, such as Lehman Brothers, on September 15, 2008, and nations such as Iceland, Hungary and Argentina have surrendered bankruptcy. When financial institutions are in serious difficulty in attracting capital, international bank lending is shrinking, stock exchanges

¹⁰Subprime mortgages are one of the consequences of the globalization process characterized by too much security of the power to know and monitor the risks related to the financial sphere that have allowed, in particular in the developed weights, an impressive expansion of the leverage increasingly supported by a process of Government deregulation. This allowed that, until 2006, the world was in possession of a large amount of liquidity that was not destined for developing countries, but developed countries, particularly the US. As a result, the US credit surplus has allowed finance to expand its investment opportunities through alternative financial instruments such as asset classes. This instrument has greatly affected the real estate sector, which was mistakenly thought to have maintained for a much longer time a positive and profitable trend. So you are creating new financial products related to the trend of mortgages, c.d. Subprime mortgages, granted to unemployed persons, without income and without ownership, or who in the past were not able to honor their debts to which they were not granted access to ordinary credit.

The rise in housing prices was the main cause of the indebtedness of many families. In fact, in the summer of 2007, the USA real estate bubble exploded, the value of real estate markets collapsed and mortgages increased.

The cause of the development and then the spread of subprime mortgages, however, is not to be solved only in the excess of liquidity, which is first produced by the central bank, but also in the simultaneous liberalization of capital movements (Filippov, Kalotay, 2009).

are beginning to decline and portfolio investments are declining. The central banks, in dealing with these issues, have intervened by lowering interest rates (FILIPPOV, KALOTAY, 2009).

As a result of this financial crisis, the economic downturn has weakened even more world economies. From Second post-war the recessions generally took place every 10 years and were recovered in three or four quarters, unlike what has happened in some countries in which the recession has had some effects negative only to a minimum recovered. Another difference that emerges in comparison with the 2007 crisis and the great previous crises, in particular that of '29, is the collapse of the industrial system that began to characterize all the countries since the second half of 2008. In an increasingly global slave market, in order to meet global demand for goods and services, industries have been forced to develop enormous production capacities that have, in the long run, caused a weakening into a profound recession. In general, there has been a route inversion than the past: all those factors that in the 1990s represented the premise of a long and unstoppable process of globalization (the liberalization and opening up of international exchanges by Asian continental economies, improving economic policies in Latin American countries and expanding to new banking markets that supported corporate internationalization strategies through credit) over time changed their features, slowing down the process of globalization¹¹. Today, the object of exchange is no longer largely represented by finished products but by *tasks*, leading to an international fragmentation of production processes not only of manufacturing but also of services. This recessionary phase of globalization has seen the development of *foreign direct investment*, *offshoring* and *global supply chains*, respectively, of foreign direct investment, delocalisation process and global value chains (FILIPPOV, KALOTAY, 2009).

The internationalization strategies adopted by companies take on different configurations, which may be alternatives or complementary. In implementing its own foreign expansion process, the enterprise can choose different entry modes, each of which assumes a different organizational and financial commitment, resulting in the level of

¹¹Some of the main causes were represented by the strong imbalances and distortions of the political system and, above all, economic underlying globalization: one of the most obvious and serious was the large amount of public debt of the developed countries. By contrast, developing countries, which in a physiological situation ought to have been financed by the wealthiest countries, recorded impressive trade trends that allowed them to invest by purchasing USA government bonds.

rooting in the foreign area. Offshoring strategies involve the most costly investment, both economically and organizationally.

FDI assume, in fact, the investor's intention to acquire a significant level of influence over the management of the underlying company by establishing a long-term relationship that guarantees the investor a lasting interest over time. These investments are the most advanced international expansion mode in terms of positioning the company at an international level and consistency in competitive strategy in geographic markets other than the origin market (Caroli, 2012).

In the event that an enterprise decides to place production activities in a foreign country, entry modes may be strategic alliances or fights. These ways of entry are very important even if an enterprise produces in the country of origin, but intends to develop abroad a part of the resources and skills needed to compete.

The *strategic alliances* are divided into two groups: a) strategic agreements; B) joint ventures. Strategic agreements are contractual and have different content, the production contract in particular is very important in the context of offshoring projects. *Joint ventures*, however, are distinguished from other agreements, as they imply the creation by new contractors of a new company, with the aim of achieving common goals (Caroli, 2012).

Foreign Direct Investment can be Greenfield or Brownfield. The choice of the Greenfield type allows the company to move to a foreign market using the most appropriate localization, giving rise to a new activity and hence the structural and organizational characteristics established directly by the home-mother (Comacchio, 2013). This model may, however, entail two types of weaknesses: the *liability of newness* due to being at an early stage and therefore not having developed trust relationships, and the *liability of foreignness* associated with the lack of specific knowledge on the new market and in general on the institutional and cultural scene. To overcome these obstacles, we can assess the adoption of *Brownfield* mode, i.e. the acquisition of pre-existing activities.

Making the right location choice is the key element of *offshoring* strategies (Manning, 2009). The most important *drivers* for American and Western European companies are saving on labor costs and access to qualified personnel. Localization

decisions therefore reflect the aforementioned *drivers* (Lewin and Couto, 2007) considered in order to assess where it is most convenient to carry out an offshoring project. Attractiveness factors have to be weighted in the light of the importance that each one takes in the business strategy, aimed at enhancing competitive advantage. Consequently, the viewpoint from which companies consider the opportunity to relocate is consequently changed: this in fact appears primarily as a set of conditions affecting competitive opportunities and not just as a set of factors objectively considered. The factors considered within these decisions are grouped into eight different sets. The level of wages, the educational level of the workforce, the state of infrastructure development and cultural differences are only some of the specific factors within the sets (Caroli, 2012).

Depending on the type of relocation, these factors will have a different significance. To undertake a manufacturing offshoring project, it will be important to choose a destination that for example ensures a lower labor cost, a good transport network and physical infrastructure and availability of raw materials. In many developing countries, investment in infrastructure to improve transport and attract more FDI is growing at a very high rate. It is enough to think that the total expenditure for these projects went to China from \$ 9.2 billion in 2000-2004 to \$ 26.4 billion in 2005-2009, while Indian spending rose from \$ 2.9 billion to \$ 29.4 billion, considering the same time (Rothenberg, 2011). For the offshoring of services, there will be elements such as the degree of telecommunications development and the high quality of human resources, attracting management attention.

1.4 The Offshoring phenomenon

Over the last few decades, there has been a radical change in the organization of industrial activities: from a single large company that manages the numerous activities of the *supply chain* to the creation of a network of many companies, in relation between them, to achieve and to bring the final product in the market. The company's production structure has so far changed significantly, only the fundamental parts of value creation have remained inside, while others have been outsourced in order to benefit from the

specialization process and the quality enhancement. *Global factory* (Buckley, 2004), *international supply chain* (Casson, 2013) or *global value chain* (Gereffi and Korzeniewicz, 1994) are some of the terms used to define the international configurations of productive activities (Frattocchi *et al.* 2014).

The coordination between the various components of the *supply network* has not proved so easy, especially if they are geographically dispersed (De Falco, 2012). In this regard, *outsourcing* and *offshoring* are the terms used respectively to define the outsourcing and delocalization choices of part of the production process activities; first of all, it is necessary to define the exact meaning of the two terms in order to give greater clarity and avoid misunderstanding. Subsequently, we intend to deepen the offshoring phenomenon as a very important variable within the choices of organizational design and internationalization.

In addition, full understanding of this phenomenon is of crucial importance to later analyze *backshoring* and, consequently, the causes that have led companies to reverse the localization choices previously made.

1.4.1 Outsourcing and Offshoring: definitions and differences

With the goal of seeking greater efficiency and exploiting the possible economies of scale, offshoring and outsourcing activities have witnessed a considerable increase over the last few decades. In fact, driven by factors such as lower labor costs and proximity to emerging markets, companies have begun to look beyond national borders to developing countries.

UNCTAD highlights different aspects of outsourcing and offshoring terms.

Outsourcing can be defined as that «particular outsourcing mode that has the purpose of enucleating entire areas of strategic, non-business activity, and which is based on a collaboration between the company that outsources and a company already present in the market as a specialist»(Arcari, 1996). It therefore provides for the reliance on certain functions or services beyond corporate boundaries, which is a real choice of "make or buy" where the firm chooses to outsource certain activities, usually those that do not fall into the *core business*. This decision allows the company to concentrate on

more value-added activities, thus its distinctive competencies, while at the same time allowing greater efficiency through the cost containment obtained by specialization and consequent economies of scale. Boin *et al.* (1998) define outsourcing as «the process by which firms permanently assign to external suppliers (possibly with the transfer of the entire business sector) for a contractually defined period, the operational management of one or more functions previously done inside».

It is clear how outsourcing differs from other forms of outsourcing as it involves a relationship between a highly structured supplier customer: the relationships between the outsourcing company and the company to which the asset is sold (*Outsourcer*) are based on both market and collaborative relationships, as the key prerequisite is the stipulation of a contract that involves a strategic involvement of the supplier in the medium-long term business development programs of the customer (ISFOL, 2011). The basic principle behind the concept of outsourcing is quite simple and intuitive: "*to make others what they do better than us*" in order to reduce costs, improve the qualitative level of the necessary intermediary services or products and thus have the necessary resources for the development of what constitutes the true business of the enterprise (ISFOL, 2011). In addition, based on *transaction cost theory*, outsourcing is convenient when the benefits of outsourcing production are higher than transaction costs resulting from the relationship with suppliers.

Instead regard *offshoring*, the company moves part of its business functions beyond national boundaries, both it establishes partnerships with foreign suppliers, or directly runs it through its own branch (Sako, 2006).

Often, the two terms are mistakenly used as synonyms, but in fact the two concepts refer to different organizational and strategic choices. In fact, contrary to outsourcing consisting of a "*make or buy*" decision, offshoring refers to a geographical boundary, so it consists of choosing where to locate the asset, regardless of its ownership.

In particular, outsourcing and offshoring employ two dimensions, namely the property and location through which Sako (2006) identifies four categories, respectively:

- *Captive offshoring*: activity is relocated to a foreign country, however it is remains under the legal and management control of the mother-house;

- *Offshore outsourcing*: the liability of a particular business is transferred to an independent business entity that carries it out in a foreign country;
- *Domestic outsourcing*: the company outsources certain functions, relying on companies national;
- *Keep in-house*: the enterprise internally performs the activity by referring resources own.

1.4.2 Offshoring and geographical distance: near-shoring and overseas offshoring

In order to be able to give a more accurate definition of the meaning of offshoring, it is important to distinguish two other concepts: *near-shoring* and *overseas*, in relation to the country of reference. These two delocalizing models, though both of the broader and most generic category of offshoring operations, relate to two different modes, which have the geographical distance discriminating factor.

Near-shoring means the relocation or outsourcing of a particular activity, beyond national boundaries, but in a relatively close country. This solution provides many benefits, such as enhanced co-ordination between home and foreign branches, better control over delocalized activity, optimized communication, and reduced shipping times due to the lesser logistical efforts required.

Instead, the *overseas delocalisation* model refers to the delocalisation or outsourcing of certain operations in countries located in more distant areas in order to gain access to particularly important competencies or markets or to seek more cost-efficiency benefits. This solution makes coordination and control operations more difficult by the home-mother, but can allow better access to certain outlet markets. It is important to emphasize that the two solutions are not necessarily alternatives, but rather empirical evidence emerges as they are often complementary. This depends first on the goals it intends to pursue the headquarters, and the type of activity that is to be relocated.

Near-shoring and *overseas* projects take on different facets depending on the countries they undertake. For example, when talking about near-shoring strategies undertaken by USA companies, the geographical area to which we are referring to is very

clear, we are talking about initiatives initiated mainly in Mexico and Canada, member countries with the USA in the area of free trade named NAFTA.

Considering *overseas* projects, it refers to non-American countries, especially European and Asian countries. As far as Italy is concerned, however, the distinction is not so clear, and besides the different geographical position, one of the main reasons may be that, compared to the United States, our country's businesses have started much more offshoring projects recently, and therefore do not have such a defined background as American ones. According to the comments made, we can talk about near-shoring strategies by Italian companies when some activities are relocated to Europe, especially in the Balkan countries and Romania, Turkey and Maghreb countries facing the Mediterranean, such as the Tunisia. When it comes to overseas projects, we refer mainly to the Middle East, Asian and American countries (Mariotti and Multinelli, 2010).

1.4.3 Development and evolution of the offshoring phenomenon

The transfer of productive activities to developing or new industrialized countries has already been present for decades in the business reorganization processes of Western companies. The changes that have affected the last decade relate to the total shift in production capacity in low-cost countries, redefining the value chain of entire industrial sectors (Baronchelli, 2008). Looking for lower exercise costs is not new. The phenomenon has manifested itself in two distinct waves. The first wave took place in the early 1990s under the re-engineering and then in the early 2000s, in a similar trend to reforming business processes with the aim of reducing costs. Today we are still in the second wave. The cost reduction has particularly affected the services sector (Robinson and Kalakota, 2004) as organizations seek to reduce costs by transferring call centers and IT functions, for example, to India (Robinson and Kalakota, 2004; Sathyanarayan, 2003; Smith *et al.*, 1996). The competitive advantage that multinationals derive from outsourcing most of their activities is the ability to manage the contributions of different stakeholders in the value chain while maintaining a leadership position in the coalition itself (Tracogna and Nanut, 2003).

Offshoring refers to the process of outsourcing and coordinating certain functions beyond national boundaries. With this term, we refer broadly, both to *captive offshoring* and to activities outsourced to specialized suppliers located in a given country¹² (Lewin, Massini e Peeters, 2008). The discriminating element is thus spatial localization (Dunning, 1998). Piscitello *et al.* (2013)'s results confirm that offshore incentives motivated by cost reduction and mainly located in developing countries lead to better operational performance if implemented through *offshoring outsourcing* strategies.

Otherwise, strategic choices driven by the desire to seek local synergies and skills in centers of excellence, achieve greater performance if implemented through captive models.

Delocalisation can be done either with the intention of trying to look more closely at a foreign market or to look for more favorable conditions in order to be more competitive in the country of origin. Offshoring occurs if some of the company's production, marketing and supply activities cross national borders and take place in a foreign country (Segnana and Bernard, 2010). However, it is to be noted that approximately 70% of offshoring transactions are based on relocation of activities at a captive center or a so-called *wholly owned subsidiary* located in a country where the labor cost of the country of origin is lower.

Companies such as Lufthansa and Philips have adopted this model by locating certain activities, such as accounting and IT, at some centers in Poland (Boston Consulting Group, 2005). This example is very important, as it denotes that the phenomenon of offshoring has undergone remarkable evolution over the years. Historically, in fact, the term was used implicitly referring to activities directly related to production, while recently, the new wave of offshoring involves important technical and administrative services (Caniato *et al.*, 2013).

The first offshoring phenomenon can be traced back to 1911, when the USA company Ford Motor relocated Ford T's assembly work to Trafford Park, England, in order to reduce its cost of transport and serve it in the best way the European market (Stringfellow, 2008). The delocalisation phenomenon undergoes a significant increase

¹²Starting from the following paragraph, the offshoring term will be used with reference to both meanings: offshore outsourcing and captive offshoring.

after the Second World War, since in the 1960s there has been a growing delocalisation activity carried out by large American companies (Gereffi, 2006). In the first phase, the motivations for companies to undertake offshoring strategies are the reduction in production costs, the attempt to secure access to new markets thanks to their direct presence on the territory and the opportunity to leverage favorable government policies (Lewin And Peeters, 2006).

The second phase, starting from the second half of the 1990s, from this period forward, offshoring is no longer related to production-related activities but begins to affect services (Metters and Verma, 2008). Through control mechanisms, such as standardization, firms also relocate service activities, even if they are intangible. It should be stressed how this has been made possible thanks to the role played by new communication technologies (Contractor *et al.*, 2011).

In the third and final phase, which is still in operation today, offshoring is expanding including high-value added services: engineering, IT and R&D. Offshoring affects not only repetitive or low value added activities, but is also done for core assets that require specific skills. The increasing relocation of these functions has been a consequence of the strong changes that have characterized the global economic environment, which led to a very sharp reduction in the so-called *time-to-market* and consequently the companies in order to be competitive, had to respond to the need to enter into market products faster in time (Clark, 1991). New factors, such as the need to find new ideas and human capital outside the corporate boundaries, then interfere in offshoring strategies (Contractor *et al.*, 2011).

During the three phases of the development of offshoring strategies, the ever-increasing evolution of IT has played a decisive role. In fact, they have enabled an ever faster and more cost-effective *intra-enterprise* and *inter-enterprise* communication, information exchange, representing the entire *supply chain* (Evans and Wurster, 1999). The separation of physical components, thanks to the development of communication and information technology, allowed companies to rethink and reconfigure their value chains, in order to maximize the added value added (Youngdahl *et al.*, 2008). Offshoring, above all in the early stages, had as its main objective the pursuit of countries where to do their

activities at a lower cost (Sharma *et al.*, 2009) by pushing many companies in Western world to move its activities to developing countries such as China and India.

Initially, therefore, the phenomenon of offshoring seemed like a huge migration of jobs from developed countries to developing countries. Over the years, however, there has been a great evolution of the world scenario and it quickly became apparent that offshoring was a much more complex phenomenon than it appears (Bardhan and Kroll, 2013).

1.4.4 Offshoring Drivers

Offshoring is a strategy initially adopted by businesses to reduce operating costs (Lewin *et al.*, 2006): goods and services should be produced in countries where it is less costly to realize them. Following Dunning's approach, offshoring is adopted in order to pursue an *efficiency/low cost seeking strategy*. As noted in the previous paragraph, however, offshoring has undergone a process of evolution over the years that has dramatically changed its strategic goals, as a result, drivers and motivations have prompted companies to adopt a relocation strategy. Recent studies show that 66% of offshoring agreements are geared to supporting business growth strategies involving R&D and product design and innovation.

Cost reduction continues to be undoubtedly the main factor motivating delocalisation decisions. However, a new trend is emerging, and more and more offshoring strategies are driven by factors such as the search for new growth opportunities, competitive pressure, and better access to highly qualified personnel (Lewin and Peeters, 2006).

It is important at this stage to define the operational performance that may be affected by the location decision. In literature, academics have achieved a general consensus on the taxonomy of such performances, which can be distributed as follows (Belvedere 2015, Grando et al 2007, Neely 2005, Neely et al 1995, Leong *et al.* 1990):

- cost, considered as the ability to achieve a satisfactory productivity of productive resources;
- quality, mainly intended as compliance with the specifications;

- time, related to the ability to produce and deliver quickly in terms of reliability;
- flexibility, considered as the ability of a system to react to the need to adapt rapidly and economically efficiently.

To confirm this the recently literature also highlighted the significant effects that these factors may have on the company's environmental and social performance, now accepted as the fifth dimension of the performance of such processes (Belvedere and Grando 2017, Gauthier 2005, Elkington 1997).

In fact, existing contributions have shown that most return decisions are made of production activities aim to overcome the problems caused by previous offshoring projects carried out (Stentoft *et al.*, 2016).

The decisive factor for de-localization decisions, according to the ORN (Offshoring Research Network, 2007), is more closely linked to the search for greater efficiency; 91% of the surveyed companies stated that amongst the reasons for doing offshoring there was the minimization of work-related costs. The 72% of companies, however, implemented an offshoring project to minimize other costs; usually the countries where you choose to relocate, have more favorable tax conditions. Over the years, worldwide, they have developed and consolidated the knowledge districts that Porter (1990) describes as «*a geographically close group of interconnected companies and associated institutions in a particular field, linked by common and complementary elements*». The third driver, with 67%, is in fact access to highly qualified personnel. The new technology clusters in Bangalore, Bombay, Delhi and Hyderabad in India (software), Dublin in Ireland (IT), Tel Aviv in Israel (software and It) and Taiwan (microelectronics) are just a few examples of centers where there is access to highly competent human resources (Torrise, 2002). The most important factors for American and West European companies are therefore cost savings, particularly labor costs, and access to qualified personnel (Manning *et al.*, 2009). Consequently, localization choices reflect the motivations that led companies to adopt offshoring projects (Lewin and Couto, 2007). Advantages on labor costs and access to qualified resources are very important criteria for choosing the location, thanks to the possession of these requirements, countries such as India and China have been very successful in attracting foreign direct investment. The different drivers that are the basis of offshoring choices contribute to having different

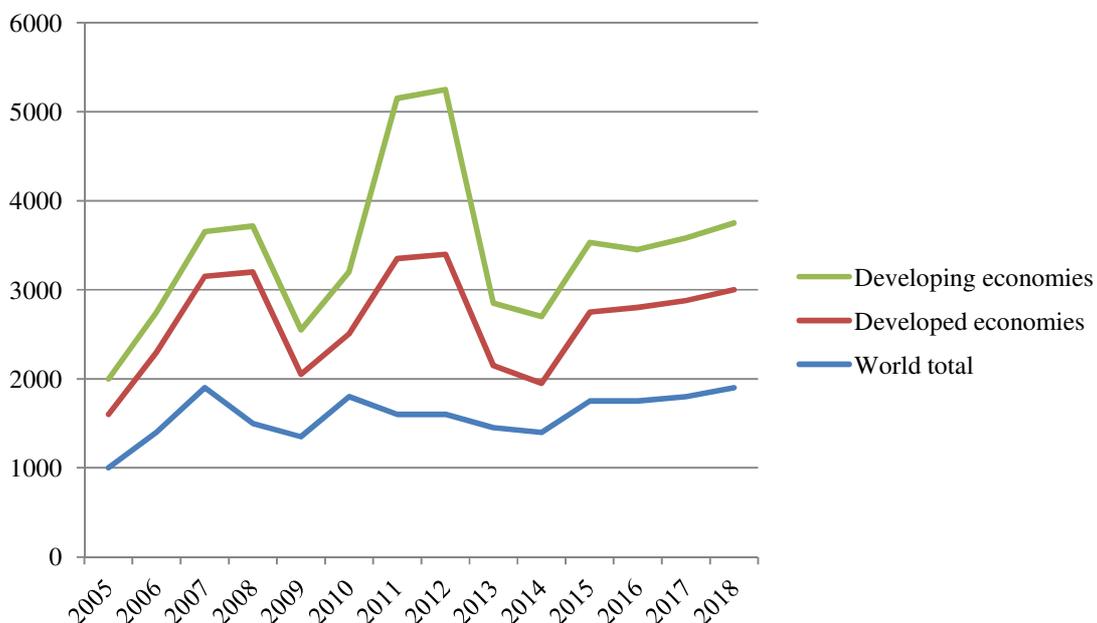
consequences on business performance. More specifically, cost-benefit drivers will have impact on operational performance: productivity, efficiency and quality. While knowledge and skills research will have a stronger impact on strategic performance: innovation, growth and competitiveness (Manning *et al.*, 2009).

1.4.5 The size of the Offshoring

In order to measure the intensity of the delocalisation phenomenon, it is possible to use in particular the data on foreign direct investments. The FDI are a very important quantitative measure to understand the intensity of the offshoring phenomenon.

In 2007, FDI flows reached a record of \$ 1,800 billion. Following the great economic crisis, FDI have undergone considerable fluctuations between developed economies (Figure 1), and in 2014 they dropped to \$ 1200 billion due to both the lack of adequate investor guarantees and both the fragility of the world economy too vulnerable to geopolitical risk (UNCTAD, 2017).

Figure 1: FDI inflows 2005-2016, and projections, 2017-2018 (Billions of dollars)



Source: Own data re-elaboration, UNCTAD (2017).

In 2015, global FDI flows recorded another evidence \$ 1750 billion, owing particularly to USA growth prospects, lower oil prices, accommodating monetary policies, and continued liberalization and investment promotion. Given the slight decrease in 2016, a particular positive influence of macroeconomic policies on FDI is expected for 2017 and 2018. A modest restoration of global FDI flows for 2017 is expected due to a cyclical increase in production and trade, faster growth in developed countries, while a likely increase in commodity prices should support the recovery of developing economies, although fluxes remain below their peak in 2007. Consequently, global FDI flows should increase by about 5% in 2017 to nearly \$ 1.8 trillion. However, high geopolitical risks and political uncertainty for investors could have an impact on FDI recovery in 2017.

It is interesting to note that emerging countries, following the 2009 shocks, have instead steadily recovered the FDI share, which reached the record \$ 700 billion of FDI entering in 2014, thus consolidating their position of World-wide beneficiaries in 2015 and forecasts in 2017 (Figure 2).

Figure 2: FDI inflows by group of economies and region, 2014–2016, and projections, 2017 (Billions of dollars and per cent)

<i>Group of economies/region</i>	<i>2014</i>	<i>2015</i>	<i>2016</i>	<i>Projections</i>
				<i>2017</i>
World	1.324	1.774	1.746	1.670 to 1.870
Developed economies	563	984	1.032	940 to 1.050
Europe	272	566	533	560
North America	231	390	425	360
Developing economies	704	752	646	660 to 740
Africa	71	61	59	65
Asia	460	524	443	515
Latin America and Carribean	170	165	142	130
Transition Economies	57	38	68	75 to 85

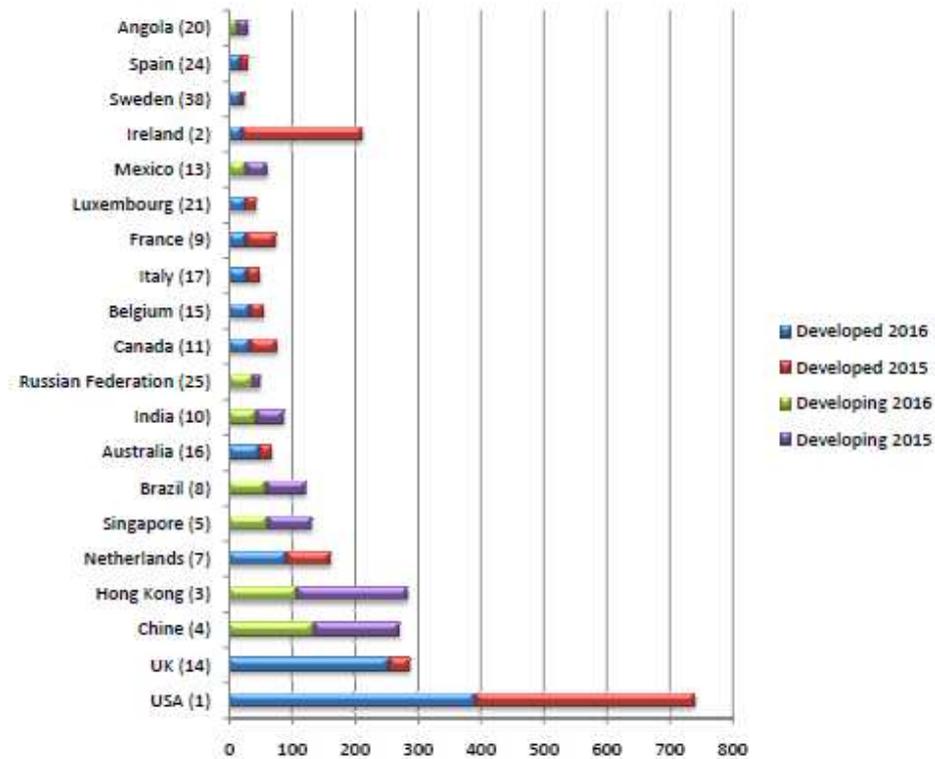
Memorandum: annual growth rate (per cent)

<i>World</i>	-8	34	-2	-4 to 7
Developed economies	-18	75	5	-9 to 2
Europe	-20	108	-6	-5
North America	-15	69	9	-15
Developing economies	4	7	-14	2 to 15
Africa	-4	-14	-3	-10
Asia	9	14	-15	-15
Latin America and Carribean	-3	-3	-14	-10
Transition Economies	-33	-34	81	10 to 25

Source: Own data re-elaboration, UNCTAD (2017).

It is possible to observe (Figure 3), as the top 10 global destination FDI flows reflect offshoring drivers.

Figure 3: FDI inflows, top 20 host economies, 2015 and 2016 (Billions of dollars)

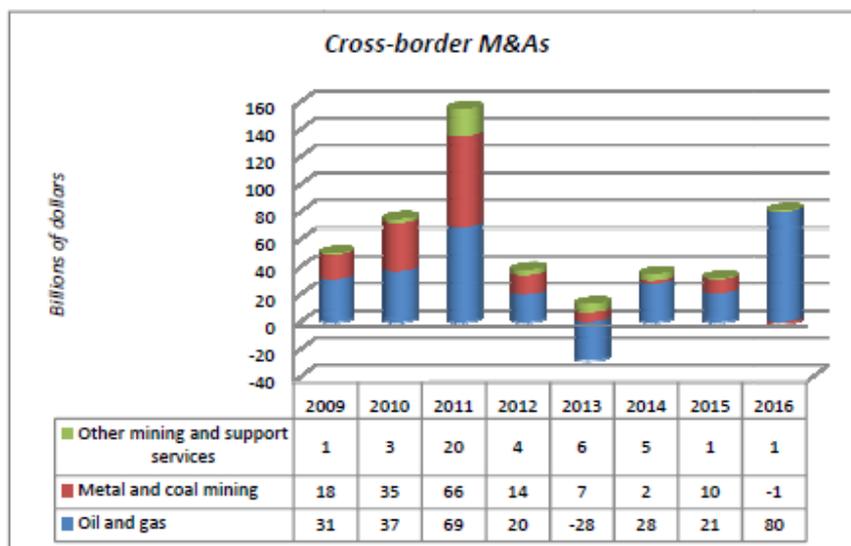


Source: Own data re-elaboration, UNCTAD (2017).

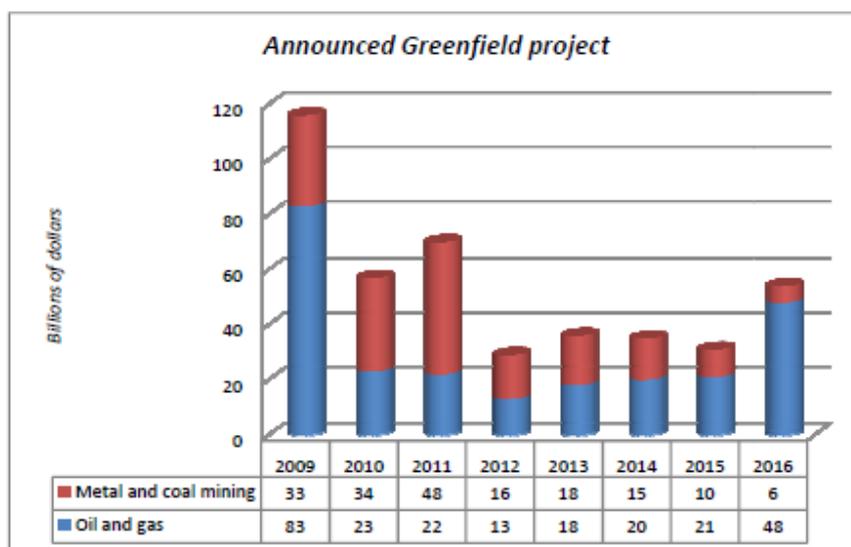
For example, China offers cheap labor, while the United States offers access to highly qualified staff, both countries are able to pursue business growth strategies and access to very important markets. Particular attention is paid to the small city of Singapore, which thanks to the policies aimed at favouring FDI, has become a major player in the global competitive scenario. It is the fourth largest financial centre in the world, with good connections to the entire Asian continent and thanks to the development of advanced technologies is an ideal location for R&D centres.

Figure 4: Cross-border M&As and announced Greenfield projects in extractive industries, value and share in all industries, 2009–2016 (Billions of dollars and number of projects)

a. Cross-border M&As



b. Announced Greenfield project



Source: Own data re-elaboration, UNCTAD (2017).

Low input prices have significantly influenced FDI inflows in recent years, affecting the share of the primary sector in FDI stocks, especially in Africa, Latin America and Western Asia. Mining industries play a leading role in these economies of

developing regions and account for 20-30% of their FDI stock. In 2016, the number of M&A's cross-border mining industries grew by 5% compared to the previous year thanks to an increase in oil and gas (Figure 4)¹³. The wave of acquisitions involved both the manufacturing and service sectors. All sectors have been involved in *brownfield* activities, and in particular the chemical/pharmaceutical and telecommunications sectors have received considerable attention.

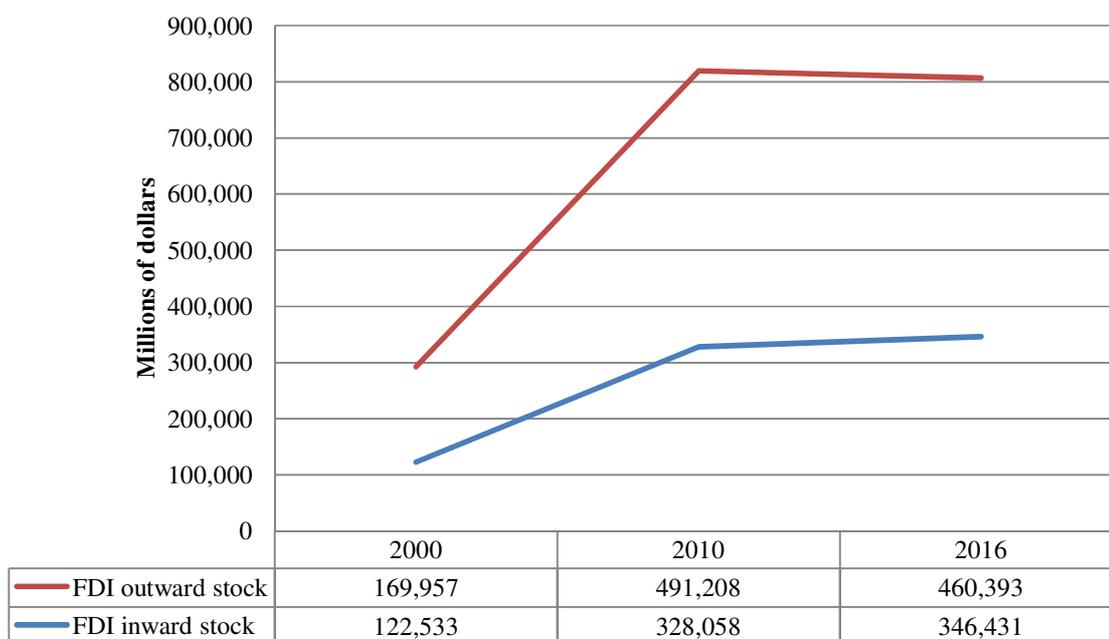
The amount of announced *greenfield* investments has also increased significantly. This type of investment has increased by 3%, with operations concentrated in the extractive industries.

1.4.6 The situation in Italy

In the above-described framework, Italy's position did not change significantly from the analysis carried out in previous research reports (Mariotti and Mutinelli 2012; Mariotti *et al.*, 2015). Despite a recovery in FDI outbound and inbound flows from 2013, the degree of internationalization, both active and passive, continues to be significantly lower than that of its major European partners.

¹³Guided by the acquisition of BG Group PLC (UK) by Royal Dutch Shell PLC (Netherlands).

Figure 5: Italy FDI stock 2000, 2010 and 2016 (Millions of dollars)



Source: Own data re-elaboration, UNCTAD (2017).

With regard to active internationalization, by the end of 2015, the FDI outbound stock was \$ 328.058 billion; the ratio between the FDI outbound and gross domestic product (GDP) was equal to Italy at 25,7%, below half of the EU-27 average (57.6%) and across Europe (61.6%), as well as those of France, Germany and the UK (54%) and broadly lower than that of Spain (39.4%). In 2016, however, the FDI outbound stock recorded an increase of about 18,400 billion dollars.

Also on the side of investments from abroad, Italy's position appears modest and reflects the persistent low international attractiveness of the country. The ratio of inbound FDI stock to GDP (18.5% in 2015) remains significantly lower than the world average (33.6%), Europe (50.7%) and the EU (47.9%) As well as that of European competitors

(51.1% in the United Kingdom, 44.5% in Spain, 33.4% in France and 31.9% in France) as it amounts to 491.208 billion dollars, down to 460.393 in 2016.

Look at how gaps with other European countries remain high, even though Italy has "benefited" a significant contraction in GDP, which is the denominator of the indicator considered.

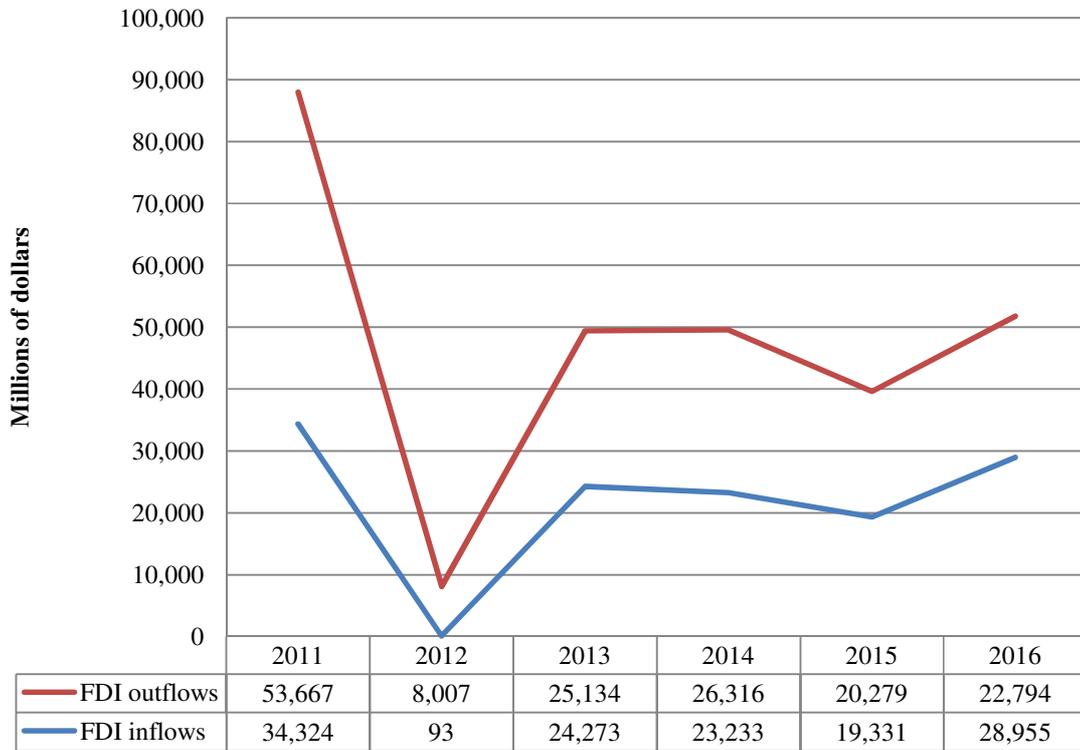
By analyzing the FDI outflow from Italy (Figura 6), the average FDI flows out of Italy in 2009-2015 were less than \$ 28 billion a year, against over 61 billion in the period 2005-2008, with a contraction in average flows higher than those of the European and EU average (-54.8% vs. -48.4% and -51%). The share of Italy has thus dropped from an average of 4.1% of the world total in the pre-crisis period to 2% of the most recent period.

In 2012 it is noted that the relative flows have dropped to only \$ 8 billion, the lowest since 2004, to rise in the following years to around \$ 25-28 billion, accounting for less than 2% of the World-wide, reaching about \$ 23 billion by the end of 2016.

The considerable gap between the other large European countries can not be justified in the arguments that internationalization of our industrial system goes hand in hand, mainly based on "lighter" forms such as production and commercial agreements and other forms of relocation that are not materialize in FDI. These theses do not seem to consider that companies in other countries also resort to such solutions, which are not infrequently complementary, rather than substitute for FDI (Barba- Navaretti *et al.*, 2011). Whilst it is possible to accept - despite the absence of comparatively statistically funded comparisons between the various countries - some of Italy's strong tendency towards these forms, especially because of the greater presence of SMEs, it can not be assumed that it has such effects as to fill or even significantly reduce the size of the above-mentioned entity (ICE, 2016).

Also on the side of incoming FDI streams, Italy is recovering from 2013, after the previous year the flows were basically zeroed (\$ 92.5 million) to reach \$ 19 billion in 2015. In 2016 there was a slight increase (\$ 29 billion).

Figure 6: Italy FDI flows, 2011–2016 (Millions of dollars)



Source: own data re-elaboration, UNCTAD (2017)

The outline route is a substantial confirmation of the FDI Markets data that globally identify Greenfield and extension projects announced by the press, although some improvement is noted on the foreign investment side compared to the recent past. Figure 7 shows the number of cross-border projects launched by the European countries and the EU-28 countries as a whole, as well as the main competitors of this area taken individually.

Figure 7: Number of Greenfield and foreign direct investment projects

		2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Number of projects	World	10.800	12.822	12.951	27.179	14.755	15.425	16.783	15.107	16.523	15.022	14.381
	Europe	5.087	6.210	6.762	8.508	7.508	7.579	7.985	7.171	8.233	7.109	6.876
	European Union (UE28)	4.742	5.742	6.271	7.783	6.903	6.909	7.283	6.559	7.514	6.449	6.236
	France	653	731	942	1.099	1.013	873	888	788	992	875	909
	Germany	1.053	1.309	1.341	1.546	1.403	1.450	1.541	1.452	1.496	1.307	1.244
	Italy	333	310	365	525	460	408	374	373	514	458	445
	United Kingdom	860	1.096	1.094	1.431	1.379	1.446	1.650	1.493	1.685	1.289	1.278
	Spain	218	281	516	654	652	638	647	560	670	518	464
Incidences %	Europe	47,1	48,4	52,2	49,5	50,9	49,1	47,6	47,5	49,8	47,3	47,8
	European Union (UE28)	43,9	44,8	48,4	45,3	46,8	44,8	43,4	43,4	45,5	42,9	43,4
	France	6,0	5,7	7,3	6,4	6,9	5,7	5,3	5,2	6,0	5,8	6,3
	Germany	9,8	10,2	10,4	9,0	9,5	9,4	9,2	9,6	9,1	8,7	8,7
	Italy	3,1	2,4	2,8	3,1	3,1	2,6	2,2	2,5	3,1	3,0	3,1
	United Kingdom	8,0	8,5	8,4	8,3	9,3	9,4	9,8	9,9	10,2	8,6	8,9
	Spain	2,0	2,2	4,0	3,8	4,4	4,1	3,9	3,7	4,1	3,4	3,2

Source: own data re-elaboration ICE, 2016

By comparing Italy data with those of other major European countries over the period between 2005 and 2015 the cross-border investment initiatives of Italian companies amounted to 27% less than in Spain, which is less than half of France's and less than a third of Germany and the United Kingdom. The gap with the main European competitors does not seem to be shrinking in time, despite the average number of initiatives being increased by less than 400 per year in the period of 2005-2012 to 472 per year in the 2013-2015 period, thanks in particular to the 514 initiatives of 2013 (below 525 initiatives registered in 2008). In the last three years, however, Italy's share of the total world has returned to pre-crisis levels, reaching 3.1%, compared with 2.4% in the previous three years (2010-2012).

In summary, the growth model of Italian firms abroad has not been undergoing significant variations in recent years and maintains a close consistency with the typical features of Made in Italy and the fragmented industrial structure of the country: an intense effort to strengthen the commercial presence especially in rich countries, able to appreciate design quality and product innovation, and to express elastic income demand profiles accompanied with relocation processes mostly towards "close" areas in the geopolitical, cultural and logistical sense.

In the background, however, a lower rate of initiative and often a smaller investment size, particularly in manufacturing activities: these factors are reflected in the persistence of a global gap, especially in reference to the Pacific area, a new epicentre Of the world economy. The situation certainly appears to be worse in the face of the country's attractiveness, especially if it considers that Greenfield investments and the expansion of pre-existing activities are part of the most "expansive" FDI for the national economic base. In this regard, Figure 8 proposes a comparison between Italy and its major European competitors with reference to the period 2005-2015.

Figure 8: Number of Greenfield and direct foreign investment projects to Europe by country of destination, 2005-2015

		2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Number of projects	World	10.800	12.822	12.951	27.179	14.755	15.425	16.783	15.107	16.523	15.022	14.381
	Europe	4.211	5.106	5.178	6.104	4.898	5.141	5.258	4.806	5.248	4.940	4.887
	European Union (UE28)	4.108	4.969	4.975	5.859	4.718	4.973	5.083	4.628	5.082	4.793	4.774
	France	506	599	602	716	429	389	349	394	572	480	457
	Germany	289	379	467	737	713	784	878	868	878	898	712
	Italy	142	162	202	253	179	206	150	127	138	152	135
	United Kingdom	665	729	732	964	1.119	956	1.050	971	1.085	1.107	1.192
	Spain	180	320	469	594	408	421	376	404	402	393	386
Incidences %	Europe	39,0	39,8	40,0	35,5	33,2	33,3	31,3	31,8	31,8	32,9	34,0
	European Union (UE28)	38,0	38,8	38,4	34,1	32,0	32,2	30,3	30,6	30,8	31,9	33,2
	France	4,7	4,7	4,6	4,2	2,9	2,5	2,1	2,6	3,5	3,2	3,2
	Germany	2,7	3,0	3,6	4,3	4,8	5,1	5,2	5,7	5,3	6,0	5,0
	Italy	1,3	1,3	1,6	1,5	1,2	1,3	0,9	0,8	0,8	1,0	0,9
	United Kingdom	6,2	5,7	5,7	5,6	7,6	6,2	6,3	6,4	6,6	7,4	8,3
	Spain	1,7	2,5	3,6	3,5	2,8	2,7	2,2	2,7	2,4	2,6	2,7

Source: own data re-elaboration (ICE, 2016)

The performance of Italy, which was already weak, was further deteriorated in the post-crisis period when the negative economic situation overlapped the other well-known and still largely unresolved factors that limit not only the attractiveness of the country towards the FDI, but also its competitiveness and endogenous growth potential.

Throughout the period, our country has attracted fewer than half of Spain's initiatives, equal to one-third of France, less than a quarter of Germany and one-fifth of those in the UK. In 2011-2015, in particular, Italy attracted only 702 investment projects, or 140 projects on average per year (135 in 2015), with a number of initiatives almost halved compared to 253 in 2008. The gaps The largest Western European countries have

become so abysmal: in the last five years they are better off than in the United Kingdom (5,405 projects), Germany (4,234), France (2,252) and Spain (1,961), but also economies of Smaller size, such as Ireland (990 projects), the Netherlands (939) and Belgium (751). Between 2011 and 2015, investment projects attracted by Italy accounted for only 0.9% of the world's total, against 1.4% of the 2005-2010 period (although this is also very modest if account is taken of of the country's economic and demographic size).

The picture is further worsened by considering the qualitative aspects of the attractiveness differentials of the various sectors and the different investor countries, discussed in the past (Mariotti and Mutinelli, 2012). Italy is experiencing strong difficulties in attracting investments in advanced services (in particular software, ICT and professional services), which are the most dynamic and relevant sectors in terms of the number and consistency of projects in industrial countries. Among the "strong" sectors in Western Europe, some of Italy's specialization is only found in the energy sector, thanks to a large number of projects - but mostly modest - in renewable and alternative energies, and in the health care sector And social services, where some investments are made in nursing homes and elderly care. Among the other sectors, the only ones in which Italy has a clear attraction, although in decline in the post-crisis period, are the tourism and the show, confirming the opportunities that the country can offer, enhancing its artistic heritage, Cultural and landscaping: in the period considered, these sectors account for less than 5% of the total number of initiatives, given their niche character on an international scale.

By focusing on the geographic origin of cross-border investment projects in Italy, greater attention is being paid by the countries of the Old Continent, particularly Spain, mainly due to investments in the energy sector, Retail, hotel and real estate. Italy, on the other hand, receives proportionally less than both Western Europe and the rest of the world, from all other economic areas except Africa.

1.5 The global supply chain in the international strategy

Stiglitz (2003) described globalization as «a closer integration of the countries and peoples of the world that was determined by the huge reducing transportation and

communication costs and reducing barriers artificial streams of goods, services, capital, knowledge and people through the boundaries».

Globalization requires that businesses have more links tight with their supply chains that are geographically dispersed. Respect to the issue of global competition, Heizer and Render (2008) explained that «competition is no longer between companies but between supply chains». There is no more complex and relevant subject for survival and success of a company than it is today, in global market times, management of the supply chain, with enormous commitments to the many critical points to monitor consistently: internal organization, relationships with partners, suppliers and consumers, IT systems, market relations and more. The supply chain is an important component of the strategy of an enterprise and it can influence its ability to reduce costs and increase profit margins (Heizer and Render, 2008).

According the controversy of New (1995) and Saunders (1995) in the supply chain management literature there is a confusion of profusion of overlapping terms and meanings. As a result, many supply chain labelling and supply chain management practices can be found in the literature, including: integrated purchasing strategy (Burt, 1984), supplier integration (Dyer *et al.*, 1998) (Lee and Billington, 1992), the network supply chain (Nassimbeni, 1998), the value added chain, the lean chain approach (New and Ramsay, 1995), the pipeline management (Farmer and van Amstel, 1990), the supply network (Nishiguchi, 1994) and the flow of value (Jones, 1995). The lack of a universal definition of supply chain management depends in part on the way in which the supply chain concept has been developed.

Over the last two decades, profound changes in the international division of labor between enterprises have led to increasingly globalized intermediary markets. Outsourcing and deactivation of production phases are key elements of this evolution. The production of almost all goods (from computers to retail services) is now made up of a series of separate tasks, probably located outside the "final" assembly company, both at home and abroad. The growth of outsourcing and offshoring is so pervasive that it partially replaces international trade in commodities with the business of trade (Grossman and Rossi-Hansberg, 2006). Global value chains form the core of this new international division of labor. The usual model sees companies from advanced countries taking the

role of lead companies in global value chains "producer" or "buyers" (Gereffi, 1994). Global value-driven chains of buyers, which have received much attention from GVC scholars.

A key topic of the GVC is that the involvement of suppliers in the global value chain is a valuable opportunity for the growth of these players, as external links can provide managerial skills, technical knowledge, innovation channels and new markets, and above all, can boost the company's upgrading in the value chain. GVC scholars provide at least four channels of improvement: a) Product innovation, ie the ability of suppliers to satisfy the mandate for higher added value, more sophisticated products (Dolan and Humphrey, 2000, Bair and Gereffi, 2001, Bazan and Navas-Aleman, 2004; Giuliani *et al.*, 2005) or enlargement of the product portfolio; b) process innovation, ie to increase the technical efficiency of the production process; c) functional upgrade, ie improving the quality of the supplier's function along the chain, or driven by global buyers and involved in industrial sectors such as textiles and shoes. Retailers mainly control downstream activities such as distribution, marketing, and sales, while production is outsourced to vendor networks (Gereffi *et al.*, 2001). Conversely, guided product-driven chains, mainly driven by big producers, are typical of capital-intensive industries such as automotive, electronics and civil aviation. In this latter type of value chain, end companies continue to control the production process by purchasing intermediate intermediates customized from selected suppliers located in both home and abroad. Gereffi *et al.* (2005) also associated the types of governance of the value chain, described above, with combinations of three peculiar dimensions: the complexity of business transactions, the ability to encode complex transaction specifications and supplier related capabilities to the needs of the transactions. Low-capacity suppliers participate in prisoners, primary by Gereffi *et al.* (2005) and subsequently refined empirical results from on-the-field work in various industries in developing countries (Gereffi, 1999, Schmitz, 1999, Bair and Gereffi, 2001, Dolan and Humphrey, 2000, Galvin and Morkel, 2001; Sturgeon, 2002; Humphrey, 2003; Sturgeon and Florida, 2004; Pietrobelli and Rabellotti, 2007). In modular value chains, leading companies provide design specifications to the vendor companies that produce components, modules and / or subsystems (Sturgeon and Lester, 2004; Gereffi *et al.*, 2005). Relational value chains, on

the other hand, are characterized by close relationships between suppliers and leading companies, as suppliers are involved in strategic manufacturing phases, such as product design and product development. Finally, in captive value chains, several suppliers can provide the same intermediate goods and the competition between them is fierce, mostly based on price.

As demonstrated by this brief review, the GVC provides in-depth information based on empirical evidence provided by several case studies on particular aspects of producer participation in the global value chain that may hinder or favour the role, performance and growth of businesses providers. In addition to the importance of productive, process, functional and inter-sectoral innovation, as the main channels for business upgrade, the link between the different types of government chains and the prospects for improvement of suppliers. As some authors have pointed out (Dunford 2006, Kalarantidis *et al.* 2011), while the value chain where companies operate has been widely explored, the company itself and its organizational choices remain somewhat in the shadows. The reason for this is undoubtedly in the absence of good quality micro data (Sturgeon and Gereffi, 2009), which can also explain why most empirical results of the GVC are based on rich, insightful and detailed case studies, surveys and tests anecdotal rather than statistical surveys. According to GVC, regardless of the type of value chain they belong to, leading companies always have a high level of productivity. But for the providers, the image designed by GCVA is more complex because both their individual potential and the type of value chain (relational, modular or captive) that they nourish are crucial to determining their success, profitability and growth. In our survey, therefore, consistent with GVC insights will take into account: 1) the supplier's ability to innovate as an indicator of supplier's ability and decisive for better performance; 2) Supplier's propensity to export as a supplier determining the productivity of businesses. The latter would seem particularly relevant in the developed sector countries in which businesses operate mainly within global product-driven chains and access foreign markets increase their participation in global organizational structures and their own business relations with the largest assemblers. In addition, the link between business export capabilities and performance is well known in literature as "learning through hypothesis export" (Bernard and Jensen, 1999). According to this, exports increase business productivity

through flow of knowledge companies are exposed by operating on foreign markets. Possible channels for such learning is analyzed for example by Baldwin and Gu (2004) and Lilleeva and Treer (2010). Contributions related to the offshoring phenomenon refer to three main streams of research. First, in international business literature, to the theory of internationalization processes of the company (Bilkey and Tesar, 1977, Cavusgil, 1984, Fletcher, 2001, Johanson E Vahlne, 1977, Johanson and Vahlne, 1990) should evaluate the transfer of production abroad. Second, the literature on strategic management has paid attention to whether or not to make offshoring (e.g. Nayyar and Bantel, 1994; Quinn, 1999). As a third approach, Supply Chain Management's literature focuses on how companies manage relationships with outsourced activities (e.g. Baldwin and Clark, 2000; Quinn, 2005; Sanchez and Mahoney, 2002). In recent years, the relationship between performance and organizational features of enterprises has been welcomed by more attention from industrial economists and management scholars. This increased interest has been triggered by the profound changes in the world economy brought about by globalization. In particular, over the last two decades there has been a noticeable vertical disintegration in most industries and a major reorganization of production across national borders. This has forced companies to look for efficient organization options in a world of increasingly complex, inter-firm relationships, rapidly expanding outsourcing and off shoring, and the development of global networks and value chains. The role of supply strategies and the connection between the organizational choice of the company and its efficiency and productivity have been underlined by influential literature known as "theory of heterogeneity firm" (Melitz, 2003, Antras and Helpman, 2004, Helpman *et al.*, 2004, Helpman, 2006). By following this approach, businesses can be ordered into a great eradication of productivity based on their organizational choices. In fact, allowing differences in the fixed costs of integration and outsourcing at home or abroad (especially in low-cost countries), different forms of organization can coexist.

While more productive enterprises are doing their business in an integrated way in low-cost countries in the form of foreign direct investment, the least productive ones continue to operate in the country of origin and enterprises with intermediate levels of productivity acquire their intermediaries abroad from unrelated suppliers. However, while the analysis of business procurement strategies (i.e. "make-or-buy" and "where-to-do-

buy" choices) have given rise to a vast volume of literature, -written to business behaviour suppliers, the "other side of the coin" of outsourcing and offshoring phenomena. Although the options of being a supplier rather than a builder or a forward-looking company or being a supplier in local and non-international markets are recognized as important and widespread choices for the firm, literature has not yet made clear about the implications of these choices for the company's performance. Initially proposed by Gereffi (1994) and subsequently expanded with important contributions by Gereffi and Korzeniewicz (1994), Gereffi (1999), Kaplinski (2000), Henderson *et al.* (2002) and Humphrey and Schmitz (2002), develops a framework that links the vertical fragility of industries to the globalization of intermediate goods markets and global value chains that are at the core of a new international division of labor. More importantly, this framework also provides sound interpretations of both chain functioning and governance and the role and dynamics of growth of suppliers.

From global contexts it also follows a change in how to understand the performance that the supply chain must be offered according to the company's different orientation. A company marketing oriented, for example, focuses its attention on the consumer and through product differentiation, it tries to manage with the different tastes and preferences of consumers and exploit market opportunities. In these cases is mainly involved in its strategic and marketing function whose supply chain is configured to provide flexibility to reduce the costs of differentiation and rapid response. Different is the situation for market-driven businesses. These involve in their competitive approach all stakeholders and actors of the sector (Hills and Sarin, 2003). The supply chain configuration becomes complex and able to respond not only to imperatives of optimization and efficiency but also to easily rearrange itself to react promptly make changes to the offer and redesign or create existing markets new, or introduce discontinuity in how to create value(Kumar, Scheer and Kotler, 2002). Also, in the awareness that competitiveness it does not depend exclusively on the quality of products and services, but also and above all how the company works and how it is able to define operational models geared towards change, high capacity is required forecasting and monitoring of markets, a significant propensity the adoption of new technologies across the network, organizational skills of network design and / or re-design (Narver, Slater and

MacLachlan, 2004). The new approach to the global supply chain adopted by businesses Market driven is therefore based on the combination of three elements:

1. Market understanding and speed in satisfying it (the winners of the industry will be those who will have the ability to reach customers by understanding them their necessity and change of their needs);

2. agility and ability to adapt to external circumstances while maintaining cost and structure of the best service;

3. Reliability with minimizing waste and reducing time in all phases.

To succeed in international business, businesses need to understand the effects of globalization on its competitive strategies. The effect of globalization forces companies to look at ways through which acquire a competitive advantage and, first, through a vision of world-wide shopping strategically oriented in the context of supply management. Since the mid of 1980s, many researchers have published reflections on transformation from purchases of a tactical nature to supply strategic management. This was probably the most investigated theme in this research area of the last decades is both conceptually and empirically. The high interest in research also indicates the importance of the new concept of supply management for management practices. In addition to reducing costs (Chapman *et al.*, 1997), therefore, the current situation requires companies to rethink their priorities strategic, restructuring of its value chains and acceleration of innovation and improvement processes (Burt *et al.*, 2003). This can be obtained by focusing on so-called core competencies (Prahalad and Hamel 1990) and cooperating closely with suppliers of "non-core" activities (Kannan and Tan, 2003). The purchasing department, which for many years has focused its attention only on order management and on price negotiation, it must do a step forward to become the "manager" of this level integration global (Burt and Doyle, 1994; Das and Narasimhan, 2000). Some researchers have identified supply management as "new a source of competitive advantage (Quinn, 1983, p. 38). Global sourcing is gaining an increasingly prominent role in the strategic arena of a growing number of companies (Samli *et al.*, 1998). It is transformed from an operational and supportive business activity (opportunistic sourcing) in a competitive weapon (strategic sourcing).

1.6 Concluding Notes

Offshoring strategies have and still have great importance. They are a cornerstone of businesses that want to position themselves decisively on the international competitive scenario. In order to seek greater efficiency and new growth opportunities, relocation activities have had a real explosion over the last few decades. The elements that helped to advance such a rapid phenomenon were, for example, the development of ICT technologies and facilitating the movement of people, capital and goods. Firms strongly involved in international markets, which have adopted offshoring strategies, are characterized by their high organizational flexibility, but coordination between geographically dispersed activities has not always been so easy. Offshoring projects are, in most cases, started to pursue cost-cutting logic, primarily towards countries where labor costs are significantly lower.

The *low cost seeking* optics continues to be the predominant one, though in recent years, factors such as the search for qualified personnel, new talents and growth opportunities have been very important *drivers*.

Undoubtedly, offshoring strategies bring considerable benefits to the firms they undertake, but the possible critical elements that may emerge do not underestimate. Empirical evidence, in fact, brings various testimonies of companies that have had to review their *offshoring* strategy and in the most extreme cases have had to undertake *reshoring* projects. The causes of this reversal are many. The change in the conditions that motivated the decision to transfer certain activities beyond national borders and the underestimation of indirect costs are just a few of them. At managerial level, short-term decisions were often taken in contrast to the medium to long-term business strategy. Following the great financial and economic crisis of 2007-2008, the governments of the more developed countries have started to launch programs aimed at encouraging the return of demoralized activities in the country to increase the level of employment. In addition, cultural distance and loss of quality control have also had a major influence on pushing businesses to reconsider their position beyond national borders.

In support of what has been said in the existing literature (Belvedere and Grando 2017, Gauthier 2005, Elkington 1997), it is evident that most of the repatriation decisions

of the productive activities are aimed at overcoming the problems caused by previous offshoring projects whose overall impact on performance was unfavorable (Stentoft *et al.*, 2016). As far as the "cost" performance is concerned, the most common disadvantages of offshoring are the increase in labor and logistics costs (Tate 2014, Tate *et al.*, 2014), higher coordination efforts than expected and high transaction costs (Gylling et al 2015; Gray *et al.*, 2013; Kinkel and Maloca 2009); as well as productivity (Pearce, 2014). As far as quality is concerned, many offshoring experiences show poor conformance to specifications made in extraneous plants (Joubioux and Vanpoucke 2016; Stentoft *et al.*, 2015; Arlbjørn and Mikkelsen 2014; Tate *et al.* 2014). Also in terms of time and flexibility, the decision to produce overseas either through ownership structures or through outsourcing solutions often involves longer delivery times that have become a higher exposure to the risk of volatility in demand (Fratocchi *et al.*, 2016; Bailey E De Propriis 2014; Fratocchi *et al.*, 2014). Focusing on sustainability performance, as environmental and labor standards become synchronized and standardized, incentives to the offshore sector in under-regulated countries become weaker, while the brand's reputation risk increases (Ellram 2013; Ellram *et al.*, 2013 , Gray *et al.*, 2013).

Offshoring is a great asset to generate, but to benefit from it, all aspects of the offshoring need to be considered, and above all any critical scenarios that may arise. In an international competition scenario, all the factors can be relevant, and it's vital not to miss anyone. It needs a thorough analysis in order to make the most appropriate decisions and do not make valuation errors often dictated by imitative behaviours.

In the next chapter, our focus will be on the phenomenon of backshoring, in particular on its evolution and the decisive drivers of the offshoring project conversion. We will try to explain how the process of returning to the country of origin occurs through the major business cases.

CHAPTER 2. THE STATE OF EMPIRICAL AND THEORETICAL LEVEL ART¹⁴

Introduction

Over the past two decades, there has been a structural change and a significant delocalization of production that leave international production increasingly global and the offer of goods and services of a country increasingly dependent on the economic activity of other countries (*offshoring*). In recent years, in addition to the phase of the *offshoring*, some new phases can be identified, including the backshoring strategies in the country of origin of activities previously outsourced abroad. Recently, in fact, there has been a strategic redeployment of production that has been imposed both by the crisis and also by the changes in conditions of the countries chosen for offshoring.

The same factors that, previously pushed to outsource production activities (the rising cost of labor, more costs of coordination and control, scarce quality of production processes, violation of industrial secrets), now seem to determinate a new phase for the strategies relocation of productions.

The ‘return’ strategies to country of origin of production activities previously outsourced abroad have been defined using several other terms (*backshoring, reshoring, back-reshoring, near-shoring, on-shoring, in-shoring*).

Also the determinants of the phenomenon are the centre of a heated dispute. It could be related to a strategic decision of the companies, as a consequence of the complex process phase of the companies internationalization resulting from the deterioration of ownership, location and internalization benefits over time, aimed to reorganize their activities on factors such as process security, high quality, proximity to the customer, as a response to new consumer patterns (Benito *et al.*, 2011; Fratocchi *et al.*, 2014); or a mechanism to correct managerial mistakes made at the moment of the initial decision of *offshoring*, as conceptualized by Kinkel and Maloca (2009); or an

¹⁴ From this chapter a scientific article was published in the Economic Journal of the South, pp. 405-432, DOI: 10.1432 / 85197 - "The new phenomenon of return strategies in Italy: backshoring", Talamo G., Guarneri F. (2016).

adaptation to new patterns in consumption matters, such as the *made-in* (Musso *et al.*, 2012).

Despite the increasing attention by academic literature, the press, and consulting companies (De Backer *et al.*, 2016, The Economist, 2013, UNCTAD, 2013) the definitions are fragmented, there is a lack in the consolidated literature on the phenomenon and the availability of data and the empirical evidence is still limited (De Backer *et al.*, 2016; Fratocchi *et al.*, 2014). However, there are some national and international *surveys* that examine the more significant factors for the strategies of *backshoring* (De Backer *et al.*, 2016; Boston Consulting Group, 2014; Kinkel, 2014, Bailey and De Propris, 2014; PricewaterhouseCoopers-PwC, 2014; UniClub More Back Reshoring, 2014). On the basis of the information extrapolated from these and other sources on individual cases related to Italian companies, it is possible to note that, *backshoring strategies* are involving the redefinition of production patterns and internationalization strategies, also on the Italian market. In this regard, the consulting company PwC and the Ministry of Economic Development, are in collaboration with “Sistema Moda” Italia which have proposed a *backshoring project* that aims to create the necessary conditions to back-shore productions to Italy and to increase the productivity in two pilot areas, Apulia and Veneto (Centro Europa Ricerche, 2015; Pricewaterhouse Coopers, 2014).

In the light of the available information, the current work being carried out will examine the actual situation regarding the phenomenon of *backshoring* in Italy.

In this chapter, after a first part focused on the literature review on the various definitions of the backshoring term, the various reasons, advantages and risks will be presented. The recent international surveys of the backshoring phenomenon and an analysis of backshoring in Italy will be presented. In particular, the causes and new strategies adopted by Italian companies that had previously relocated production abroad. Finally the industrial policies adopted in the USA and the EU, with a focus on Italy and how backshoring can represent opportunities for economic recovery will be analyzed.

2.1 The state of art of backshoring

To define the strategic decisions connected to a reconsideration or a change of the previous choices of *offshoring*, there is a wide debate that gave rise to a terminological confusion to classify and to describe the phenomenon. The choices to come back to the country of origin can be connected to several definitions:

1. *reshoring*
2. *backshoring*¹⁵,
3. *back-reshoring*,
4. *inshoring*.

2.1.1 The term *reshoring*

Ellram (2013) and Gray *et al.* (2013) define the return of production activities from the *host country* to the *home country* with the term *reshoring*, mainly used in the USA. Reshoring means a strategic decision regarding the place where to move the production. Depending on the return of production activities (*in-sourcing* or *outsourcing*) the Authors identify four *reshoring procedures*: i) *in house reshoring*: when the previously outsourced production activity returns to be part of the company of the country of origin; ii) *outsourcing reshoring*: when the previously production object of the *outsourcing* moved from the foreign supplier to the country of destination; iii) *reshoring for outsourcing*: if the production activities previously managed in foreign factories of the company are after, when repatriated, handed over to third suppliers (compared to the parent company) of the country of origin; iv) *reshoring for in-sourcing*: in which the production previously outsourced is directly internalized in the domestic production units.

Frattocchi *et al.* (2014), define reshoring as «a voluntary corporate strategy for home-country partial or total relocation of value activities to serve the global rather than a regional demand a of existing or wholly new products that rely on internal (captive) and/or external (Outsourcing) governance modes».

¹⁵ For a complete review of the state of the art on backshoring see: Stentoft, J, Olhager, J, Heikkilä, J, Thoms, L (2016), Manufacturing backshoring: a systematic literature review, *Operations Management Research*, 10(3), 1-10.

Kinkel (2014), based on the four categorization of outsourcing and offshoring concepts identified by Sako (2006), analyzes reshoring modalities distinguishing relocation into two categories: *outsourced backshoring*, where production was entrusted to outsiders, and *captive backshoring* where foreign factories were owned by the company itself. According to the German scholars, in the first case, the main problems are related to product quality and logistical costs. As for the second mode, the problems are related to the difficulties of coordination between the parent company and the foreign affiliate.

2.1.2 The term backshoring

Holz (2009, p. 156) defines *backshoring* as follows: «the geographic relocation of a functional, value creating operation from a location abroad back to the domestic country of the company». The Author underlines how, the concept of *backshoring*, mainly used in Europe, cannot be meant as a disposal abroad or a divestiture, but as the relocation of the company to the country of origin (*home country*) of value activities localized in international geographical contexts (*host country*). It is about, therefore, a return of manufacturing activities in national factories owned by the company or carried out from suppliers present in the same country of the parent company.

Kinkel and Maloca (2009, p. 155) define *backshoring* as a «re-concentration of parts of production from own foreign locations as well as from foreign suppliers to the domestic production site of the company». The Authors underline the re-concentration of a production unit in the *home country* of a production activity previously carried out abroad in factories owned by the company or by local suppliers. Kinkel and Zanker (2013), have conceptualized the aspect of the re-concentration as the production capability, that takes advantage from the benefits of the use of a higher production capability and a higher relation of variable costs, “correcting” the locality and focusing on how, for the re-concentration, it is necessary a previous production carried out abroad.

Mouhoud (2007), building on different cases of *backshoring*, has identified, since 1980, four waves of *backshoring* that take into consideration the following criteria: the country; the headquarters of the company; the industrial sector; the reasons that have pushed the company to outsource. The first *wave* of *backshoring* coincides with the start

of the automation of the production process, thanks to which it was possible to reduce production costs and in particular the labor costs. This has levelled the competitiveness in labor costs between the host country and the home country. The second wave mainly concerns the German industrial sector, that already registered in the first half of the 80', some *backshoring* cases¹⁶. The third wave concerns other European countries that, following the example of German companies, have adopted the strategy of *backshoring*¹⁷. The last wave can be allocated at the beginning of the new Millennium¹⁸.

The existence of *backshoring* cases also seems interesting for managerial implications. A part of the literature (among other also Kinkel and Maloca, 2009) affirms that these choices are the consequence of some previous corrections of managerial mistakes regarding the decision to outsource production activities. Other Authors (amongst others also Dachs and Kinkel, 2013; Fratocchi *et al.*, 2015) state that, beyond the assumption of a mere correction of previous managerial mistakes, it may also take into consideration the deterioration over time of the existent conditions at the moment when the decision to outsource was made.

Fratocchi *et al.* (2015) proposes a definition “operative” of *backshoring*, in other words a definition of a summary of theoretical concepts proposed in the academic and managerial fields: *back-reshoring*.

2.1.3 The term *back-reshoring*

Back-reshoring means: “ a – deliberate and voluntary – company strategy that aims to domestic relocation (partial or total) of activities carried out abroad (directly or through suppliers) in order to face the local demand, regional or global”. (Fratocchi *et al.*, 2015, p. 131). The authors suggest a dynamic approach to international localization procedures of companies, and identify in the *back-reshoring* one of the phases of the development of manufacturing activity at international level.

¹⁶ Bosch is one of the first case of German *backshoring*.

¹⁷ At the beginning of the '90s the sectors interested are: Electronics, in particular, but also textile. Some example: Nathan for toys; Sagem for mobile phone; Essilor for glasses; NafNaf and Caroll for clothing

¹⁸ For example, Nokia, since 2014 Microsoft Mobile, after three and a half years of permanency in Romania decided to return the production to Finland.

Analyzing the factors that have facilitated the process of return and relocation, total or partial of the production and of inputs procurement in the *home country* (*backshoring*) or in countries geographically closer than those countries where it was initially invested (*near-shoring*), we can identify three category of factors: economic, strategic and operative (Ricciardi *et al.*, 2015).

Among the economic factors there are production costs and labor costs, in particular, the reduction in the differential of the total costs of production between western countries and foreign countries of relocation; the increasing labor cost in the Asian countries and in the emergent markets (Leibl *et al.*, 2009; Sirkin *et al.*, 2012; Kinkel, 2012); the increasing cost of raw materials, fuel, duties, taxes, and of rates (Goel *et al.*, 2008; Leibl *et al.*, 2011; Dachs e Kinkel, 2013).

Among the strategic factors there is: the emergence of implicit costs that makes the contract less effective and economically less efficient (Raiborn *et al.*, 2009; Larsen *et al.*, 2013); the intention to reactivate the total control on critical procedures, activities and/or resources in order to act as a strategy to react properly to solicitations from the external environment (Willcocks, Smith, 1995; Khalfan, 2004; Ricciardi and Pastore, 2010); improve the quality of the products, considered inferior compared to the standards requested, with negative effects on the reputation of the company *brand* and on the economic-financial *performances* and to be, in this way, more competitive on the market (Agrawal *et al.*, 2003; Kinkel and Maloca, 2009; Leibl *et al.*, 2011; Kinkel, 2012; Dachse Kinkel, 2013; Kinkel and Zanker, 2013).

Among the decisive operative factors for the choices of *backshoring*, the literature (among other, Kinkel *et al.*, 2007; Ferreira and Prokopets, 2009; Dachs and Kinkel, 2013; Kinkel and Zanker, 2013; Fratocchi *et al.*, 2015; Ricciardi *et al.*, 2015) refer to: 1) *transport* costs and labor cost¹⁹; 2) the disadvantages due to the delay in delivery of the goods²⁰; the presence of restrictions in setting orders determined by the payload of the

¹⁹ For example, in China, in addition to the costs of labor, also those regarding the logistics and transport of goods, storage and the anticipation of the time of delivery of the order have increased (advance payment). (Fratocchi *et al.*, 2015).

²⁰ The delay in the delivery of goods concerns the relationship between the speed in changing tastes of the customers and the average time spent it takes by the ship, for example, from China to Europe. Zara group, for example, that renews its catalogue every three months, unlike other competitors that renew every nine, has decided to carry out strategies of *backshoring* and *near-shoring* precisely because of the time

containers and the lack of responsiveness to customer needs²¹; 3) the supplies of the contractors and company not directly controlled (see the activities moved to China); 4) the incentives to return and more flexibility of the labor market. All of that has to be added to the political/social risks, and the risk to change as well as the lack of qualified technicians and personnel.

All this adds to the political/social risk, the risk of exchange and the lack of qualified technicians and staff. Finally, the backshoring process can be better understood by analyzing offshoring processes, foreign direct investment, de-internationalization, near-shoring. This work follows the line dictated by Tallman (2011), which clarifies that it is good not to consider these processes as a single modern phenomenon since in reality they have different characteristics.

Foerstl (2016), on the other hand, defines *reshoring* as «transferring value creation from offshore to geographically closer positions [...] regardless of ownership» (Foerstl *et al.*, 2016: 495) And further subdivides the concept from the geographic point of view in backshoring (Foerstl *et al.*, 2016) or back-reshoring (Fratocchi *et al.*, 2014), ie transfer to the enterprise's country of origin and near-shoring (Foerstl *Et al.*, 2016) or 'almost-reshoring' (Fratocchi *et al.*, 2014), ie transfer to a nearby (but not within) locality of the country of origin. Then put the 2 terms (backshoring and back-reshoring) on the same definition plan²².

2.1.4 Templates: Inshoring, Foreign Investments, De-internationalization and Return Relocation

While offshoring means the process of internationalization and delocalisation of activities in foreign establishments, the opposite of which is the in-shoring, i.e. the return to the home-based establishments located elsewhere abroad (Dholakia *et al.* , 2012, Skipper, 2006). Holz (2009) points out that in the Anglo-American language the word

spent for the transport from China that cannot allow a rapid modification of its production considering the change of taste of its customers. (Fratocchi *et al.*, 2015).

²¹ Regarding the load to be sent, China considers the *container* as minimum size for shipment and this represents an obstacle for all foreign entrepreneurs that need to order smaller parcels (Fratocchi *et al.*, 2015).

²² From this paragraph onwards, the term backshoring will be used.

identifies an investment by foreign companies in a country other than that of origin, whereas in Germany it is used as a synonym for back-reshoring (2009). At the same time, Liao (2012) defines in-shoring home-based supply of goods by an enterprise.

Fratocchi *et al.* (2015), distinguish three concepts relating to the transfer of FDI into production or production activities: 'foreign divestment', 'de-internationalization' and 'return relocation' and defining backshoring as an inverse decision to a previous choice of offshoring and propose it as a possible step of a process of internationalization of non-linear society.

Foreign direct divestments mean the disposal of the foreign activities previously moved. There are several definitions of foreign disinvestment proposed by the literature: decisions “deliberate and intentional” at management level (Boddewyn, 1979), management solutions, as a result of force majeure (Kobrin, 1980). The common conception of these Authors is to consider a foreign production unit in its whole, rather than refer to a specific activity of the value chain. In this regard, Belderbos and Zou (2006) define international disinvestment as cessations of production activities of an existent member. Several Authors share the thinking of Boddewyn and Torneden (1973), which define the foreign disinvestment as a reduction, intentional or not intentional, of the percentage of the participation of the active foreign direct investments. Therefore, the foreign disinvestment can refer to the company controlled in its whole, rather than to a specific activity as in the case of *backshoring* (Fratocchi *et al.*, 2015).

Moreover, this phenomenon does not require the sale of the totality of FDI, but is also based only on the repatriation of a production line (Fratocchi *et al.*, 2015).

Hennart *et al.* (2002), affirms that foreign divestments are considered as negative events. Recent studies (McDermott, 2010; Engel and Procher, 2010) demonstrate that the recent economic crisis has increased the probability of divestment.

Another terminological reference to be analyzed is the de-internationalization. Welch and Luostarinen (1988) develop the concept of de-internationalization starting from the prerequisite that the internationalization of companies does not necessarily represent a durable process. Calof and Beamish (1995, p. 116) analyze de-internationalization «as a deliberate adaptation of the firm’s degree of international exposure to the international environment», or rather a strategic adaptation conditioned

by the international environment conditions. Benito and Welch (1997) add something different to the concept of de-internationalization, considering this process not only the consequence of an intentional action, but at times also like a constriction in rethinking or reduce the presence of the undertaking in global contexts. In fact, depending on the agents that influence the decision of de-internationalization, they distinguish the total de-internationalization (when it is about the closure or the cession of the entire foreign subsidiary company) from a partial one (if it is about some activities of the value chain). Casson (1986), instead, distinguishes the de-internationalization of control from the ownership one. The guiding principle of this group of definitions is represented by the fact that the de-internationalization is generally perceived like an undesirable operation: rethinking regarding strategic choices.

Despite the theoretical reference to the international disinvestment concept it is very useful in order to identify the definition of *backshoring* phenomenon, it is evident that the two concepts are not homogenous between them. McDermott (1989), in fact emphasizes that the divestment of the foreign subsidiaries companies do not imply the relocation of production activities in other places, as it occurs instead in the backreshoring. Benito, instead, focuses, on the fact that the disinvestment can be motivated by «relocation or concentration of production resources at national, regional, or global level» (1997, p. 1366).

In their turn the concepts of de-internationalization and foreign disinvestment cannot be overlapped to *backshoring*, because, according to Holz (2009) *backshoring* can occur also, but not necessarily, with regard to de-internationalization activities (partial) or to foreign divestment. This theoretical conceptualization allows the progressive use of the production capability of the foreign system in order to satisfy both the local and the regional market (Holz, 2009).

Return relocation is the first expression used by Jungnickel (1990) as regards those decisions that from time to time concerned: A) the foreign affiliate as a whole or a single function of the same; B) the return of manufacturing activities to nationally owned establishments or to suppliers located in the same country of origin of the casualty; C) the closure - in whole or in part - of the production unit located abroad.

In conclusion, Frattocchi (2014), analyzing the various definitions proposed by the literature, lists three main features regarding backshoring:

1. is the reverse decision, compared to the previous choice of offshoring;
2. does not necessarily imply the repatriation or closure of all the delocalised activities or of the whole plant;
3. it is essentially a relocation decision to another site in the country of origin.

In the following paragraphs, when using the term backshoring, reference will be made to this definition.

2.1.5 The near-shoring term

In the previous chapter, this term was used to outline specific offshoring strategies. However, this concept can also be used in an inverse manner in this context as well. In fact, with reference to return logic, near-shoring strategies indicate the relocation of formerly outsourced overseas activities in relatively close to home country countries. A common example may be the case of a USA company that had previously started offshoring projects in China, and then decided to move some of these manufacturing activities to Mexico. Such decisions are taken in order to gain greater control and to save on coordination costs. In addition, they allow to considerably reduce the so-called time to market. This result is of considerable importance, especially for that product category characterized by a very short life cycle.

2.2 The backshoring manufacturing

The backshoring phenomenon is more concerned with manufacturing activities, as almost all companies in the home country operate in this sector. However, recently, it has also started to engage in more sensitive activities in the field of services. Suffice to say that, as evidenced by Holz (2009), the first to use the term backshoring, is Michael Field, president of Oracle U.S.A., during an interview with Fortune Magazine. The topic of the interview was the return to the United States of the IT business, first delocalized in India. The well-known PricewaterhouseCoopers consulting firm estimates that in the next

decade the phenomenon of return on services will be significantly higher, especially in the field of R&D, back-office and telecommunications. Software programming, call-centres, and data-management activities were among the first to be delocalized. As for manufacturing, even here the difference in labor costs is rapidly eroding, leaving less and less margin businesses and all problems related to the distance to be managed (The Economist, 2013).

In addition to the reasons for the increase in labor costs, many companies realized that they considered the peripherals of the activities, which were of central importance. The first cases of return occurred in the 1980s, but in recent years there have been significant increases. Backshoring has attracted academic attention and press coverage only in recent years, for which there is no official database and statistical data, which observe the phenomenon, are very limited and difficult to find. In fact, such return strategies are called "error correction mechanisms": management has not properly assessed all the disadvantages of the investment project abroad. For this reason, companies are reluctant to talk about their own internal choices (Kinkel and Maloca, 2009). Moreover, the recorded and observed cases are almost entirely in the productive sector. As a result of the work, for these reasons, attention will be focused on cases of backshoring manufacturing.

In particular, backshoring studies focus on companies operating in the Textile, Clothing, Leather and Footwear Industry (TCLF), whose products are often sensitive to the "Made In" effect, a frequent motivation that pushes Companies operating in these areas to return (Ancarani *et al.*, 2015; Ashby, 2016; Fratocchi *et al.*, 2016).

2.3 Motives: Offshoring vs. Backshoring

The reasons behind offshoring and backshoring are typically studied as separate entities in literature. This dissociation hinders a deeper understanding of the two phenomena, and denies the conceptualization of backshoring as a possible phase of the internationalization process. Di Mauro *et al.* (2017) cover this gap in order to understand what are the common motives behind offshoring and backshoring at the corporate level in

order to understand whether backshoring is a "failure" of offshoring, or rather the evolution of strategies Competitiveness and location of the company.

In the literature, many reasons for backshoring have been proposed (see Bals *et al.*, 2016; Foerstl *et al.*, 2016; Fratocchi *et al.*, 2016; Stentoft *et al.*, 2016). One of the first theories argued that backshoring was born as a correction of managerial-level evaluation errors in planning and insufficient knowledge of the country's investment target (Kinkel and Maloca, 2009). Later, Dachs and Kinkel (2013) agree that backshoring may be caused by the deterioration of the conditions that existed at the time when the offshoring decision was initially taken (Fratocchi, 2014). To recognize backshoring as the reversal of a fully rational offshoring decision motivated by contingencies and changes in either the country of origin or country of origin, such as the growing total cost of ownership in China or lower energy costs in the West (Martinez-Mora and Merino, 2014; Simchi-Levi *et al.*, 2012; Tate *et al.*, 2014). Other scholars have argued that backshoring may be due to the inability of companies to handle the complex challenges they face from de-delegating abroad (Manning, 2014). Finally, backshoring has been associated with the 'Made in' effect deriving from the perception of higher quality of domestic production (Ancarani *et al.*, 2015; Fratocchi *et al.*, 2016; Grappi *et al.*, 2015; Martínez-Mora and Merino, 2014; Robinson and Hsieh, 2016; Tate *et al.*, 2014).

There are numerous variables that have prompted companies to reconsider their strategy of internationalization and their organizational structure, and often the drivers that motivated offshoring initiatives, are also the same ones that now lead to the return of the previously delocalized activities at home. Studies and analyzes on the phenomenon of returning to the country of origin of the previously delocalized activities are still available in limited quantities, and above all, focused on manufacturing backshoring.

Attracting a systematic review of the literature of Di Mauro *et al.* (2017) compare the motives that push companies to relocate and the reasons that drive businesses back home. In detail, the reasons for offshoring are:

- Access to know-how (e.g., knowledge, technology)
- Access to locally unavailable products
- Access to scarce and distinctive resources and materials
- Availability of skilled labour in the host country

- Capacity bottlenecks in the home country
- Countertrade Requirements
- Delivery Reliability
- Economies of scale
- Energy Costs
- Key customers demand to produce in their vicinity
- Foreign market access or development
- Government incentives (including favourable taxation)
- Host country supply base
- Host country trade environment (including legislation)
- Imitation of competitors' strategies ("bandwagon") or counterattacking competitors
- Costs and productivity of skilled and unskilled labour
- New product development
- Operational Flexibility
- Production and logistic costs (except labour costs) reduction
- Proximity to foreign customers (e.g., shorter delivery time)
- Quality Improvement
- Risk Mitigation
- Time to market reduction
- Total Cost of Ownership

The most frequent offshoring motivation is the cost and productivity of work in the host country (Kinkel and Maloca, 2009; Gylling *et al.*, 2015). Another frequent offshoring motivation is the availability of skilled labor also Mykhaylenko *et al.* (2015) claim that this driver primarily applies to service offshoring.

For backshoring, however, 42 reasons have been identified:

- Termination of supplier relationships
- Change in firm's business strategy (e.g., vertical integration, new business area)
- Coordination costs

- Correction of earlier managerial mistake (e.g., lack of knowledge about the foreign destination, bandwagon effect, lack of systematic location planning)
- Customers 'gratitude and willingness to buy
- Customs duties for re-import
- Demand changes and volatility in the home/host country
- Emotional elements (e.g. patriotism/loyalty)
- Energy costs and shortage
- Environmental and social sustainability
- Excessive paperwork/Administrative costs
- Exchange rate risks
- Firm's global reorganization
- Freight costs
- Global supply chain risks
- High inventory levels
- Home labour market flexibility
- Increased home country productivity
- Labour cost' gap reduction
- Lack of the infrastructure in the host country
- Lack of skilled workers in host country/Availability in the home country
- Logistics costs
- Loss of innovation potential/Vicinity to R&D
- Loss of know-how in the host country/IP risks (including brand counterfeiting)
- Made-in effect
- National subsidies for relocation
- Need to increase customer satisfaction
- Payments terms
- Penalties for late orders
- Poor manufacturing quality culture in the host country

- Product/Process/Organizational Innovation (e.g. lean management, automation)
- Production and delivery time impact
- Psychic distance
- Purchase order rigidity (also in terms of minimum order)
- Raw material availability
- Redefinition of the global supply chain (including vertical integration)
- Reduced operational flexibility
- Reduced responsiveness to customer demand/Customer proximity
- Technology clusters (at the home country) and spill over benefits
- Total Cost of Ownership
- Union pressure at the home country
- Untapped production capacity at home/Capacity bottleneck in the host country

Grandinetti and Tobacco (2015), Huq *et al.* (2016) and Robinson and Hsieh (2016) consider competitiveness as a key factor in backshoring decision-making. Backshoring is understood as a change in localization strategy by Bals *et al.* (2016) who, in this context, conceptualize backshoring as not merely a correction of a decision-making error (Gray *et al.*, 2013; Kinkel and Maloca, 2009) but rather as a deliberate strategy (Mintzberg and Waters, 1985), intended to respond to exogenous or endogenous changes that result from it (Fratocchi *et al.*, 2015; Gylling *et al.*, 2015; Martínez-Mora and Merino, 2014; Mugurusi and de Boer, 2014).

Maintaining the desired quality standards is also a major problem as both cultural and physical distance make quality control difficult and costly. For manufacturing companies from countries such as Italy, a very important and important factor to consider when deciding to transfer production is undoubtedly represented by the loss of the so-called "made in" effect, hence the prestige and the possibility of requesting a higher premium price (Bals *et al.*, 2016, Grappi *et al.*, 2015).

Significant driving factors are also the increase in costs, delivery times and the reduction in the labor cost differential (Fratocchi *et al.*, 2013). Over the last few decades,

it has been particularly attended to the exodus of manufacturing activities to countries in Asia, where it was possible to access labor and skilled, low-cost staff. An article by The Economist in January 2013 already noted that salaries in China and India had risen 10-20% over the previous decade - with the European and American ones who had barely moved. According to an estimation from the Boston Consulting Group (2014), in certain highly industrialized areas of China, such as the Yangtze River Delta area, where specialized personnel are available, the salary has increased considerably. Indeed, to date, the cost of labor is equal to 70% of the American correspondent; A significant increase, if we consider that in 2010 it was 31%. In 2003, the monthly gross of a Chinese worker in an urban area was 13696 yuan a month in 2013, it was more than tripled to 50,723 the International Labor Organization, estimating that real wages between 2000 and 2008 are Up from 7.1 to 7.8% per annum. In emerging countries, such as the People's Republic, wages are rising, also due to favorable government policies; Furthermore, the rapid industrialization and the enormous inflow of FDI meant that the quality of life of workers improved, prompting them to claim a higher salary.

In advanced countries, such as the United States, salaries grow at a much smaller pace, or even remain stable, this situation greatly affects offshoring strategies and leads to reconsidering organizational choices made. Linked to this factor, there is the problem of high staff turnover and the difficulty in finding suitable staff, which results in a reduction in productivity. In fact, the high concentration of firms makes the demand for skilled and reliable workers very high, competing companies are willing to offer a better pay for attracting employees, and workers are ready to abandon the company they work for For just a little higher wage. This precarious situation makes control and coordination costs very costly. Transport is another very important element, especially with regard to overseas relocation. The high shipping times and the minimum quantities, depending on the size of the container, result in a reduction in operational flexibility (Ferreira and Prokopets, 2009). The logistical and relevant factor, especially in contexts where time to market is the key competitive leverage, as evidenced by Zara's recent decision to "shrink" its supply chain by turning to the Mediterranean basin and Portugal part of the purchases made before In Asian countries (Frattonchi, 2014). Distance, therefore, plays a key role as the increasing cost of transport undermines the benefits of producing where labor costs

are lower (UniClub MoRe Back-reshoring, 2014). Innovation, in fact, was heavily affected by low-cost localization, and R&D usually located in the country of origin of the mother-house (The Economist, 2013). In countries like China, it is difficult to protect intellectual property, as the laws in this matter are much less restrictive.

Another important factor to be underestimated is the theme of environmental protection and workers' conditions. The company is becoming more sensitive to these serious problems and for Western companies it can not be allowed to do their business without considering this factor. Often in developing countries, companies operate without respecting the environment, and working conditions in most cases are not unacceptable. Lastly, a very important and not underestimated element is "country risk" and "exchange risk". Country risk is linked to a situation of strong internal instability, which can lead to a break in supply chain (The Economist, 2013). Instead, the "exchange rate risk" is related to currency developments and monetary policies, for example, in the last period, the Chinese yuan has experienced considerable appreciation.

By comparing the reasons behind offshoring and backshoring, it becomes an overlapping of the main motivations. This suggests that often the expectations of offshoring were not met and prompted a rethinking strategy, hence the "mistake" hypothesis (Kinkel and Maloca, 2009) when, for example, reference is made to operational flexibility for Offshoring and reduced operational backshoring flexibility. The overlapping relative to government incentives for offshoring and national transfer subsidies for backshoring, it can be pointed out that over time some of the benefits of offshoring could be taken as an example from the country of origin in an attempt to hinder or reverse the relocation trend abroad.

2.4 Recent international surveys regarding backshoring phenomenon

Despite the increasing attention on *backshoring* strategies in the origin country of activities outsourced abroad (for a complete overview, see, De Bacher *et al.*, 2016; Centro Europa Ricerche, 2015; Fratocchi *et al.* 2015; The Economist, 2013; UNCTAD, 2013), up to date, without official statistics, there is not a real dimensioning of the phenomenon. There are two factors that allow to overcome an anecdotal context: some

surveys concerning the behaviour of some companies regarding foreign investment decisions, and some interventions by consulting companies that re-discuss *offshoring* decisions in the light of economic changes (Mariotti, 2009). The data that comes to light from the few available sources mainly concern activities previously outsourced especially in China, Asian countries and Eastern Europe, in fashion, electrical and electronic equipment sectors. The available evidence show that the strategy of *backshoring* cannot be simply referred to as corrections of previously managerial errors, but to a dynamic approach of strategic decisions taken after the change of the conditions that affect on the localization of activities within international production networks (Centro Europa Ricerche, 2015). In several cases it comes the increasing value obtained on markets, the geographical origin of the products (*made-in effect*), the quality the products and services, the access to innovations, the costs and time of supply.

Among the few available sources, we can distinguish:

a) the historical series of *Fraunhofer Institute for Systems and Innovation Research*. It concerns a *multiple purpose* statistic inspection carried out every two years and regarding a representative sample of 1.663 German companies. Up to 2006, the analysis was focused on companies working in metalworking and electrical sectors; subsequently the attention has been extended to the entire manufacturing sector. Summarizing the results gained in the last 15 years regarding backshoring strategies, Kinkel (2014) has underlined that only Germany has counted between 400 and 700 cases of companies that have relocated (entirely or partially) production activities previously outsourced beyond boundaries. More specifically, the phenomenon increased between 1997 (4% of the interviewed companies) and 2001 (6%) which was followed by a decrease, with a stable share of between 2% and 3% from 2006 onwards (Centro Europa Ricerche, 2015). From this it comes to light that, probably, German companies have overestimated the opportunities of reduction of costs following the fall of the Berlin Wall.

b) The empirical evidence of the *European Manufacturing Survey* regarding a series of UE countries: Austria, Denmark, France, Germany, Netherlands, Portugal, Slovenia, Spain, Sweden, Switzerland and Hungary (Dachs and Zanker, 2015). In this case it also concerns a statistical sample investigation that is not focused on *backshoring phenomenon*, but concerns the managerial dynamics of the manufacturing sector. The

available data show that between 2010 and 2012, 4% of the interviewed companies have repatriated their productions, with a contraction of 0,6% in the period between 2007-2009 (Eurofound, 2013;Centro Europa Ricerche, 2015).

c) The survey made in the United Kingdom from *London-based Engineering Employers Association*, in collaboration with the *accounting company BDO International* shows that 14% of 300 companies that, between 2008 and 2009, had outsourced abroad, have diverted the strategy, returning the production to the United Kingdom (Flanagan, 2009).

d) The study carried out by the Offshoring Research Network of the *Duke University* and by *Pricewaterhouse Coopers* on a sample of 100 European and American companies, has revealed that the crisis has changed the strategic *drivers* in respect of the *offshoring operations*: 15% of companies are directed towards *backshoring*, while 14% are inclined to further repositioning in countries where the production costs are lower than China, therefore Southeast countries such as Sri Lanka, Egypt, Nicaragua (Lewin *et al.*, 2009).

e) A survey made by *Millward Brown* in March 2014 on behalf of Confederation of British industry on a sample of European companies²³, has observed that the German companies are those more interested to back-shore: 50% of the interviewed companies have repatriated production and employments, while the other 50% intends to do so in the next three years. From this survey it comes to light that one third of the interviewed companies, that on the whole occupy 1,28 million of employees and invoice 938 millions of pounds, have already repatriated, partially, some production activities in the last three years. In particular, 73% declare a better quality of production in the country of origin, while 54% considers this important to be closer to markets and loyal customers. Italian companies percentage is 29%. At European level 40% of companies are favourable to *backshoring* while only 6% are contrary (SVIMEZ, 2015).

f) An inspection carried out in the USA in January 2009 on 100 companies *leader* in *high-tech* points out how about 42% of them have carried out investments abroad, compared to 79% of the previous year. In addition many of them (22%) stated

²³ The sampled companies were from the following countries: Italy, Germany, Great Britain, France and Holland.

that the USA is the privileged destination to invest, and only 16% preferred China and 3% Eastern Europe. This is a consequence mainly caused by the increasing of the petrol prices that has considerably affected the transport costs, of production inputs and outputs, as well as by the dollar fall, and in general the Chinese²⁴ and Asian wages inflation. (Goel *et al.*, 2008). These factors, combined with other typologies of costs (for example, the reworking for the scarce quality of the products, the logistics and transaction costs) have identified “three Optimal Region” (Mariotti, 2009): China which tends to *offshoring*, Mexico that tends to *near-shoring* and the United States that, instead, tend to *backshoring*. According to recent data (Reshore Initiative, 2014), up to all of 2014, 357 decisions to back shore have been registered and that has brought – in the last considered year – a flow of new employment comparable to that lost due to the new choices of *offshoring*.

g) The Uni Club More Back Reshoring Research Group²⁵ has conducted empirical evidence from secondary sources²⁶. The database is made up of 728 cases of 600 Italian and foreign companies, as an enterprise has implemented on average 1.2 decisions of back-near-reshoring. The available data show that there is a substantial level of evidence between the USA and the EU (45% and 52% respectively), demonstrating that the phenomenon directly involves Western countries and is not specific to the United States, as suggested by Historical economic Leunig (2011). In the area of the old continent, Italy and Germany until 2014 were the two most represented countries, confirming that they are the two most-oriented manufacturing economies (Fratocchi *et al.*, 2015). In 2015, however, the two most representative countries are Italy and Great Britain (respectively 121 and 68 cases), (Zanoni, 2016).

h) The necessity to have updated data regarding the backshoring strategies has recently been recognized by “Eurobond” (2013), the European Foundation to improve

²⁴ A study carried out by the Boston Consulting Group (2014) revealed that salaries in China are increasing in a considerable manner of up to 15-20% per year in particular in Shanghai and Tianjin.

²⁵ The acronym stands for the initials of the respective Universities of Catania, L'Aquila, Udine, Bologna, Modena and Reggio Emilia.

²⁶ Uni Club More Reshoring Research Group project and coordinate their bank data on transactions of *backshoring* and *near-shoring carried out* by manufacturing firms. The various cases studied are identified thanks to the continues monitoring of international scientific literature on matters of international business and management global consulting firms, the information reported by economic and managerial newspapers at international level and search engines.

life and work conditions. The agency has recently established a European Observatory on *reshoring*, and its implementing and managing for the three years 2016-2018 have been given to four of the five Italian Universities of Uni Club More Reshoring Research Group. The Observatory will control the decisions to relocate manufacturing activities of European member states and non European states. Moreover, the EU and member states legislative regarding industrial policies that support reshoring will be detected, analyzed and discussed in more detail in the next paragraph (Eurofound, 2013).

2.5 The size of backshoring

2.5.1 *Backshoring in the world*

As mentioned in the previous paragraph just recently, academic literature has come close to the phenomenon of backshoring, the available evidence is still limited and, in most cases, focusing only on productive activities. As already mentioned in the previous paragraph, thanks to the Uni-CLUB MoRe Back-Reshoring project, a database was built, describing the intensity of the phenomenon. The evidence regarding companies implementing a number of back-and-near-reshoring strategies is an interesting discovery. More specifically, it raises the question of whether the two strategies are simple "short-term corrections" (Kinkel and Maloca, 2009). Rather, the joint implementation of the two resource decisions seems to be part of a wider and more complex dynamic adaptation strategy to changing environmental conditions that lead companies to adopt "regional" production strategies so it is not so important that production facilities (Simchi-Levi *et al.*, 2012), but are fairly close to market demand to reduce shipping costs and delivery times²⁷.

The cases analyzed represent a relevant empirical basis in order to formulate hypotheses about the phenomenon of back-reshoring through various variables, such as

²⁷ In this regard, the case of Italian mechanical engineering Bolzoni is interesting, which has supported some production lines from Finland and Spain to Italy and, at the same time, to other Estonian countries in Finland and Finland in Germany. While we acknowledge that our data is in no way exhaustive and can not fully represent the investigated phenomenon (eg some industries, such as clothing and footwear, in some countries, such as the US and China, as well as some companies, Such as Apple

temporal, the one relating to the geographic position of the market where offshoring and motivation had been carried out.

The three countries with the largest number of cases are United States, Italy followed by Britain and Germany, which are among the developed countries with the highest production specialization (Figure 9).

Figure 9: Backshoring Cases in the World

GEOGRAPHIC AREA	COUNTRY	DECISIONS	ENTERPRISES	AVERAGE	% ON TOTAL
North America	USA	326	278	1,2	45,2%
	Canada	3	3	1,0	
	Total	329	281	1,2	
Europe	Italy	121	88	1,4	51,8%
	UK	68	63	1,1	
	Germany	63	47	1,3	
	France	42	33	1,3	
	Spain	23	15	1,5	
	Netherlands	12	11	1,1	
	Finland	10	9	1,1	
	Sweden	9	6	1,5	
	Switzerland	7	6	1,2	
	Slovenia	5	5	1,0	
	Belgium	4	4	1,0	
	Austria	3	3	1,0	
	Denmark	3	2	1,5	
	Norway	2	1	2,0	
	Poland	2	1	2,0	
	Czech Republic	1	1	1,0	
	Luxembourg	1	1	1,0	
	Slovakia	1	1	1,0	
	Total	377	297	1,3	
Asia	India	1	1	1,0	2,7%
	South Korea	5	5	1,0	
	Taiwan	2	2	1,0	
	Japan	6	6	1,0	
	Chine(withHK)	2	2	1,0	
	Singapore	1	1	1,0	
	India	3	3	1,0	
Total	20	20	1,0		
Oceania	Australia	1	1	1,0	0,1%
	Total	1	1	1,0	
Africa and the Middle East	Egypt	1	1	1,0	0,1%
	Totale	1	1	1,0	
Total		728	600	1,2	100,0%

Source: own data re-elaboration (Uni-CLUB MoRe Back-Reshoring, 2016)

Italy, world-wide, is therefore the second country immediately after the US to have experienced the largest number of return cases. This figure is consistent, as the

United States is the country with the largest manufacturing offshoring experience, while Italy, Great Britain and Germany are the first three countries in economic terms in the European Union.

Analyzing the geographic variable (geographic position of the offshore market) it emerges that China with 80% of the cases is the country from which the largest number of return activities is being followed by others Asian countries and Eastern Europe.

Figure 10: Offshoring country

GEOGRAPHIC AREA	DELOCALISATION GEOGRAPHICAL AREA									
	China	Asia (no Cina)	East Europe and ex Urss	West Europe	North America	Central and South America	Africa and Middle East	Oceania	n.d	Total
Europe	127	39	64	116	9	5	11		5	376
North America	214	46	2	24	23	14	1	2	3	329
Asia (without China and Japan)	4	1	1	5						11
Japan	3	1	1	1						6
China				2						2
Africa and Middle East			2	1						3
Oceania	1									1
Total	349	87	70	149	32	19	12	2	8	728
% on total	47,9%	12%	9,6%	20,5%	4,4%	2,6%	1,6%	0,3%	1,1 %	100,0%

Source: own data re-elaboration Uni-CLUB MoRe Back-Reshoring, 2016

These results, on the one hand, contradict when emerging from internationally-compiled databases in previous years (see, for example, Kinkel and Maloca, 2009; Kinkel and Zanker, 2013), probably due to the widening of USA context analysis (Fratocchi *Et al.*, 2015). On the other hand, they are in line with empirical evidence, as China has been the main target of offshoring strategies. Moreover, it is a country where labor costs have increased considerably and the protection of intellectual property is difficult. Apart from offering numerous market opportunities and infrastructures, this country also conceals several pitfalls.

The duration of the offshoring strategy is a fundamental variable in backshoring analysis from a temporal point of view. It is highlighted that as many return initiatives refer to offshoring decisions taken within ten years prior to relocation, only 25% took place in less than three years (Fratocchi, 2014).

Figure 11: Offshoring Duration

Years range	Number of decisions		
	USA	West and East Europe	Italy
1 to 5	61	53	24
6 to 10	50	44	15
11 to 20	54	46	26
Over 20	26	45	7
n.a.	1335	212	49
Total	326	370	121

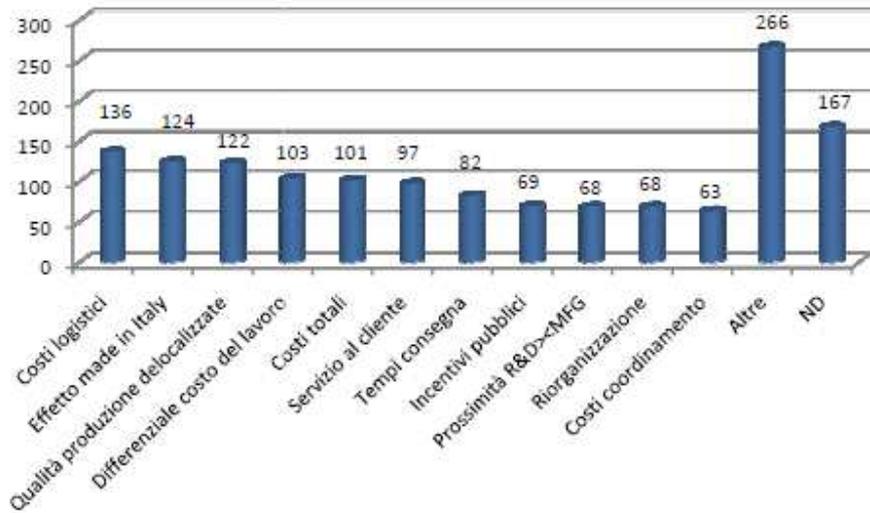
Source: own data re-elaboration Uni-CLUB MoRe Back-reshoring, 2016

From the data relating to the time between the year of the offshoring decision and the subsequent decision of backshoring, it is clear that the latter decision depends on the country in which it was decided to relocate production: the temporal profile most extended to Eastern European countries compared to China and other Asian countries (averaging 10 years vs. 3-4 years).

This is in contrast to the results of previous studies by authors such as Kinkel and Maloca (2009), who, analyzing a sample of German companies, had observed how repatriation decisions were taken in a period ranging from three to five next years. Following this result, according to these scholars, the backshoring phenomenon is a short-term correction of the delocalisation choices previously undertaken. The analysis of the research group shows, however, that return strategies are not merely a consequence of mere managerial errors, but rather depend on medium to long-term changes in the context (Frattocchi *et al.*, 2014).

The stated reasons give rise to logistical reasons both in terms of cost and supply times (136 observations), effect made (124 observations), product quality (122 observations) and cost differential.

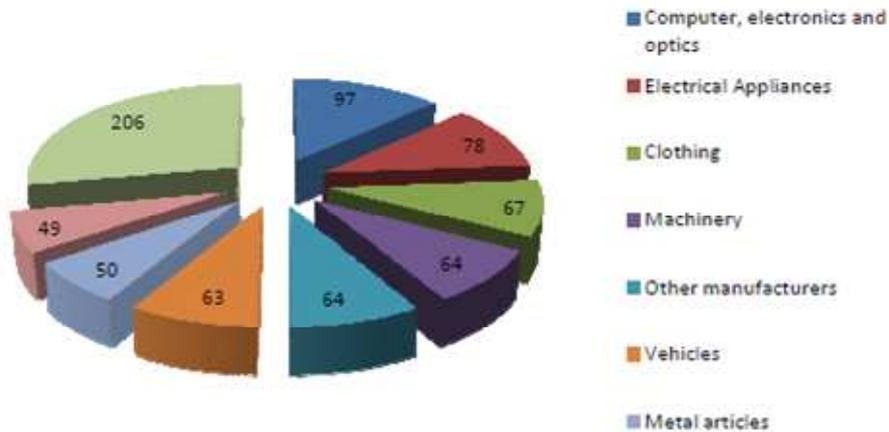
Figure 12: Backshoring motivation



Source: own data re-elaboration Uni-CLUB MoRe Back-reshoring, 2016

Finally, companies that have decided to return their production activities to their country of origin are particularly active in the fashion industry, as evidenced by the 206 empirical evidence. 106 are those of other manufacturing sectors.

Figure 13: Manufacturing sectors



Source: own data re-elaboration Uni-CLUB MoRe Back-reshoring, 2016

2.5.2 Backshoring in Italy

Data from Uni Club More Back Reshoring (2016) reveals that Italy is the second country in the world after the US and the first in Europe to repatriate overseas production activities, with a 20% Global scale and about 42% on a European scale (Fratocchi *et al.*, 2015). From 1997 to 2001, the number of backshoring cases in Italy has declined steadily and then remains steady until 2006. In 2007 there was a substantial increase, reaching a peak in 2009 with 17 cases, reducing by a third As early as 2010. The latest positive change in the number of companies returning to Italy occurred between 2011 and 2012, the year in which the number of companies is quadrupled to 12. In analyzing the data, It is necessary to consider that companies, by their size, have done more than a backshoring operation and that the results for 2009 and 2012 are the result of the fact that the global financial crisis on the Italian economy has been intensified (Uni Club More Back-reshoring, 2014).

Considering the geographical location, it emerges that the backshoring strategy in Italy mainly concerned the Northern regions (95 decisions on 121), primarily Veneto (36), Emilia-Romagna (21) and Lombardy (18).

Figure 14: Italian backshoring by region

GEOGRAPHICAL AREA	REGION	DECISIONS
North East	Veneto	36
	Friuli Venezia Giulia	6
	Trentino Alto Adige	3
	Total	45
North West	Emilia Romagna	21
	Lombardia	18
	Piemonte	7
	Liguria	4
	Total	50
Central	Marche	9
	Toscana	9
	Umbria	2
	Lazio	1
	Abruzzo	1
	Total	22
South	Campania	2
	Puglia	2
	Total	4
Totale		121

Source: own data re-elaboration Uni-CLUB MoRe Back-reshoring, 2016

At the macro-area level, the North-West has attracted 50 companies returning mainly from China and other Asian countries, while Northeast 45, coming mainly from Eastern Europe and the Balkans. The Centre and the South, on the other hand, have few cases. The companies that restored production in the regions of the Centre were 22: 9 in Tuscany, 9 in the Marche, 2 in Umbria and one in Lazio. Backshoring has affected only 4 companies in Southern Italy: 2 in Apulia, 2 in Campania. Sicily and Sardinia are not included (Uni Club More Back Reshoring Research Group, 2016). (Figure 14). These data show that the gap between North and South may not be taken into account, even in companies' return processes. This confirms a close correlation between the geographical breakdown of foreign and backshoring investments.

Considering the areas of specialization of Italian companies, it emerges that, as is the case in the world, in Italy, the sector in which several cases of backshoring occur are textile clothing (29 cases) and footwear (21 cases).

Figure 15: Manufacture sectors

NACE code	DESCRIPTION	DECISIONS
14	Clothing accessories	29
15	Packs of leather goods and the like	21
26	Manufacture of computer and electronics and optical products	15
27	Manufacture of electrical equipment	15
28	Manufacture of machinery and equipment n.c.a.	12
31	Manufacture of furniture	6
30	Manufacture of other means of transport	5
20	Manufacture of chemical products	4
22	Manufacture of rubber articles and plastic materials	3
25	Manufacture of metal products excluding machinery and equipment	3
32	Other manufacturing industries	3
29	Manufacture of motor vehicles	2
10	Food industries	1
21	Manufacture of pharmaceutical products	1
24	Metallurgical activities	1
Total		121

Source: own data re-elaboration Uni-CLUB MoRe Back-reshoring, 2016

Data show that 34% of Italian companies that decided to adopt the backshoring strategy had relocated their activities to China, 24% in Eastern Europe and Russia, and 12% in other Asian countries (Uni Club More Back-reshoring, 2016).

Figure 16: Abandoned geographic area

Abandoned geographic area	Choices	% on Total
China	41	33.9 %
Asia except china	15	12.4 %
Eastern Europe	29	24 %
Western Europe	27	22.3 %
North Africa and Middle East	4	3.3 %
North America	2	1.7 %
Central and southern America	1	0.8 %
N.A.	2	1.7 %
Total	121	100.0 %

Source: own data re-elaboration Uni-CLUB MoRe Back-reshoring, 2016

Despite the great Italian manufacturing tradition, there have been many companies that have started offshoring projects in the past few decades. However, rising costs, distance issues and, above all, an exponential increase in the demand for "made in Italy" products has led companies to reconsider their international position. Companies that have 'luxury' customers have realized that productive delocalisation can be counterproductive in terms of product quality and business reputation. On the other hand, complex productions, such as precision mechanics, require a mix of knowledge, technology and specialized work that are difficult to replicate in emerging countries where it was decided to invest (Il Sole 24 Ore, 2015).

Figure 17: Backshoring motivations

MOTIVATIONS	DECISIONS	% ON DECISION CHOICES
Effect made in	42	41,6%
Improving customer service	25	24,8%
Delocalized production quality	18	17,8%
Global corporate reorganization	15	14,9%
Global economic crisis	14	13,9%
Focus on product innovation / process and closeness Production / Research	13	12,9%
Logistics costs	13	12,9%
Total costs	10	9,9%
Local RU inadequacy	8	7,9%
Social pressures country of origin	8	7,9%
Differential labor cost	6	5,9%
Country-of-origin production capacity availability	6	5,9%
Decisions without a reasoned statement	20	
% on total decisions	16,5%	

Source: own data re-elaboration Uni-CLUB MoRe Back-reshoring, 2016

The motivation of the factor made-in is the most indicated by Italian companies (42%), confirming what has already been mentioned in earlier works (Musso *et al.*, 2012).

25% of the cases, however, concern the poor level of customer service, 18% due to the quality of production, 14% as a result of the economic crisis. Reasons for return to Italy are negligible in logistics (10%) and manufacturing costs compared to what is happening globally, and particularly in the USA. This explains the high gap in terms of labor costs that characterize our country compared to those of traditional delocalisation (Uni Club More Back Reshoring, 2016).

The data, confirm, that, there are different reasons that pushed Italian companies to adopt *backshoring* strategies: not only economies of scale, studied advantages and global planning networks, production and distribution through the insertion of the companies in value global chains extended to more countries and markets, coordinated by multinational companies (Coe *et al.*, 2008; Gereffi e Fernandez-Stark, 2011), but also other forms like, to be competitive oriented on high quality, innovation, safety and *made-in*. In the end, also redundancies of personnel and the availability of unused production capability in Italy have been, at times the motivation to adopt *backshoring strategies*, especially when labor unions agreed to increase the production per hour worked (for example Natuzzi and Safilo cases, see Fratocchi *et. al*, 2015).

In Italy, a further increase of the phenomenon is due to the imitative effect of *backshoring*. When some companies, increasing the use of local suppliers, have noticed that many customers/competitors had already moved their productions back to the country of origin, or sought productions made in Italy, have re-evaluated the link with the territory of origin. Therefore, the start of backshoring flows of productions outsourced abroad had pushed several companies, specialized in certain kind of activities carried out

behalf of big Italian brands, to back-shore their production to the country of origin (Williamson, 2012).

2.5.2.1 Italian industrial districts

District production follows qualitative and quantitative standards that are relevant. For this reason Italian industrial districts have always given a significant contribution to Italian exports (Asheim, 1996).

The Italian industrial district, therefore, is a "bifacial Janus": local production and sales on an international scale. Manufacturing autarchy generates value in the products and, hence, becomes a qualifying factor for direct or indirect export on Western markets (Ferrucci, Piciotti 2017).

Since the 1990s, with the progressive enlargement of the borders of the European Union to the countries of Central and Eastern Europe, the economic and strategic horizon of the districts is radically changed. This new European area, in fact, has significant competitive advantages on the production costs (Marin, 2006; Egger and Egger, 2006; Turkish, 2007).

In this direction, several district firms have access to these new opportunities according to two different strategic settings aimed at containment of the total cost of production (Ferrucci and Varaldo 1996). The first strategy is to offshore some of the processing phases to produce certain components or workings in some Central Eastern countries. District enterprises, however, internationalize in these foreign areas according to agglomeration logics, creating territorial clusters abroad. In other words, they tend to get thicker in specific local areas, so they try to reduce individual risks and regenerate a district atmosphere, though in a foreign area (Rabellotti *et al.*, 2009; Grandinetti and Zoratti, 2003). These offshoring strategies still have obvious competitive implications on the value chain. In the industrial district, there are many capacity or specialty subcontractors who can no longer use the entire investment in production capacity that they originally had. Many of them, because of a significantly higher labor cost than those in the new European countries, suffer from a competitive outbreak.

The presence of district companies in the Southeast Asian markets continues to strengthen every two thousand years. Only recently the emergence of new factors that lead to a change in the competitive environment and which could push for a reorientation of the strategic orientation of some district businesses emerge. In particular, at least three elements that are currently characterizing both the dynamics of markets and the strategic attitude of district firms can be highlighted. District companies that have invested in these areas are called to increase their organizational effort in terms of monitoring manufacturing and distribution activities. The move of some parts or entire manufacturing chains to Southeast Asia leads to the need for new activities in the management of the international value chain: often, it is necessary to proceed to redesign products by introducing a greater standardization content. In some cases, technical staff from the district enterprise is sent to facilitate the transfer of technological know-how and to carry out the production control activities carried out in the foreign plant. In other cases, when the foreign settlement also assumes the role of a distribution platform, an intense effort is being made to coordinate manufacturing and trade activities. In all these circumstances, it is evident that the district enterprise has to strengthen its ability to monitor the quality of products, processes and components as well as distribution and logistics activities (Bontempi and Prodi, 2009; Andersen, 2008; Nassimbeni and Sartor, 2007). Finally, in addition to these individual behaviors of Italian district firms, some large banks are indirectly stimulating the return of businesses to their country of origin.

Ultimately, it is on the basis of these dynamics that several district firms are beginning to evaluate a different strategy, namely that of back-reshoring. In these terms, the industrial district can be considered and become a "new" attraction investor, of initiatives originating in the country of origin in order to exploit and at the same time regenerate a wealth of intangible resources and to acquire competing advantages that are difficult to imitate and reproducible. With regard to this aspect, the cases of different districts can be highlighted, purely by way of example. In the district of Montebelluna, for example, companies such as Aku, specialized. In the production of hiking and outdoor shoes, and Novaton S.p.A., a company formerly belonging to the Nike Group, which manufactures motorcycle boots and sports technical articles, reported part of their productions respectively from Romania and Far East, relying on the local district chain

that historically holds specialist expertise in the sportssystem (La Repubblica, July 22, 2013).

Back-reshoring strategies can reflect a diversity of motivations, and the economic consequences that emerge on the competitiveness of the individual industrial district are quite different. More specifically, considering both the motivations and the nature of the resources that the enterprise intends to acquire, back-reshoring strategies can come to three different ends. In the first case, back-reshoring can be induced by a comparative economic assessment of the various internationalization alternatives due to labor cost benefits per product unit (Leibl *et al.*, 2009; Platts and Song, 2010; Kinkel, 2012) or the possibility of access to particular industrial policy incentives set up by the national government (Tate, 2014). This is, therefore, a reactive behavior on the part of the company that evaluates its international presence strategy essentially on the basis of economic factors (increase in labor costs which makes production abroad less expensive, substantial transaction cost invariance due to the inadequacy or inefficiency of learning mechanisms and organizational costs for monitoring foreign activity).

In the case of advantages in terms of a territorially self-contained manufacturing chain, the firm may consider it appropriate to strengthen and extend that part of the product range characterized by a high intrinsic quality (Kinkel and Maloca, 2009; Kinkel, 2012). The resulting machining can therefore require not only materials but technical skills, technological equipment and tacit skills that can be easier to find in the manufacturing district than abroad. Among other things, the greater ease of face-to-face interaction among district operators enables effective transfer of know-how as well as the activation of inter-organizational design sharing and work-in-progress models. This competitive repositioning of manufacturing chains (Arlbjørn and Mikkelsen 2014; Martínez-Mora and Merino 2014) favors, among other things, the realization, especially in the fashion sectors, of quick-response strategies to the needs of retail businesses, showing a the most effective level in responding to the sudden and pressing demands and changes in market demand (Chiarvesio and Di Maria, 2006). It is evident in these circumstances that the company's strategic will to look for resources of a relational nature (chain relationships, customer-supplier relations, etc.) and the role that district contexts assume as areas in which such relational capital is historically sediment and accumulated.

It is in these terms, therefore, that the industrial district can be considered and become a "new" investor attraction.

Finally, in the case of benefits in terms of intangible assets attributable to the territory where the enterprise is located, district firms may decide to return to their country of origin because they believe there is a positive country of origin effect and, in that logic, there is added value for their products (Usunier, 2006; Laroche *et al.*, 2005). In this perspective, it is considered that the territory manages to express intangible and intangible values that can be transferred to the products and can therefore be exploited through appropriate back-reshoring strategies. It is, therefore, not only a problem of intrinsic quality of the product realized, objective made possible with the other option of back-reshoring based on the centrality of the domestic manufacturing chain, but rather intangible values that become an integral part of the extrinsic quality of the product, thanks to territorial context with cultural, artistic, historical and landscape values. This value is transferred and comes directly to the ultimate consumer, who increasingly belongs to the wealthy class of some foreign countries, has the expectation and demands that the Made in Italy product incorporates these intangible values from the territory. Back-reshoring therefore becomes an essential component for a recovery in the economy.

2.6 Industrial policies for backshoring

2.6.1 An overview at international level

UNCTAD (2013) has recognized the importance of the *backshoring* and *near-shoring phenomena*, as well as the implications towards the persons in charge for national policies²⁸. The recent literature shows how one of the main reasons that facilitate *backshoring* is represented by the available subsidies put at the disposal of national

²⁸ The analysis of FDI flows in the industrialized countries focus two trends: 1) less outsourcing choices; 2) increase of divestments in the developing countries, that causes the backshoring of companies to the countries of origin. Despite the data regarding divestments are limited to only some countries (United States, United Kingdom, Italy, France, Germany and Japan), the evidence demonstrates that it is about a significant dynamic and increasing tendency (UNCTAD, 2013, p. 26).

governments²⁹. Consequently, the *backshoring* phenomenon could have a crucial role in industrial policies, which as well could try to overcome the economic crisis. In the light of the recent crisis, the USA, France and the United Kingdom have arranged several kinds of support in favor of national industrial companies and specific policies for the economic re-industrialization and *backshoring promotion* (Fratocchi *et al.*, 2014).

Taking into consideration the analysis of the USA industrial policy, which is the most advanced in supporting backshoring, and the relationship with backshoring, it comes to light how, a target policy proposed, which consists in guaranteeing an active support in the manufacturing sector through subsidies to companies (tax breaks, subsidies, etc.) (Fratocchi *et al.*, 2014).

For example, the United States have facilitated the promotion of “*made in the USA*” and have reduced significantly the gas price for domestic use (*shale gas*), and for some companies working in industrial sectors at high energy consumption – such as steel and fertilizer – that are backshoring (Needham, 2014). Also in the United States, some plans to promote backshoring have been arranged both for big and small medium-sized companies, in order to attract manufacturing backshoring investments and bring some remarkable advantages in terms of occupation (Fratocchi *et al.*, 2014). In 2014 the Obama Administration, together with the *Advance Manufacturing Partnership Steering Committee*, launched three initiatives in order to support all those technologies considered essential for competitiveness in the United States economy. The first initiative provides an investment of 300 million dollars to allow companies to test innovative materials and products directly in laboratories located in big structures of American research (*Nasa, National Science Foundation*) to remaining in the country of origin. The second initiative provides a total of 100 million dollars for the best qualification and re-qualification manpower programs. The third initiative provides 130 million distributed among ten States in order to allow small-sized companies to adopt new technologies and build new systems over a period of 5 years. The active American government policy is supported, not only by empirical evidence (Boston Consulting Group, 2014; The Manufacturing Institute and Deloitte, 2015), from which it comes to light an increasing

²⁹ Such as tax benefits to investments for technology innovation, support of the workforce or support to exportations (Fratocchiet *al.*, 2014).

interest from companies to adopt *backshoring* strategies, as well as by *backshoring* concrete cases: Apple, Google, Element Electronics, General Electric and Master Lock³⁰ to quote some of them. In addition to the Federal Government action, the local government subsidies that arranged to facilitate *backshoring* have been crucial. A systematic approach to re-launch an efficient and coherent industrial policy has been followed. Instead of a competitiveness based on a low labor cost, a policy oriented to pursue competitive advantages over a long period has been followed. In conclusion, the *policies* proposed by the United States are based on complementary strategies: on one side, subsidies and tax relief, allow, in the short term, companies to adopt *backshoring* strategies; on the other, the development of technical partnerships and the development of synergies in terms of innovation, in the long term, can guarantee the persistence of local advantages and consolidate the territorial companies. (Fratocchi *et al.*, 2014).

Analyzing the relationship between European industrial policy and *backshoring*, it emerges that the EU have not carried out yet, any strategies of *policies* coherent with those adopted by the United States. Recent studies (PricewaterhouseCoopers, 2015; “Centro Europa Ricerche”, 2015; Fratocchi *et al.*, 2014) confirm that the tendency to *backshoring* could be speeded up, if the EU would adopt some reforms focused on innovation and a higher competitiveness. For example, “Strategy Europa 2020”, through specific policies to repatriate, has a goal to increase up to 20% of the percentage of the European GNP relating to the industrial sector. However, the guidelines have not been actualized in industrial policies, causing several negative *trends* that characterized the current data regarding the European manufacturing sector. Recently, the European social and economic committee has approved a series of advice for the European Commission, regarding strategies to adopt in order to support the EU re-industrialization and *backshoring*. In particular, at national level, the attention is focused on the development of a tax system able to promote internal consumptions and to attract international investments, on the development of new industrial *cluster* and the support of the external

³⁰ Google, in 2012, announced to produce again in the United States “Nexus Q”, a music and video device; Apple has revealed that, since 2013, the production of one of the existent *Mac* line would have exclusively been produced in the United States. The Same cases are represented not only by other industrial giants such as *Ford*, *Caterpillar*, *American Express* and *Dell*, but as well as by a multitude of small and medium sized companies that works in different industrial sectors (Fratocchi *et al.*, 2014).

ones, as well as the arrangement of information centers capable to support *backshoring* procedures for national companies (Iozia e Leirião, 2014).

Summarizing the *policies* adopted by the United Kingdom, France, Germany and Italy it is possible to note that each State has adopted different *policies*, mainly focused on the manufacturing sector³¹.

In January 2014 the United Kingdom applied for *pro-backshoring*, activating the *Manufacturing Advisory Service* that put together the factors that push to repatriate British companies, that previously outsourced their activities, to factors that facilitate the foreign investments. This was strengthened by the British government which worked in order to create a favorable context through: the reduction of energy costs, higher flexibility on the labor market, legislative simplifications and tax reforms (UniClub More Back-reshoring Research Group, 2014) as backshoring has been identified as a key opportunity to rebalance the UK economy (De Backer *et al.*, 2016).. According to a recent study carried out by Pricewaterhouse Coopers(2014), if the tendency to *backshoring* continues, in Great Britain between 100 thousand and 200 thousand positions in the manufacturing sectors would be created with an increase in the GNP of between 6 and 12 billion pounds over the next decade.

France, since 2013, has given to the “*Agence Francaise des Investissements*” (AFI) the management of the policies to push French companies, that have outsourced, to back-shore, making available a self-assessment *software* in order to give the companies a chance to better evaluate the conditions to adopt for *backshoring* strategies. Furthermore, after this self assessment, a single representative of the public administration has been identified in order to turn to for any aspect related to any phase of the *backshoring* to the country of origin. Moreover, France has developed a voluntary mark, *Origine France Garantie*, to guarantee the quality of French products (UniClub More Back-reshoring Research Group, 2014).

In Germany, *backshoring* has interested between 400 and 700 companies in the last fifteen years (Kinkel, 2014). In that case the “back-shore” is indirectly supported by policies that increase the local advantages and give competitive advantages for the entire

³¹ For an overview regarding different approaches of industrial policy followed by the main European countries and the lack of the interventions on production activity in Italy, see Cappellani *et al.* (2013) and Giannola *et al.* (2015).

system; this was made possible by maintaining dynamic and innovative, highly specialized innovations in the manufacturing sector. To this purpose two strategies have been approved: *Germany as a competitive industrial nation* and *High-tech strategy for Germany* that aim to support competitiveness and company innovation, increasing competences and the level of qualification of the labor force as well as support the interaction between the manufacturing and tertiary sector.

2.6.2 The backshoring initiatives in Italy

In Italy, up to date, to facilitate *backshoring* phenomenon little has been done. The important trade associations, in particular in the sectors of fashion and footwear, have been asking for a long time to put into effect the planned tax reforms, regarding IRAP and hiring in order to facilitate the *backshoring*. One of the main reasons of *backshoring* for Italian companies is the *made in Italy*. In this regard, it has been recognized as a central role to consumers and international markets because of an increasing demand of productions completely *made-in Italy* (Musso *et al.*, 2012). The necessity of more attention to customers' needs has, pushed companies to reconfigure their *supply chain* (Baldassarre *et al.*, 2014) on an international scale, also because of the pressure caused by the crisis. Italian companies that have adopted *backshoring* strategies mainly connected to the added value of *made in Italy*, require, also, an improved legislation regarding the certification of the origin of the productions, that could guarantee a greater protection of the *made in Italy*.

Recently some initiatives have been promoted in order to support Italian companies that want to pursue a *backshoring* strategy. In this regard it is interesting to analyze the "Project *reshoring*", which came about from the collaboration between "Sistema Moda Italia" (SMI) and PwC Advisory, that it is oriented to create the necessary conditions to back-shore the productions and to increase the productivity in two pilot areas, Veneto and Apulia. The project aims to promote assistance to companies, re-qualification and education through an Academy but also to collect acceptances by those

companies, and mainly by PMI, that intend to carry out *backshoring*³². SMI has created new contacts with the manufacturing companies and it controls the state of the project in order to expand it to other Regions. The district of the production chain relative to Veneto has been chosen for several companies present both upstream and downstream of the sector: the production chain is made up of clothing companies, textile, third party companies, machinery and material suppliers, service suppliers, wholesalers and distributors as well as intangible services. Apulia, represents, instead, the first southern region in textile-clothing, both for the number of active companies and for the number of employees (footwear in the North of Bari, Clothing in Bari, Hosiery and Clothing in Salento, footwear of Casarano) that boast handcrafted excellence. The Apulia Fashion District, has been affected by the recent economic negative phase, that has caused a great weakening and it aims, through “Project *reshoring*”, to contribute to backshore production in Apulia and activate a virtuous circle in order to expand the project to other regions. The “Project *reshoring*” will work by educational interventions and re-qualification of personnel, supporting investments regarding R&S in order to give a concrete result to reach the recovery of the territory. Another example of initiatives to facilitate *backshoring* is represented by “Laboratorio Moda Molise”³³, that aims to give value and guarantee scientific, professional, and manufacturing competences of the *made in Italy* sector through instruments and policies of traceability and certification, as well as to promote company cooperation by means of contact and collaboration also with national and international authorities. The Region of Molise has also signed a protocol of partnership with “Missardi L.t.d”, a company *leader* in the fashion industry, in order to re-launch the sector with *made in Italy creations*.

Moreover, it is interesting the strategy adopted by “Natuzzi”. This company in 2013 signed an agreement, defined as “historical”, at the Ministry of Economical Development with the Government and the Regions of Apulia and Basilicata, that aims to create new opportunities for all the territory in terms of competitiveness, in particular regarding the area between the provinces of Bari, Taranto and Matera. The main points

³² According to the observatory PwC, 76% of controlled companies have modified, or have the intention to do so, the suppliers in the last ten years, in the majority of the cases, less than 25% of the production is carried out in Italy.

³³ Laboratorio Molise, promoted by EURIDIT, with the Province of Isernia and the Municipality of Pettoranello.

of the agreement are: investments for more than 200 million euro; re-qualification of a large part of the personnel; the creation of two *new companies, by order of the* “Natuzzi Group”, that thanks to the back-shore of productions to Italy, previously outsourced in Romania, can carry out, the first line of sofas currently produced in Romania (500 employees in 2014 that will increase up to 700 in 2018), the other, furniture components (150 employees). The creation of new activities, which are favored by the resources (101 million of euro) allocated by the Agreement, aims to reuse around 220 employees, facilitating voluntary labor mobility for 600 employees, blocking more than 1.700 redundancies. In this way the attempt is to create a sort of contrary delocalization, from Romania: this is something very new that represents the peculiarity of the Agreement and it opens new interesting possibilities for the Italian economy. “Natuzzi” represents an important example for other companies: it is possible to divert the work flow brought abroad, coming back to Italy, and also returning to Italy those productions with a high rate of work.

In addition to *made-in*, also the factor *time-to-market* is becoming more determinant for Italian companies that decide to adopt *backshoring* strategies: to promptly answer consumers requests is a successful key factor and those companies which can make it have an enormous advantage on their competitors. Therefore, it is necessary, to move at least part of the production close to faster production cycles in order to keep in pace with other markets (Andreetta, 2015).

In the light of the present examples, we can conclude that *backshoring* can represent a great opportunity to develop the economy of Southern Italy.

2.7 Conclusions

The analysis presented in this current work starts from literature in itself uncompleted. The *backshoring* phenomenon has been identified in a wider theoretical context, to which we can refer other terms already present in literature (de-internationalization, foreign divestments, *in-shore*, *relocation*, etc.) that not always can be referred to this phenomenon but they contribute to identify a *backshoring definition*, as well as how it came about and its peculiarities.

For all these several implications, it is possible to look at *backshoring* as a process destined to increase in the future (Couto *et al.*, 2008).). The question of some scholars is if up to date we can actually talk about a substitution of *offshoring* with *backshoring*. Recent studies demonstrate that, actually, we cannot talk about a substitution, but rather of an increasing in the heterogeneity of company behaviours, depending on the strategic variables restudied in the light of the economic changes such as the crisis that is one of the main factors (Mariotti, 2009).

The increasing attention on *backshoring* phenomenon by the scientific community and *policy makers* will involve a revision of traditional *business* models both for *policy* implications, and for managerial strategies to adopt and this represents an occasion to rethink on the sector and on the sustainability and in order to re-qualify Italian productions.

Recent studies from the United States (among others, Reshoring Initiative, 2014)³⁴ demonstrate that *backshoring* strategies, supported by the right industrial policies, can cause positive relapse: higher occupation and attraction for foreign direct investments. However, to date, European *policy* strategies are still fragmented and are up to the initiative of the single States. European states, in particular, must provide combined strategies, such as tax relief and subsidies, in order to contribute to the territories in making them more productive attractive.

Focusing our attention on Italy, it comes to light that a higher coordination between national Government, Regional government and the private sector to promote *made in Italy is necessary*, offering: efficient infrastructures; location opportunities; employees and competences; subsidies and tax reliefs. From the present analysis in the previous pages it is evident that if in Italy there were better conditions, a high percentage of companies would be available to back-shore the production to Italy (Research Group UniClub More Back Reshoring, 2014). Backshoring could represent a great opportunity of development for the South of Italy in terms of investments and innovative services by foreign and national investors.

³⁴ Reshoring Initiative, a company from the States that deals to constantly control the phenomenon, has recorded 357 cases of companies from the states that, since 1997 to 2014, have repatriated their productions or part of them previously outsourced. These companies have created 39.530 jobs. It concerns, mainly, companies that produce products with a small medium technology: upper medium (97 companies equal to 27%); low (73 companies equal to 20%); high (68 companies equal to 19%).

Although in the last few years *backshoring* has obtained relevance for its diffusion at global level, it has not yet been sufficiently studied, it is a phenomenon to be better analyzed in terms of the impact that it could have on economic recovery.

Beyond the reasons and the terminology differences that characterize backshoring, however, it seems appropriate to point out that these are complex processes where the reasons appear only as one of the elements to be analyzed for a complete view. If we consider that backshoring operations are taking place from different countries, through different modes, at different times, it's interesting to see if there are regularities between the various operations and to which variables.

Distance, in fact, qualifies as an organizational key, respectively as proxy for the risk of loss of skills and for the coordination and control costs associated with the management of delocalized activities. In particular, it emerges that the psychic distance, as well as the geographical and cultural, influence the decision of backshoring even if managers still have a low perception of those factors that disturb the flow of information between the company and the target market are not only geographic and cultural factors.

The next chapter proposes to verify whether the concept of psychic distance takes on the repatriation processes of Italian companies' formerly delocalized production abroad. In particular, the aim is to check whether there is a relationship between the last of the offshoring strategy (the time between the choice of offshoring and backshoring) and the psychic distance (between the home country and the foreign country where the company invested).

CHAPTER 3. THE CULTURAL AND PSYCHIC DISTANCE IN BACKSHORING DECISIONS OF ITALIAN COMPANIES: A CLUSTERING APPROACH

Abstract

The topics discussed in the previous chapter helped to identify a theoretical model used for the study of backshoring which has the potential to give new insights on the topic. This model is the Schult model. This model seems indicated to the study of backshoring because it analyzes the hidden costs of a company and distinguishes them in a model that starts from the difference between direct and indirect costs of a project of productive delocalization. Then, it classifies the hidden costs according to their various nature, putting the attention on the question that costs are not always calculated correctly.

The exclusion of these factors from the calculation of the total costs of a productive transfer program can lead companies, at a later stage, to make decisions that challenge the choices previously made. In fact, many companies of companies that relocate production, because they have erroneously calculated the actual benefits that can be achieved by relocation. The total cost incurred by companies abroad, therefore, is composed of a series of factors, not all quantifiable, which however must be considered so that the choice made is not less convenient than one might think in the planning phase. Nevertheless, one of the reasons behind the backshoring is precisely this, linked to the existence of hidden costs, whose prediction is not always easily assessed.

The original contribution of this work is the study of backshoring through the Schulte model: the psychic distance (in terms of religion and in terms of language) must be considered among the hidden costs.

This work, through an exploratory analysis of 59 backshoring operations in Italy, shows that the time elapsed between the choice of offshoring and backshoring, and the distance (cultural and psychic) between the source country and the foreign country from which the re-entry takes place are two significant variables to explain the variety of cases. Distance represents an organizational key, respectively as a proxy for the risk of missing

or insufficient computation of hidden costs associated with the management of delocalized activities.

In particular, it emerges that the psychic distance, as well as the geographical and cultural distance, influences the decision of backshoring even if managers still have a low perception of those factors at a geographical but also cultural level that disturb flows of information between the company and the target market.

Introduction

In Italy, the press has focused heavily on backshoring only in the last years, giving a resonance to the results of the research group *UniCLUB-MoRe Back-reshoring Research group* (Fratocchi *et al.*, 2014; Zanoni, 2016). The cases of Italian companies documented by the group are 121 and they are related to 88 companies. Many of the cases concern the clothing and footwear sector, and involve companies such as Tod's, Prada, and Ferragamo, but also smaller companies such as Nannini, Masters, Piquadro, And Camicie, Aku, and others. Except in special cases, in the fashion industry that drives companies to return to Italy, according to the UniCLUB-MoRe there is a problem of quality and recognition of the "Made in Italy" brand. In China or Romania it is easy to produce at low cost, but it is not easy to produce with quality and at the same time be fast and flexible, especially in a very dynamic sector subject to frequent changes in the product.

However, the cases of companies that repatriate the production in Italy also occur in sectors other than clothing. Even in these sectors, the main destination countries are China and Eastern Europe, while the main reasons that pushed towards the back-reshoring are the lower ability to control quality abroad, the need to be close to the processes of R & D located in Italy, the high costs of logistics and in general a total cost of production that over time has become higher abroad than in Italy (ANIE, 2014).

This work focuses on the topic of backshoring that indicates the geographic relocation of a functional, value creating operation from a location abroad back to the domestic country of the company (Holz, 2009). Different from reshoring that, instead,

means a strategic decision regarding the place where to move the production (Fratocchi *et al.*, 2014).

Compared to exports, these forms of internationalization are more stable and durable and require greater financial involvement and, as a consequence, require a closer interaction between economic actors belonging to different countries. For this reason it seems justified to think that if the objective factors of the psychic distance (linguistic and religious differences within and between countries) affect the commercial fluxes and those of investment, then, with good probability, they will have an even more significant impact on the offshoring and consequently on the backshoring. It is believed that this hypothesis is reasonable based on the fact that some factors underlying psychic distance, such as religion and language, directly affect the internationalization of the company in whatever form it manifests (Dow and Karunaratna, 2006). In evaluating an offshoring project, managers often take into consideration the possible costs that would be transferred to a foreign country rather than another, and compare them with domestic ones, thus determining any savings. In this process, the error that is often committed, however, is to make a calculation only on the basis of the most visible and tangible cost entities, and therefore neglect all those elements that indirectly affect business spending. Schulte's model seems indicated to the study of backshoring because it analyzes the hidden costs of a company and distinguishes them in a model that starts from the difference between direct and indirect costs of a project of offshoring. In its original version, Schulte's model considers only cultural distance among the hidden costs, neglecting the psychic distance.

The chapter will then proceed with an introduction on the theoretical and historical origin of cultural and psychic distance and then on the Schult model. It continues with an analysis of the most relevant contributions to the application and conclude with the presentation of how a specific model employed in the theory can be adapted to examine backshoring processes. Later the results of a research carried out in order to better understand the phenomenon of backshoring as it manifests itself in Italy will be illustred and analysed. This research consists in a collection and study of backshoring data for many Italian companies, which led to the identification of two clusters/models that describe the phenomenon. The objectives that guided the research

work, the type of data collected, the methodology applied for the analysis, and the results obtained will therefore be illustrated in the following paragraphs. At the end of the chapter the academic value and the limits of this research will be explained, and proposals will be made for future improvements.

3.1 The cultural and psychic distance in internationalization strategies

The concept of distance has played an undeniably important role in international commercial research in recent decades. Indeed, in a recent comment, Zaheer *et al.* (2014, p. 55) came to affirm that "essentially international management is distance management". Only in 2012, 176 articles published in eight major international journals (IB) include some forms of distance in their discussions or analyses.

Yet, while the amount of attention paid to the construction of the distance continues to grow, even the amount of criticism has increased. Beginning with the seminal article by Shenkar (2001), commentators such as Harzing (2003), Tung (2009), Tung and Verbeke (2010), Zaheer *et al.* (2012), Beugelsdijk and Mudambi (2013), and Ambos and Håkanson (2014) have repeatedly criticized the way in which researchers have conceptualized and implemented various forms of distance.

Often psychic distance and cultural distance are described as synonyms, but many studies such as Sousa and Bradley (2006) and Dow and Karunaratna (2006) identify in the first an influence at the individual level, while in the second an ascendant at the level of the country.

The concept of psychic distance is in fact constituted by the term "distance", which depends on how the world is perceived, and the term "psychic" that derives from the Greek Ψυχή (mind, soul) and refers to an extremely intimate and subjective part of the individual.

The cultural distance is instead associated with a collective or country level where culture means «that human and social environment created by man for the man himself: the union of knowledge, beliefs, art, morals, laws, customs and other potentials and habits acquired by men as members of a society. So the markets - which are one of the many

forms of social activity that man has invented for himself - can not but be pervaded, deep down» (Cateora and Graham, 2007, p.80).

The psychic distance (differences in culture, language, business practices, legal and political systems) between home and host country can lead managers to underestimate the costs of implementing offshoring decisions, thus increasing the likelihood of returning to their source country (Ancarani *et al.*, 2015). From a supply chain perspective, the potential for chain disruption, delivery times, long response times to replace poor quality products and a loss of flexibility and agility have also contributed to the decisions taken by companies to rethink their strategy supply and repatriate production (Gray *et al.*, 2013). As a result, the game was considered as a pure consequence of learning and correcting previous poorly weighted offshoring decisions (Kinkel and Maloca 2009; Kinkel 2012, 2014).

Research on the role and impact of distance on international management decisions has spanned many cycles in the last half century. The most obvious starting point is the role that geographic distance has played in the classic gravity models used to predict patterns of trade flows around the world (Linnemann, 1966). Indeed Anderson (1979) describes the gravitational model - with the geographical distance as a key predictive variable - as "probably the most successful empirical device of the last twenty-five years".

In the mid-1970s, thanks to the incorporation of the psychic distance of Johanson and Vahlne (1977) into their model of internationalization, there was a dramatic shift in attention from the geographical distance to the use of the term "distance" as metaphor for national differences. In particular, this approach has accelerated with the creation of Kogut and Singh (1988) of a "national cultural distance" index using the four dimensions of Hofstede culture (1980). In fact, at the beginning of the 2000s, the index of Kogut and Singh was undoubtedly the measure of rigor of distance in empirical research IB (Harzing, 2003), and its use has continued to gain popularity (Leung and Morris, 2015 ; Venaik and Midgley, 2015).

3.1.1 The psychic distance

The psychic distance is made up of all those factors such as differences in language, culture, and the political system; everything that disturbs the information flow between the company and the market (Johanson and Vahlne, 1977). Johanson and Wiedersheim-Paul (1975), Boyacigiller (1990), Evans *et al.* (2000) include in this sum of factors differences in language, culture, political systems, level of education, degree of industrial development, religion, marketing infrastructures. It follows, consequently, that the greater the psychic distance, the greater will be the liability of foreignness (Johanson and Vahlne, 2009). The liability of foreignness is the baggage of difficulties that the company is forced to face having to settle in a country different from that in which it was born or of which the entrepreneurs are part. The liability of foreignness is defined as the set of foreign management costs associated with the position of a company operating in a market which leads to a competitive disadvantage due to additional costs that would not exist for a local company (Zaheer, 1995).

Psychic distance is a fascinating concept that has a central role in international management research. It expresses the differences between foreign nations and their people, and measures the perception of these differences (Sousa and Bradley, 2006, Håkanson and Ambos, 2010).

It is an ambiguous notion that has attracted increasing attention in recent years (Dow and Karunaratna, 2006; Liu, Chai and Nebus, 2013). Despite the great interest aroused by international literature in recent decades, the concept still has great gaps and unexplored potential.

Over the years, empirical studies on internationalization decisions have shown that companies are more likely to enter and compete in psychically more similar markets (Drogendijk and Blomkvist 2013; Dow 2000). Recently, Håkanson and Dow (2012) examined nearly 50 years (1962-2008) of international trade history and found that, although the effect of psychic distance is slowly diminishing, there is still a significant negative relationship between distance psychic and international trade.

The nearest markets have more characteristics in common with the domestic market, reducing and exploiting the skills of the source country more easily (Gomes and

Ramaswamy 1999). Two theories have been widely used to study these aspects of the company: transaction cost theory (Dunning, 1981; Rugman, 1981; Williamson, 1975, 1985) and Uppsala's internationalization model (Johanson and Vahlne, 1977; Johanson and Wiedersheim-Paul, 1975; Luostarinen, 1979). The proponents of the internationalization model describe it as a model of the stability chain as regards the choice of forms of entry modalities and as a model for the selection of foreign markets (Johanson and Wiedersheim-Paul, 1975). The concept of psychic distance was mainly associated with the latter, providing for the temporal order in which foreign markets are selected for entry. The potential recipient countries of investments should be similar to the source country of the company, involving a few unknown conditions and reducing the learning effort related to the phase of internationalization (Johanson and Vahlne, 1977).

Initially in studies of international economics, distance represented only a proxy of transport costs. The distance between the two countries involved in bilateral trade was essentially geographic and was used as a variable in the gravity models used to study trade flows. Subsequently the meaning of distance has become a multidimensional construct whose geography is only one of its dimensions. In investment decisions and therefore also in localization, however, cultural and psychological variables, like transport costs, could guide the company to select the destination market (Beckerman, 1956, Johanson and Vahlne, 1977).

In the realm of international business, the related constructs of psychic distance (Johanson and Wiedersheim-Paul, 1975) and national cultural distance (Kogut and Singh, 1988), along with other forms of national differences such as institutional distance (Xu and Shenkar, 2002) and the socio-cultural one (Agarwal, 1994), have been cited as potential predictors variables for a wide range of management decisions, such as the decision to start exporting (Gripsrud, 1990), export market selection (Ellis, 2008), foreign direct investment (FDI), entry mode (Kogut and Singh, 1988; Slangen and Hennart, 2008), problems management of human resources (for example, Boyacigiller, 1990). However, despite this wide range of applications, substantial differences of opinion remain with regard to the best way to conceptualize, and to make operational, the distance constructs (Brewer, 2007; Dow and Karunaratna, 2006; Evans and Mavondo, 2002; Håkanson and Ambos, 2010; Sousa and Bradley, 2006).

Beckerman (1956) introduced the concept of psychic distance as a "subjective" element that moderated the role of "objective" economic distance. The so-called Uppsala school (Johanson and Vahlne, 1977; Vahlne and Wiedersheim-Paul, 1973) defines the psychic distance as "factors that prevent or disturb the flow of information between potential and true suppliers and customers" (Vahlne and Wiedersheim-Paul, 1973). In particular Johanson (1977) defined it as: "... the sum of factors that prevent the flow of information to and from the market, examples are linguistic, educational, commercial, cultural and industrial differences". To these factors Boyacigiller (1990) adds the dominant religion, the business language, the form of government, economic development and the level of emigration. Nordström and Vahlne (1994) redefine the psychic distance as "factors that prevent or disturb business learning and the understanding of a foreign environment". As a result, companies enter countries that are more strictly psychic because of the ease of learning of these countries (Kogut and Singh, 1988; Odorici e Presutti, 2013).

Later the psychic distance was defined as the degree of insecurity that the enterprise has of an international market due to cultural differences and other business difficulties that represent barriers to learning about the market and how to operate on it (O'Grady and Lane, 1996) or as a combination of factors at a national, organizational and individual level.

The psychic distance is not reduced to a mere cultural dimension, but contains everything that hinders and prevents the linear flow of information between the company and the market; therefore as Dow and Karunaratna (2006), Dow and Ferencikova (2010) and Håkanson and Ambos (2010) assert, cultural distance is only one component of the psychic distance. The national level is linked to cultural affinity so the psychic distance can be seen as an aspect of cultural distance (Swift, 1999).

The psychic distance, interpreted in terms of cultural distance and business distance, implies that cultural distance is measured through the Hofstede model (1994) and the business distance refers mainly to distance in terms of political / legal aspects, competitive structure, economy level, business practices, language (Evans and Mavondo, 2002).

Dow and Karunaratna (2006) clearly state that "psychic distance is one of the most commonly cited, but constantly measured constructs in the field of international business research". Dow and Karunaratna (2006) and Håkanson and Ambos (2010) offer in-depth analysis of different variables that the studies used to calculate the psychic distance. Furthermore, Dow and Karunaratna (2006) even propose "the separation of the psychic distance in a sequence of correlated constructs", which they call *distance stimuli*. These macro level factors have been proposed by researchers such as Evans, Treagold and Mavondo (2000) and Johanson and Vahlne (1977). The methodology under discussion considers 5 series of differences: language, religion, industrial development, educational system and political system (Shenkar, 2001). The latter is further divided into two sub-factors, namely differences in the degree of democracy and political ideology. Each of the five groups of factors is the result of a linear combination of different variables (23 in total), calculated for each dyad of 120 countries.

Given the objectives of the study, for each of the nine dyads of the country (with Italy always considered the first country because it is the host country of the investigated companies), Dow and Karunaratna (2006) first found the specific value of each of the five factors (calculating a simple average of the two sub-groups related to political systems) and calculated the average value. Finally, they used absolute values as measures of the distance between each pair of countries.

The formalization of risk summarizes the concept of psychic distance. The various authors and their theories associate a lower psychic distance with an exchange of information that is far more transparent and trustful between business and foreign environments closer to it and family. In these cases, in fact, the management decides to face uncertainty (because perceived as inferior) focusing its choice on the predisposition and accessibility of communication and on the similarity between economic and cultural backgrounds. The literature on internationalization uses this concept to direct the expansion: initially it moves towards the nearest foreign countries, then gradually move to the most distant countries.

Specifically analyzing the theory of the Uppasala model and the approach of Dow and Karunaratna (2006) there are common elements like the multidimensional concept of psychic distance, the correlation between it and the work of management and the focal

influence exercised by the knowledge of the environment in which it is decided to enter. Johanson and Vahlne (1977) prefer gradual learning for successive and incremental steps, while Dow and Karunaratna (2006) theorize the presence of objective forces (macroeconomic aspects) and subjective traits of the decision maker. Objective stimuli regarding the circumstances of the environment (culture, economic condition, institutions, religion, language) are assessed by the conscience of the decision-maker who analyzes expectations by taking into account his past experiences, age and degree of education.

It is therefore understood that the concept of psychic distance does not have a definition recognized by the whole theoretical world, consequently there are no universally accepted and recognized measurements or analyzes.

Another problem inherent in the concept of psychic distance is its similarity with the concept of cultural distance or its ability to incorporate it. The psychic distance and the cultural distance were used to explain the sequence of foreign investments (Benito and Gripsrud, 1992), the modalities of insertion and the degree of adaptation of the international marketing strategy (Leonidou and Katsikeas, 1996), the control of export channels (Bello and Gilliland, 1997) and company performance (Evans and Mavondo 2002).

These cultural inequalities amplify the perception of risk because unclear behaviours increase and it is more complex to seize opportunities.

In terms of the chosen dimensions of distance and diversity, the linguistic and religious differences within and between countries are particularly relevant. Despite the rapid recognition of the importance of linguistic and religious differences in international affairs (for example, Beckerman, 1956, Ronen and Shenkar, 1985, Boyacigiller, 1990), these two dimensions of distance began to be considered only recently in the literature of international empirical studies as potential determinants of managerial decisions and constant behaviours (Dow and Karunaratna, 2006; Berry *et al.*, 2010; Luiz, 2015; Castellani *et al.*, 2013). Of particular relevance is the fact that there are also substantial differences between countries in the amount of heterogeneity within the country on these two dimensions, which makes them very suitable for studying the effects of diversity within the country. For example, in terms of language, Japan is very homogeneous, while

countries like India and Switzerland with their many (official) languages have much higher levels of linguistic diversity. Likewise, some countries like Iran are very homogeneous in terms of religion, while other countries like the United States and Singapore are much more different.

The language is specifically mentioned as an important form of distance both in the original work that coined the term psychic distance (Beckerman, 1956) both in the seminal work of Johanson and Vahlne (1977), and received attention in a number of recent studies and a special issue of the *Journal of International Business Studies* (e.g. Slangen, 2011; Brannen *et al.*, 2014; Cuypers, Ertug, and Hennart, 2015). Religion is a less studied distance factor, but is proposed and / or employed by a growing number of researchers including Shenkar (2001) and others (e.g., Berry *et al.*, 2010; Boyacigiller, 1990; Castellani *et al.* , 2013; Dow and Karunaratna, 2006; Ghemawat, 2001; Luiz, 2015). Indeed, Gomez-Mejia *et al.* (1997) argue that "alongside the language, religion is probably the most distinctive cultural feature", and include both language and religion as predictive variables. These two specific distance dimensions relate to the fact that distance between countries will only affect managerial decisions if managers are aware of such differences when making decisions. In this sense, the differences in language and religion are undoubtedly among the most visible and salient of the various factors of distance. Even managers with minimal international experience will be immediately aware of any linguistic differences from the beginning of the acquisition process. While differences in religion may not be immediately apparent as differences in language, awareness of religious differences often becomes apparent immediately after interaction with someone from another religion. In contrast, many of the more subtle cultural differences, which make up the most commonly used national cultural distance index (Kogut and Singh, 1988), can initially be overlooked and become apparent only later, during the acquisition process. Thus, differences in language and religion can have a stronger impact on managerial decisions simply because of the increased awareness of such factors at the time such decisions are made (Slangen, 2011). The final benefit of focusing on languages and religions is that they are more fully documented and therefore it is possible to more easily calculate diversity measures within the country.

A potential way in which linguistic and / or religious diversity within the country can influence cross-border acquisitions is a simple direct effect parallel to the impact of linguistic and religious distance. Just as the big differences between countries increase the difficulty of communicating and understanding people in another country, the presence of multiple languages and / or religions in the destination country can also negatively impact such information gathering efforts. When a company needs to learn how to deal with a new language or religion, it is not insurmountable, but it is expensive in terms of management time and the risk of misunderstandings and errors increases. Learning how to deal with multiple languages and / or religions all at the same time will increase the difficulty of management.

Dow and Karunaratna (2006) argue that the linguistic and religious diversity in the source country of the target has a similar effect to that of distance. A greater diversity will lead a foreign buyer to invest less. Finally, they argue that diversity in the buyer's home country makes the buyer more aware and sensitive to the challenges associated with higher levels of distance between their country and the target country, as well as the challenges associated with greater diversity in nation goal. As a result, they have shown that the level of linguistic and religious diversity in the buyer's home country changes the respective effects of distance and diversity in the destination country. The study was tested on a sample of 59,092 cross-border acquisitions in 67 purchasing countries and 69 target countries. Dow and Karunaratna (2006) aim to make a relatively unique contribution by exploring and theorising the impact that diversity within the country can have on international management decisions.

It is evident how the two distinct roles that diversity could play, and by doing so, could be adapted and introduced into the debate on backshoring, where the social psychological concept of "cognitive complexity" has never been discussed.

3.1.2 The cultural distance

The impact of culture on international business has long interested scholars (for example, Gales, 2008; Stringfellow *et al.*, 2007; Hahn and Bunyaratavej, 2009). One of

the most important research frameworks in this field is that of Hofstede (1980, 1996, 2001).

Geert Hofstede (1994) defines culture as «*a set of collective mental schemes that distinguish the members of one category of people from another*». Hofstede investigated, from 1967 to 1973, the behavior of about 100,000 people who worked for IBM in about 70 countries and discovered four dimensions that illustrate the cultures that distinguish the various countries (a subsequent study allowed the insertion of a fifth variable) . The variables explored are: distance from power (power distance), individualism - collectivism (individualism versus collectivism), masculinity - femininity (masculinity versus femininity), aversion to risk (uncertainty avoidance), orientation towards the future (long term orientation)³⁵.

He developed global culture measures in terms of four primary factors, summarized by Kirkman, Lowe, and Gibson (2006). The authors have long noted that the similarities in culture between a host country and the source country provide many benefits to a company. In a more similar culture, businesses will likely be able to reduce transaction costs that could arise from training and information acquisition and reducing the costs of overseas investment (Hahn and Bunyaratavej, 2009).

³⁵ The index of distance from power: indicates the extent to which subjects accept hierarchies and inequalities in the distribution of power. Companies with a high rate of PDI (power distance index) are organized in rigid and highly structured forms; where the indicator appears to be less than the origin of power appears to be knowledge and respect, in fact in these cases there is equality.

Individualism versus collectivism: measures the strength of behaviours that favour individual interest through the subject's initiative and autonomy; at a low rate of IDV (individualism/collective index) a country will be associated in which the subject is part of a cohesive group, always faithful, oriented towards a community perspective. According to Hall and Reed Hall, individualist cultures can be associated with low-context cultures characterized by explicit and direct communicative styles, while collectivist cultures are comparable to high-context cultures characterized by a non-verbal and gestural communication style.

Risk aversion / uncertainty index: highlights the ability to tolerate situations of uncertainty and ambiguity. A high rate of UAI (uncertainty avoidance index) is associated with a massive use of superstructures with rules and systems that allow for order and consistency; a lower score is instead associated with companies that are more open and closer to change.

Masculinity against femininity: shows the level of closeness to values related to the male stereotype (competition, success, well-being, ambition), a low index shows a closeness to social relationships.

Long-term orientation versus short-term orientation: defines the temporal horizon of society, distinguishing values that lead to long-term results (such as perseverance) or a vision oriented to the circularity of time influenced by the short term.

Coherently, Fratocchi *et al.* (2013) suggested that it might be interesting to question whether the likelihood of returning / replacing changes from one host country to another, given the industry and the size of the company (see also Ellram *et al.*, 2013).

The greater the distance between the "domestic" country and the "host" country, the greater the costs deriving from cultural distance. Expectations among managers and employees are generally better aligned in similar cultures (Stringfellow *et al.*, 2007). Although the theoretical perspective shows that cultural distance, which is influencing costs and, consequently, the results of offshoring initiatives, is still very undervalued by companies and managers in the decision-making process (Gales, 2008).

The analysis of cultural differences assumes considerable importance in the study of backshoring since they can derive the choice of the entrance strategy implemented by the company, the management of market segments and the identification of the value perceived by consumers.

The impact of culture on international business has long been interested by scholars (see, among other things, Gibson, 1999; Chui *et al.*, 2002; Ralston *et al.*, 2008) and recognized as very significant in transfer projects. . In fact, the failures of offshoring (which have caused strategic rethinking) have been partially related to the management of insufficient and ineffective cultural differences, sometimes defined as bridges (Gray *et al.*, 2013).

From the business point of view, although culture has been established as one of the determinants for multinationals when they enter foreign countries as explained by Hahn and Bunyaratavej (2009), culture has still been indiscriminate in offshoring, in particular from an empirical perspective.

From a business point of view, although culture has been established as one of the determinants for multinationals when they enter foreign countries as explained by Hahn and Bunyaratavej (2009), culture has still been indiscriminate in offshoring, in particular from an empirical perspective .

As we have seen so far, the practice of offshoring has become quite common and frequently used by organizations. In fact, there are numerous benefits that companies make by implementing this strategy, such as a lower cost of labor and production (Dossani and Kenney, 2003), access to a pool of highly skilled and significant workers

and professionals learning processes (Maskell, *et al.*, 2007). Companies usually make decisions about re-locating part of the company based on visible costs, such as the hourly wage of workers in a certain location or the costs of the facilities and infrastructures to be created. However, some organizations, following the implementation of the offshoring strategy, did not find the benefits and economic savings that they had initially foreseen in the project. The economic literature has highlighted that there are hidden costs of offshoring (Larsen, *et al.*, 2013) that escape from managerial attention and therefore emerge *ex post* in the strategic decision-making process. In fact, companies may find the need for greater coordination between the headquarter and units across national borders, or they may find the transfer of knowledge and implementation of the strategy more costly than expected. These costs have direct consequences in the strategic process because they are responsible for the gap between the planned benefits and those actually had and may be the cause of the failure of the offshoring project, forcing the companies to bring back the part of the organization that they initially had brought beyond national borders. An example of failure of an offshoring project is represented by the multinational computer company Dell Inc., which was forced to back-reshore its call centre located in India following difficulties encountered at the linguistic and cultural level (Frauenheim, 2003; Larsen, *et al.*, 2013).

The causes of these invisible costs (Stringfellow *et al.*, 2008) are numerous and are present both in the case of captive offshoring and in the case of offshore outsourcing although they may not be the same for both phenomena.

3.2 The Schulte model

The main objective pursued in implementing production relocation strategies abroad is to reduce the cost structure of the company, moving its production units from an evolved and more expensive context, to another in which the productive factors can be acquire at lower prices. In evaluating an offshoring project, therefore, managers take into account the possible costs that would be transferred to a foreign country rather than another, and compare them with domestic ones, thus determining any savings. In this process, the error that is often committed, however, is to make a calculation only on the

basis of the most visible and tangible cost entities, and therefore neglect all those elements that indirectly affect business spending. In this sense, there are *direct costs* that straight affect production costs, which are therefore more easily calculated, and whose imputation is certain and unambiguous (for example raw materials) and the hidden costs, less visible, but no less important for this. Delocalizing production on the basis of an estimate of only direct costs, gives both the idea of effective savings - even substantial - to which the firm is going, but at the same time turns out to be a calculation not properly accountable and consistent with the real expenditure that it will be faced. The set of costs to be incurred, direct, indirect and hidden is defined as "Total Cost of Ownership" (TCO), the total cost to be incurred for the possession - in this case - of a production unit abroad for its life cycle. The accurately and rigorously computation of the TCO, for a project of corporate relocation, is of fundamental importance, and it allows to avoid situations of unfavourable character to stay abroad. In fact, there are many cases of companies that, once the company has been transferred, and after some time, have realized that the costs to be incurred were higher than expectation, thus making the offshoring strategy less convenient than it had anticipated. The impact of *hidden costs*, therefore, is not negligible for the purpose of calculating the economic adequacy of the transfer project and, finally, its success. The German researcher Schulte analyzes the hidden costs of a company and distinguishes them in a model that starts from the difference between direct and indirect costs of a production relocation project. Then, it classifies the hidden costs according to their various nature, putting the attention on the question that not always, however, they are correctly quantifiable. According to this model, therefore, the main hidden costs of the companies that relocate production are:

- *Region specific costs*: costs related to the particular context of the host country, such as local taxes, health and social security, customs duties;

- *customer service costs*: costs related to customer care, and therefore to customer assistance during the purchase and post-sales processes. Usually in developing countries these services are more backward than in advanced countries, and to compensate for these shortcomings, they induce companies to invest higher amounts to train personnel directly on site, or to have the services managed from the offices located at home. ;

- *quality costs*: costs related to compliance with specific quality standards, by virtue of the activation of quality control and internal inspection processes. Furthermore, additional costs in this regard are represented by the risk that the quality of finished products is in any case lower than that required on the end markets and in the advanced countries;

- *supply chain costs*: costs related to the lengthening of the offshore company's distribution and logistics chain, and to risks deriving from longer delivery times, from the existence of intermediaries and from the integrity of production factors and final products;

- *operational costs*: costs related to the management of plants, machinery and equipment, both during the transfer phase, both once located abroad, and finally during assistance and maintenance;

- *people / talent costs*: costs related to the procurement of qualified human resources of value professionals, both for the roles of greater responsibility and for those of the base. In the management of this phase, offshore organizations suffer from greater problems - which can be translated into costs - that induce managers to activate more intense and recurrent selection and training courses, without counting the economic resources required for the management of expatriates;

- *financial costs*: costs related to the procurement of financial resources necessary to cover the economic needs essential to be able to manage the business activity. In this case the costs will be connected to the problems that characterize the financial systems of the developing countries, very often slow and full of bureaucratic constraints;

- *intellectual property rights*: costs related to the risk of theft of intellectual property. In developing countries, in fact, the percentage is much higher than in the western ones, and China ranks first in this ranking with 50% of cases;

- *cultural differences*: costs related to cultural differences existing between different countries and belonging to different geographical areas. This factor, often neglected in the evaluation of the projects of delocalization, greatly affects the health of the business, the process of setting people in a new context and the transfer of new production models, which if not done in the most correct way would cause management problems and coordination;

- *bribery*: costs related to the level of internal corruption in the countries. Factor to consider when the plan is to relocate production of a company, since the payment of bribes could call into question both the healthy protraction of the business and discourage the same foreign investments.

- *Psychic distance*: The exclusion of these factors from the computation of the total costs of a production transfer program can lead companies, in a second step, to make decisions that challenge the choices previously made. In fact, many companies that relocate production because they have erroneously calculated the actual benefits that can be achieved by relocation. The true cost incurred by companies abroad, therefore, consists of a series of factors, not all quantifiable, which however must be considered so that the choice made is not less convenient than one might think in the planning stage. Nevertheless, one of the reasons for the backshoring is precisely this, linked to the existence of hidden costs, whose forecasting is not always easily assessed.

3.3 Cluster analysis

The business strategy studies are very often focused on topics that have a "complex" nature, in the sense that they embrace differentiated profiles of investigation (competitive, social, economic-financial, organizational), involving composite elements and often linked to each other (the strategic direction and operational management, the "choices and actions" and the results that follow, the underlying strategic orientation and the strategy that implements it), meander along the different levels of the company structure (the ownership structure, the governance bodies, the managerial structure).

This awareness pervades intimately the research Coda (1988), from which emerges as the business strategy represents a sort of physiological field of encounter and integration of varied, multidimensional and even multidisciplinary knowledge.

Reference should be made, for example, to the surveys of "*business formulas*" instrumental to "*business success*", to studies on the "*current and future competitive positioning*" of companies, to the work around "*finalism*" that orients the company design, to the configuration of the "*organizational contexts*" functional to the unravelling of deliberate or intentional strategies, to the analysis of the performances and their

relations with the structure of the company. Consider, again, the themes of "quantitative growth" and "qualitative development", considered to be co-essential for the "*innovative and coherent combination of all the elements*" of the entrepreneurial formula in a long-term perspective. However, each of these themes embraces composite phenomena and must address the problems related to the multidimensionality of the object of study.

The hypothesis that complexity is an intrinsic feature in the analysis of business dynamics is shared by much strategic literature, which often underlines the need for a multifaceted perspective to understand the nature of organizations and evaluate their behaviour (Fiss, 2007). Particularly in international research, especially in the one devoted to experimental investigations, attention has been paid to the obstacles presented in the study of "complex" issues, largely due to the multidimensionality of the concepts to be examined (Hatten and Hatten , 1987).

Despite these difficulties, from a methodological point of view, the reference to simpler explanatory sub-concepts of complex constructs allowed scholars to identify distinct groups of companies on the basis of one (or a few) variables. Along these lines, the multidimensionality typical of the phenomena faced has often been resolved by identifying reference "business models" that summarize the characteristics of a group of companies that share a common profile in relation to the few distinctive variables chosen for the purposes of the study.

Beyond the name adopted in the literature to identify these "models" (groups, archetypes, prototypes and so on), they are typically divided between types and taxonomies (Miller 1996). The typologies describe ideal types, defined by a unique combination of organizational attributes: among others, Miller (1996) emphasizes that typologies are particularly useful for understanding the dominant patterns in the business environment, arguing that there are only a limited number of company assets, of viable strategies, of productive choices that can be adopted in certain situations.

In contrast, taxonomies seek to classify organizations into comprehensive and mutually exclusive groups, although the choice of variables can significantly influence the identification and composition of groups.

The hypothesis underlying these reconstructions is that "business models" constitute a way to "simplify" and "capture" the intrinsic complexity of the investigated

phenomena. Consider, by way of example, the studies on business performance: in them performance is often divided into elementary components that are easier to study and analyze (such as income results, competitive results, social results), which can therefore be the object of a more reliable "measurement" process.

The international literature, to give an *empirically* founded answer to the configuration of "business models", often refers to techniques that go beyond the study of individual cases, identifying similarities between organizations, describing comparable behaviours and designing archetypes for as far as possible generalizable.

Cluster analysis is certainly one of the most widespread techniques in this field of investigation, used in *Strategic Management* studies since the seventies.

In particular, among the multivariate statistics techniques, cluster analysis represents an exploratory analysis, of an unsupervised type, which allows to group statistical units (belonging to a given population) into groups, based on their logic distance. The latter is quantified by means of similarity / dissimilarity measures, so that the observations are as homogeneous as possible within the clusters and as unevenly as possible between the different clusters (Fabbris, 1997).

With respect to a given distance measurement, it is therefore possible to convert a data matrix $n \times p$ into a matrix of the distances $n \times n$, where each element of the matrix d_{ij} is an expression of the distance between the vectors, with respect to all the p variables considered. Next, the rules for grouping units into subgroups (based on their similarities) were be defined.

Clustering techniques allow the selected sample to be broken down into groups, each of which is characterized by the minimum internal "distance" between the group elements and the maximum external "distance" with respect to the elements belonging to the other groups identified. To this end, cluster analysis is able to consider multiple variables that define the characteristics of the sample, grouping a statistical population made up of companies according to a principle of homogeneity (Hatten and Hatten, 1987).

The dissemination of these techniques in the strategy studies is not accompanied by the general acceptance by scholars of the analytical capacity of cluster analysis (Barney and Hoskinsson, 1990; Meyer, 1991; Thomas and Venkatraman, 1988). The

doubts to the use of cluster analysis stem mainly from two orders of criticism (Ketchen and Shook, 1996). Firstly, the high degree of discretion of the researcher in the evaluation and interpretation of results is criticized, which reduces the level of generalization of the business models deriving from the analysis. Subjectivity concerns not only some steps of the clustering process, but refers, in particular, to the absence of a statistical test capable of clearly attesting the presence (or not) of a significant relationship between the results of the analysis and the hypotheses of departure of the investigation. A second order of criticism concerns the not infrequent lack of a solid theoretical system by researchers, often more attentive to statistical profiles than to a complete analysis on the cognitive aims of the research and on the structure of the relationship between the different company dimensions involved (Barney and Hoskinsson, 1990, Thomas and Venkatraman, 1988). In these circumstances, the identified clusters may not reflect any empirically grounded situation, due to the ability of cluster analysis to identify groups even where they do not exist.

To reduce the effect of these criticisms, a sort of agenda has been developed in the Strategic Management studies, which indicates the criteria to be followed for a reliable use of cluster analysis (Ketchen and Shook, 1996). These works show how the rigorous application of cluster analysis is the prerequisite for obtaining reliable results. These works highlight the importance of the following aspects: (a) the selection and treatment of variables; (b) the choice of the appropriate clustering algorithm according to the type of analysis to be performed.

Variables can be chosen on the basis of an *inductive* approach (in the sense that they are selected by the researcher according to the dimensions of analysis considered relevant), *deductive* (the choice derives from the theoretical framework on which the research is based) and *cognitive* (the variables are defined by experts of the phenomenon under study). Moreover, the selected variables may be subject to standardization or not and may or may not be treated to solve the problem of multicollinearity between them.

The algorithms for the application of a cluster analysis are divided into two large families, the *hierarchical* ones (in which a hierarchy of partitions is constructed characterized by an increasing - or decreasing - number of groups, viewable through a tree representation) and those non-hierarchical (in which the distance from a

representative point of the cluster is used to define group membership, having fixed the number of partition groups a priori).

Hierarchical cluster analysis identifies a hierarchy of partitions, such that each cluster is part of a larger cluster, which is itself contained in a higher amplitude class, until the cluster containing the whole set of entities is identified analyzed. The hierarchical methods can be further classified into *agglomerative* or *divisive*, respectively in the case where the research is of a *bottom-up* type, and then proceeds by successive aggregations of the units starting from groups formed by a single object, or *top down*, and then it starts from a single cluster containing all the entities and proceeds to identify successive partitions until arriving at clusters formed by a single unit. The divisive algorithms generally require a greater computational effort than the aggregative ones since they do not imply the need to identify the inclusion / exclusion thresholds on the single objects. In cluster analysis we use a threshold, which however does not partition at the level of the single object, but at the group level. In fact, it is possible to identify a hierarchy of possible partitions and, therefore, by inspecting the dendrogram, using statistical criteria. You can decide to determine a partition in groups simply by cutting the branches of the dendrogram horizontally. Hierarchical clustering operates in a similar way to the way to perform classification in biological taxonomy, where for example insects are hierarchically classified by specializing their species from very large families to much smaller families. The hierarchical methods (among the best known Single-Link and Complete-Link can be mention) are in practice used above all when the patterns are discredited and do not belong to a metric space. In this case, in fact, "ad-hoc" similarity criteria can be implemented to control aggregation and division.

The methods belonging to the second class, the non-hierarchical one (such as the K-means) allow (i) a limitation of the impact of extreme values, due to the fact that they allow observations to change membership between groups and (ii) facilitate the achievement of higher levels of homogeneity within groups. Hence non-hierarchical or partitive methods generate non-hierarchizable groups, generally requiring that the number of groups be determined a priori and provide a single partition as a final result. Such methods identify (usually through iterative heuristic algorithms) of the partitions that minimize a given clustering criterion, for example the sum of the squares of the errors.

Although there are no right and wrong clustering algorithms, the partitive methods have the disadvantage of requiring the ex ante specification of the number (k) of the clusters to be extracted (Kaufmann and Rousseeuw, 1990). Given the need to determine this number empirically, a hierarchical algorithm is used in the present work.

Hierarchical methods have a clear advantage from the computational point of view. However they are more sensitive to outliers and do not allow falsify the configuration reached: once a unit has been assigned to a group remains in it forever. Non-hierarchical methods do not suffer of this problem, but require the proper selection of seed. It is good practice to apply a plurality of methods to verify the stability of the groups: a hierarchical analysis is applied first to identify the number of groups and any outliers; then a non-hierarchical technique is applied to allow for change the configuration reached. The determination of the number of clusters it can take place on the basis of a priori information or the distance at which it takes place aggregation (Proietti, 2000).

The second relevant choice in the cluster analysis concerns the measure used to evaluate the similarity between two units and / or between units and clusters. This measure takes the generic name of distance: in the presence of quantitative variables, the Euclidean distance can be typically used to aggregate single observations. For aggregation to clusters and clusters, however, there are several possible criteria.

Distance-based methods are characterized by a number of limitations in addressing group analysis problems. The impossibility of solving some important issues in a statistically rigorous way and with inferential techniques, and to know the statistical properties of these methods, are probably the most relevant problems that lead to research other methods of grouping. There is therefore a need for procedures based on more formal statistical criteria and which allow to tackle clustering by inserting it in a more rigorous context.

When discussing group analysis, a fundamental problem remains that of determining the number of clusters in the data. These problems are not resolvable when using partition methods or hierarchical methods and, for this reason too, *model-based clustering* has been introduced that can answer these questions with inferential techniques. In particular, the problem concerning testing the number of components in a

mixture, and therefore the number of clusters in the data, is obviously very important from both a theoretical and a practical point of view, and has therefore attracted much attention in various studies over the years. In model-based clustering this problem is prompted to a question regarding the selection of the model to be used; therefore, model selection methods are used.

Model-based clustering (Fraley and Raftery, 1998) (Fraley and Raftery, 2002) is based on the idea that the observed data come from a population characterized by a certain number of sub-populations within it. This approach models each sub-population separately and the entire population as a mixture of these, using the finite-mist models.

The first analyzes based on finite-mix models date back to the late 19th century (Pearson, 1894) but they had little following, basically due to the complexity of the models and the computational efforts needed to estimate them. Their subsequent development is therefore due to the advent of computers and the introduction of the EM algorithm. Although not specifically dedicated to these models, the EM algorithm has in fact allowed a simplification of the estimation process and a greater understanding of the properties and is undoubtedly the most popular estimation technique in this field. The EM (Expectation-Maximization) algorithm (Dempster *et al.*, 1977; McLachlan and Krishnan, 2007) is a general approach to the process of estimating maximum likelihood in cases where incomplete data are present.

The use of the EM algorithm is therefore justified and easily understandable because, seeing the data as incomplete allows, in this type of analysis, to think of the variables as the labels indicating the membership of the i -th observation at k -th group. These labels are the main difference between discriminant analysis and group analysis and, in this situation, the focus is on estimating them so that a clustered data can be subdivided. The partition of the observed data takes place after estimating the finished mixture model and, in particular, after obtaining estimates for the vector of the labels z_{ik} . In the moment in which the convergence of the EM algorithm is reached, data can be obtained thanks to the posterior probability using the MAP (maximum a posteriori rule) rule which assigns the observations to the group with the higher posterior probability. The data partition in groups is then made by classifying the i -th observation to the group.

For what has been said so far, the advantages that are found, when a clustering approach based on a finite mixture model is adopted, are manifold: inferential procedures can be used and there is a greater flexibility of the forms assumable by clusters, especially if flexible distributions are adopted and, as a result, groups do not take typical forms based on the method used, as is the case with distance-based methods. Furthermore, this method provides the probability of group membership for each unit. It can be noted that model-based clustering does not necessarily provide a partition in groups but it can happen that it groups all the observations into a single cluster, which is not possible with hierarchical and non-hierarchical methods.

Cluster models focus on identifying groups of similar records and on labelling records based on the group they belong to. This is done without the benefit of prior knowledge about the groups and their characteristics. In fact, you may not even know exactly how many groups to look for. This is what distinguishes clustering models from other machine learning techniques: there is no predefined output or target field for the model to predict. These models are often referred to as unsupervised learning models, as there is no external standard on which to evaluate model classification performance. There are no right or wrong answers for these models. Their value is determined by their ability to capture interesting groupings in the data and provide useful descriptions of such groupings.

Before analyzing the results (paragraph 3.4), paragraph 3.3.2 describes the main variables used instead. All the variables described have been standardized (subtracting, that is, at each value observed its mean, and dividing by the standard deviation) (Norušis, 2011).

3.3.1 The data

Quantitative analysis is based on the use also of economic-financial variables, in the assumption that the dynamics of the values of the duration of offshoring over time is at least partially symptomatic of the incidence of the psychic distance, considered as a hidden cost, on the decision of the companies to have relocated abroad and thus entailed backshoring. In light of this assumption, it was not intended to interpret the groups

identified through the sole use of EM based on the duration of the offshoring. Logically, the survey does not aspire to propose generalizations, but attempts to identify dynamic "business groups" built from the data collected. On a methodological level, the analysis process is articulated in the following steps, briefly described. With regard to the definition of the sample, the sample examined is composed of: (i) manufacturing companies with local units operating in Italy³⁶; (ii) companies for which the AIDA³⁷ provider has provided information on the turnover and number of employees for the 2016 financial year; (iii) from the data taken from AIDA, which almost completely covers the reference population, a sample of 59 companies has been reached.

Since the interest in backshoring has emerged only recently and that the data useful for a meaningful study must be particularly analytical, the information currently available on the phenomenon is very limited. As often specified by other authors (Gray *et al.*, 2013), the information required for an in-depth reshoring analysis, including backshoring, is often at a level of detail to which the budget and most of the surveys publicly available companies do not come, because it is about accessing internal data at the level of managerial choices. In Europe there is a database of the Fraunhofer Institute for Systems and Innovation Research (ISI) called the European Manufacturing Survey (EMS), which collects periodic surveys on manufacturing companies and has already been used by other researchers to study reshoring (Kinkel and Maloca 2009, Kinkel 2014, Dachs *et al.*, 2012), but it is not publicly accessible for personalized analyzes. In Italy, the UniCLUB-MoRe back-reshoring research group has collected, through secondary sources, a list of constantly updated and constantly increasing backshoring cases, but not accessible to the public. Without having publicly available databases sufficiently complete to carry out an in-depth analysis, it was decided to build a list of cases with all relevant information using only secondary sources: academic journals and specialized periodicals and generalists (Il Sole 24 Ore, Corriere della Sera, La Repubblica, websites and blogs specializing in economic news, business consulting reports (BCC, PwC), reports by sector organizations (ANIE Confindustria), studies of Italian and international

³⁶ Companies in liquidation or who have ceased their activity have been excluded.

³⁷ Aida is the database managed by the Bureau Van Dijk which contains financial information and personal data on over 500,000 joint-stock companies operating in Italy, taken from the financial statements filed with the Chambers of Commerce.

public institutions (ICE, UNCTAD, Unioncamere Veneto), press releases of companies Interested in the company: general information and business sectors, commercial, economic and financial data of the company for the available years (database Bureau van Dijk "Aida" and Eurofound), characteristics of the offshoring operation carried out in the past: destination, methods, times and motivation to leave the country.

In a first phase, all the unprocessed information was collected and therefore the variables were refined in order to bring them back to the theoretical dimensions analyzed and prepare them for the subsequent quantitative analyzes. The information considered fundamental for the definition of a complete case derives from the models referred to chapter 1 and 2 and concern: reasons, timing of backshoring, the distance of the offshore country in geographical, cultural and psychic distance.

3.3.2 The variables used in the cluster analysis

Coherently with the nature of research, which is essentially exploratory, the choice of variables is more oriented to theory building than to theory testing. The variables have been identified with the aim of inserting in the algorithm the richest possible description of the properties of the sample. To this end, also in light of the indications of the literature, the variables have been identified following all the possible approaches: inductive, deductive and cognitive. As a result of this process, eleven variables were identified and the data-base that draws from the information present in the AIDA provider was then constructed.

In order to construct a significant map of the backshoring cases, even starting from what was suggested in the literature analyzed above, the following variables were collected and calculated.

The duration of the offshoring

The time references considered most significant to consider were the start year of the offshoring and the year of the start of the backshoring process. The availability of this data allows to completely frame the delocalization and relocation cycle, and allows to obtain an interesting derivative variable, that is the time spent abroad. This variable can

be interesting to distinguish in an approximate but probable way, short-term errors (in the case of short-term delocalization operations) from probable strategic reformulations following changes in the macroeconomic or competitive context of reference (in the case of delocalization operations) longer).

The geographical distance and geographical distribution of companies in the source country

Despite the decline in transport costs and the global economy, the Dow e Karunaratna (2006) research confirms that geographic distance is still the single most influential "commercial inhibitor". The geographical distance represents almost twice the total variance explained as all the other combined psychic stimuli. This is consistent with the findings of Leamer and Stopper (2001) that the importance of geographical distance has not substantially decreased.

The geographical distance between Italy and the different foreign countries from which the companies in the sample have carried out return operations. It was calculated a geographical distance in km (as the crow flies) between the positions of the two production sites involved in the backshoring process. In case of lack of information on the specific city where the foreign plant was located, the geographic centre of gravity of the foreign country was used as a reference point. The geographical distance variable constitutes a proxy that can be linked to other evaluations: as the geographical distance increases, it is reasonable to assume that the costs of organizational coordination increase (for example, for longer trips and time zone differences) and logistics costs.

The companies that populate the sample were also classified according to their geographical area.

The cultural distance

In addition to the simple geographical distance, a cultural distance was also calculated, following the measure defined by Kogut and Singh (1988). As cultural distance increases, difficulties and costs of integration and coordination increase in a multicultural context.

The different dimensions of Hofstede³⁸ (distance from power, social orientation, masculinity / femininity and rejection / acceptance of the 'uncertainty, long-term orientation, Indulgence versus Restraint) are measured for each country on a scale from 0 to 100 and can be used to compare cultures with each other, but can be applied quickly and directly even in business and managerial contexts, having been taken directly from organizational behaviour. This feature has also been very successful, so much so that today the Hofstede model is certainly one of the most used in the study of intercultural management. Many studies have followed and expanded Hofstede's approach, and among these it is interesting to note the contribution of Kogut and Singh (1988) who, applying the dimensions to the concrete problem of determining the optimal way to enter a foreign market, have determined a summary indicator that measures the cultural distance, and therefore allows you to sort and compare different pairs of countries. This indicator is useful because it also makes it possible to simplify the multidimensional model to a single measure which, in the specific case, assumes the following algebraic form:

$$CD_{jk} = \sum_{i=1}^n \frac{(I_{ij} - I_{jk})^2}{nV_i} \quad (1)$$

Where

CD_{jk} it is the measure of cultural distance between the country j and the country k ,

I_{ij} e I_{ik} indicate the measure for the i -th index of Hofstede in the countries j e k ;

V_i indicates the variance for the i -th index of Hofstede, and n is the number of Hofstede indices taken into account (often the first 4, as for the most complete data).

Assuming that the first four Hofstede indices are considered, on a theoretical level, the index can assume values ranging from zero to 23.9 (in the case where one country has all the indices equal to zero and the other all the indices equal to 100). However, since there are no different countries up to this point, in most cases the index does not exceed the value of 5.0.

The psychic distance

³⁸ As discussed in section 3.1.2.

To calculate the psychic distance Dow and Karunaratna (2006) propose the identification of the so-called *psychic stimuli of distance* rather than direct measures of psychic distance. This reflects the centrality of the debate that has developed over time about the exact nature of psychic distance. Researchers at Uppsala University first popularized the concept of psychic distance as: "Factors that prevent or disturb the flow of information between business and the market." Examples of such factors are language differences, culture, systems politicians, level of education, the level of industrial development, religion, etc. " (Johanson and Wiedersheim-Paul, 1975).

However, more recent studies (Evans *et al.*, 2000) argue that it is better to focus on the psychic distance perception of managers, because it is their perception of distance that influences their choices and behaviours. In an attempt to reconcile these two points of view, Dow and Karunaratna (2006) have adopted the terminology of "*stimuli of the psychic distance*" and "*perceived psychic distance*".

In terms of the dimensions chosen to calculate the psychic distance, referring to the studies of Dow and Karunaratna (2006), in this paper the focus will be on linguistic and religious differences within and between countries which are just two of the group of stimuli identified by the authors.

Despite the rapid recognition of the importance of linguistic and religious differences in international affairs (for example, Beckerman, 1956, Ronen and Shenkar, 1985, Boyacigiller, 1990), these two dimensions of distance have only recently become relevant in international empirical affairs literature as potential determinants of managerial decisions and constant behaviours (Dow and Karunaratna, 2006; Berry *et al.*, 2010; Luiz, 2015; Castellani *et al.*, 2013). Of particular relevance is the fact that there are also substantial differences between countries in the amount of heterogeneity within the country on these two dimensions, which makes them very suitable for studying the effects of diversity within the country.

Language

While a number of researchers have made efforts to incorporate language differences into empirical international economic studies; most of them (Geraci and Prewo 1977, Davidson and McFetridge 1985, Srivastava and Green 1986, Arora and Fosfuri 2000) used simple dummy variables for a common language. Vahlne and

Wiedersheim-Paul (1977) and Klein and Roth (1990) are among the few who have used more complex approaches to measuring linguistic differences. Unfortunately, both scales have been built in a way that makes them unique to their particular samples and can not be applied to companies that come from other countries. In light of this situation, Dow and Karunaratna (2006) have developed three new indicators to measure differences in languages. The first measure (L1) is a five-point scale that focuses on the difference between the main languages of two countries. This scale takes a step beyond the dummy variables, recognizing that some sets of languages are more similar than others and can be grouped into a hierarchy. The second and third measures (L2 and L3) focus on the reported incidence of the main languages of one country in other countries. These indicators recognize the heterogeneity of languages within countries. The linguistic data come from Grimes (1996).

A primary language for a given country is defined as any language that can be spoken by more than 20% of the population (widely used second language qualifications), or a language that has a special official status within the country (for example English in India and in several African nations). For their analysis Dow and Karunaratna, (2006) have used 34 languages that have qualified as the main language for at least one of the 38 countries. These languages have been grouped into a hierarchy of families, branches, sub-branches of first level and second-level sub-branches based on Grimes (1996) a more substantial classification of 6.809 languages.

With respect to the specific role that linguistic distance could play, it is more commonly cited as a key factor in the disruption of the information flow, as explicitly recognized by Johanson and Vahlne (1977), and has been widely discussed and explored by numerous authors (Demirbag *et al.*, 2007; Dow and Karunaratna, 2006; West and Graham, 2004). It has been shown that linguistic distance has a strong impact on market selection (Berry *et al.*, 2010), commercial flows (Dow and Karunaratna, 2006), entry mode (Demirbag *et al.*, 2009), establishment methods (Dow and Larimo, 2011) and knowledge transfer (Schomaker and Zaheer, 2014).

Religions

Issues relating to the measurement of differences in religions are directly analogous to the difficulties previously discussed in measuring languages. Three

indicators are used for differences in religion. The first indicator (R1) is a five-point scale that focuses on the difference between the dominant religions of two countries. The second and third indicators (R2 and R3) focus on the reported incidence of the dominant religion of the source country in the receiving country and vice versa. The data on religion come from Barrett (1982). Dow and Karunaratna (2006) developed a multiple regression model calibrated on a set of 627 pairs of randomly selected countries from a population of 1303 pairs of countries (38 countries minus some specific pairs due to missing data) for estimates for all five of Hofstede's dimensions have been published. The resulting model is then validated on the remaining 676 pairs of countries in the same population.

As reported in the article "*The effects of a linguistic and religious diversity within foreign acquisitions*" (JIBS, April 2016), two measures of diversity were created within the country using essentially the same data to create the linguistic distance and the scales of religious distance.

In both cases (for linguistic diversity and religious diversity) the indices are constructed in such a way that the value 1 represents the situation in which there are no two individuals within the country who speak the same language or adhere to the same language religion. On the other hand, value 0 represents the situation in which every individual in the country speaks the same language or adheres to the same religion.

To represent it mathematically, it is considered a country with n different languages or religions. P_i represents the proportion of the population for which language is their mother tongue, or religion; i is their professed religion. The diversity index D is calculated as follows:

$$D = 1 - (P_1 * P_1 + P_2 * P_2 + \dots + P_n * P_n) \quad (2)$$

The indices of religious and linguistic diversity have been used in this work to calculate the psychic distance, in terms of religion and language, between the country of origin and the country of relocation.

The motivations

The motivations, which instead led companies to back down and transfer the production in Italy, were divided into:

- *Made In Effect*. The companies come back to Italy for reasons related to the quality of the product and the Made in Italy factor. They decide to start backshoring operations, to rely on Italian suppliers, much more reliable and competent than Chinese rivals, for example. In Italy, they can rely on artisans, with expert hands, that allow them to obtain a high quality product. Precisely for this reason, many companies have included the production of high-end lines, so as to exploit the "Made-in" factor and obtain a higher premium price.

- *Firm's Global Reorganization*. In this macro group of motivations were included:

- Market. The companies start backshoring operations, in order to better manage important outlet markets or to follow a client who has decided to return to Italy. The so-called time to market, is a very important factor, however the long transport times did not allow to achieve this advantage and provide adequate assistance to customers.

- Efficiency. The strategy is to concentrate R & D and production, in order to obtain a better result with regard to innovation and not to waste resources. Pursuing a logic of waste reduction and revision of the company organization, the international network is rationalized.

- Economic crisis. According to the studies of Uni-CLUB MoRe Backshoring, from 1997 to 2013 the production lines reported in Italy were 79, most of which in the last five years, at the height of the Great Crisis.

- Taxation and labor costs. The reduction in the labor cost differential in the countries of offshoring (Frattocchi *et al.*, 2013) encourages companies to repatriate their production activities in their source country, especially if they are supported by tax relief on recruitment in Italy.

- Know-how in the source country. Re-establishing supply relationships abroad and, above all, looking for lost know-how at the time of relocation is less

convenient than maintaining or restoring the know-how built in the country of origin.

- *Logistics costs*. Companies fall by pursuing a logic of reducing transport costs, but also to avoid delays in delivering goods and improving customer service.

In order to be able to insert them into the database, the macro-groups were classified by assigning to each macro-group a value (1 for Made In Effect, 2 for Logistics costs and 3 for Firm's Global Reorganization).

The frequencies related to the backshoring motivations that emerged for the sample in question are:

Figure 18: Backshoring motivations

<i>Back-shoring Reasons</i>	
Made In Effect	24
Firm's Global Reorganization	14
Logistic Cost	5

Source: Own elaboration

Figure 18 summarizes the most relevant descriptive statistics relating to the database thus formed: as evidenced by the number for each variable, with the data available it was not possible to identify some data for some of the cases analyzed.

Figure 19: Descriptive statistics for the identified backshoring cases

Variables	n	Mean value	Min value	Max value
Year Offshoring	35	1999,1	1984	2013
Year Back-shoring	42	2013,5	2009	2017
Last Offshoring (in year)	36	13,8	1	27
Number Employed 2016	59	900	4	6968
Income 2016	59	250.437.400 €	515.233 €	1.357.883.000 €
Geographic distance from home country	42	4.807,7 km	597 km	9.671 km
Psychic distance (Religion)	42	-0,03	-0,39	0,36
Psychic distance (Language)	42	0,17	-0,43	0,57
Cultural distance	42	2225,25	0,29	4042
Motivations	43	1,72	1	3
Geographic area	59	1,29	1	4

Source: Own elaboration

3.4 Methodologies and results

The research has set itself the goal of giving an overview of the phenomenon of backshoring using a concrete basis given by empirical evidence. Consequently, the subsequent analyzes were not oriented to the verification of certain hypotheses derived from the theory, and instead proceeded with an exploratory analysis.

After this preliminary analysis, several hypotheses of exploratory analysis were taken into consideration to understand the cases collected and the empirical evaluation of the consequences deriving from the use of distance metrics and different types of bonds. Given the limited number of samples, in a first moment to identify a number of starting groups a hierarchical cluster analysis was adopted (Fraley, 1998); subsequently, to characterize the analysis by identifying the models through a non-hierarchical method (EM) was used.

3.4.1 The cluster analysis algorithm: choice of method and distance measurement

By defining the general mode of operation of the classification, the various possible specifications of the analysis model were tested. Various combinations of variables are used to apply the hierarchical clustering procedure; for each of the classifications thus elaborated, different solutions were analyzed with a different number of clusters and the "goodness" was evaluated. Among the various possibilities evaluated, it was the most descriptive and statistically significant choice, a model that considered the variables: Geographical distance, Psychic distance (language), Psychic distance (religion), Cultural distance, Employee number, Revenue, except Last Offshoring.

In this work, the Ward method was used to generate the clusters, an algorithm that in each phase of the procedure combines the groups that minimize the increase in the sum of the quadratic distances within the groups (Norušis, 2011). Consequently, the measure of the distance between the cases chosen for grouping is the Euclidean quadratic distance, that is the sum of the quadratic distances for each variable. The Ward method minimizes variance within groups. The objective of the partition is to minimize the amount of variability within the groups, while maximizing the variability between the groups, so as to obtain homogeneous classes within them and well separated from one another. This method aggregates at each intermediate step the objects that determine the minimum loss of inertia between the classes and then aggregates the pair of entities that minimizes the deviance between the centroids of the possible groups. In fact, a partition is considered as much better the more the classes are homogeneous within them and different from one another, i.e. cluster the higher the variance between the clusters, and the internal variance of the clusters is reduced (Ward, 1963).

Finally, to characterize the analysis by identifying company models the EM method that calculates the probability that an object belongs to a cluster will be applied.

The information included in the built database - made up of 11 observations for each of the 59 companies in the sample, for a total of 649 input data - were treated with the algorithm called Expectation-Maximization (EM).

The research was carried out assuming a very broad survey perspective, integrating a quantitative EM-based method with qualitative methods traditionally used in corporate strategy surveys. This made it possible not to reduce the complexity of the concept to be analyzed (the decision to repatriate) by choosing a few variables a priori, but allowed to observe the behaviour of companies with regard to numerous "quantitative dimensions" expressing differentiated patterns.

3.4.2 Choice of the optimal number of clusters

Depending on the chosen criterion, there are various clustering algorithms that provide a procedure for determining the solutions that optimize it. Most of the clustering criteria are defined on the basis of the following two observations: patterns within the same cluster must be more similar to each other than patterns belonging to different clusters; clusters consist of relatively high density point clouds, separated by areas where density is lower. Among the various possible criteria:

- *sum of the squares of the errors*: it minimizes the squares of the distances from the centers of the classes (also called criterion of least variance).

- *other criteria based on intraclass variance*: this is a family of methods all aimed at minimizing variance within classes.

- *scattering-based criteria*: they tend to minimize the intraclass variance and at the same time maximize the interclass variance.

The most commonly used partitioning (non-hierarchical) clustering algorithms are K-means (or its Fuzzy C-means variant) and Expectation-Maximization (EM).

K-means is a very simple method that is computationally simple and simple to implement, which optimizes the "sum of error squares" criterion. In its basic version, the algorithm can be described as follows: generates K clusters and determines the centre; or it directly generates K points to be used as cluster centres; assigns each point to the cluster whose centre is nearest, based on the chosen distance criterion (Euclidean, Mahalanobis, ...); recalculates the cluster centres as the mean of the coordinates of all the points belonging to them; repeat until the termination criterion is satisfied (generally the

termination criterion provides that the centres remain constant, and therefore the partitions do not change between two successive steps).

This algorithm tends to converge rather quickly (rarely takes more than 10 steps) and to provide rather good results, provided we start with a reasonable initial solution. K-means has some disadvantages: first the number of classes K must be known a priori; moreover, the optimization is iterative and local, so you can have convergence on a local maximum of the solution.

The fuzzy variant of the K-means allows a pattern to belong with a certain degree of probability to different classes; this variant sometimes provides a more robust convergence towards the final solution, but suffers essentially from the same problems as the standard version of K-means. Several variants have been proposed to solve these problems: for example, to minimize the risk of convergence towards local minima the algorithm can be executed many times starting from different initial solutions, random or perhaps produced by an evolutionary method (genetic algorithm).

A statistical methodology for determining how many clusters divide objects is to determine the number of groups at the maximum average silhouette value. A silhouette value for each object is a measure of how similar that object is to other objects in its own cluster compared to objects in other clusters. This value varies from -1 (maximum dissimilarity) to 1 (maximum similarity). It is defined as:

$$s(i) = \frac{b(i) - a(i)}{\max\{a(i), b(i)\}} \quad (3)$$

where $a(i)$ is the average distance from the i -th object to all other objects in the same cluster A and where $d(i, C)$ is the average distance of the i -th object with respect to all objects contained in all clusters $C \neq A$ (Rousseeuw, 1987).

The *Expectation-Maximization* method is based on the hypothesis that the data in space were generated by a mix of distributions, i.e. that each class generated data according to a specific distribution, but at the end of the generation the patterns appear as products from a single multi-modal distribution. The goal of clustering through EM is to trace (starting from the training set patterns) to the parameters of the individual distributions that generated them. To this end, the form of the distributions is assumed

and it is assumed, for simplicity, that they are all of the same type: the most frequent case is that of mixing multinormal (Gaussian) distributions whose parameters are estimated from the data definition.

EM was born for the calculation of the maximum likelihood in case the available data $X=\{x_1, x_2, \dots, x_n\}$ are incomplete due to the lack of some values $Y=\{y_1, y_2, \dots, y_n\}$. Therefore each complete pattern $z_i=[x_i, y_i]$, $i=1..n$ consists of two parts of which only the first one is known. In fact, in some cases, for example when the Gaussian distribution parameters are to be derived, the data are complete, but the potential of EM is exploited to make the complexity of the maximization tractable.

In general, the likelihood L of the parameters \emptyset given the X patterns corresponds to the probability (density of probability in the continuous) of having obtained the patterns given the parameters. For simplicity, instead of likelihood, its logarithm is maximized. Considering the independent patterns the probability of having obtained the training set patterns is the product of the probabilities of the individual generations.

The algorithm consists of two steps, which are iteratively repeated until convergence. In the Expectation phase the expected value of the complete log likelihood is calculated:

$$\log L(\emptyset|Z) = \log L(X, Y) = \log Pr (X, Y|\emptyset) \quad (4)$$

starting from the training set and an initial estimate of the parameters \emptyset ; in the Maximization step the set of parameter values is calculated that maximizes the expected value obtained in the Expectation step. This set of values is used as parameter estimation in the next Expectation step.

The algorithm always converges, but runs the risk of falling into an excellent room; moreover, as with k-means, with some initial solutions it is possible to obtain bad results, and it is not easy to determine the optimal number of clusters if they are not known a priori.

Instead of assigning examples to clusters to maximize differences in means for continuous variables, the EM clustering algorithm calculates the probability of cluster membership based on one or more probability distributions. The goal of the clustering

algorithm is therefore to maximize the overall probability or probability of the data, given the (final) clusters.

The approach and basic logic of this clustering method are as follows. Suppose to measure a single continuous variable in a large sample of observations. Furthermore, suppose that the sample consists of two groups of observations by different means (and perhaps different standard deviations); within each sample, the distribution of values for the continuous variable follows the normal distribution. The goal of EM clustering is to estimate averages and standard deviations for each cluster in order to maximize the probability of the observed data (distribution). In other words, the EM algorithm attempts to approximate the observed distributions of values based on mixtures of different distributions in different clusters. The results of EM clustering are different from those calculated by k-means clustering. The latter will assign observations to the clusters to maximize the distances between the clusters. The EM algorithm does not calculate the actual assignments of the observations to the clusters, but the probability of classification. In other words, each observation belongs to each cluster with a certain probability. Obviously, as a final result, it is usually possible to review an effective assignment of the observations to the clusters, based on the probability of classification (larger).

With respect to these choices, the following paragraph reports the results of the cluster analysis conducted, carried out using the programming language R³⁹.

3.5 Results of the cluster analysis

3.5.1 Overview

As mentioned in paragraph 3.3, the data collected were subjected to a standardization process. Once the agglomerative hierarchical clustering method was chosen, the cluster number was first identified by applying the Euclidean distance and

³⁹ All the choices made involve a high level of discretion, but above all a long process of defining the algorithm and the final result. It is evident that this analysis can only be concluded when the number of clusters (and in the case of a territorial analysis also their geographical disposition) is sufficiently descriptive of the observed territory. In a trial and error process, the results presented in this work are actually the result of many agglomeration attempts, each with the aim of adding meaning or correcting any mistakes made in previous versions.

then applying the Ward method. The groups obtained in this first clustering process were two.

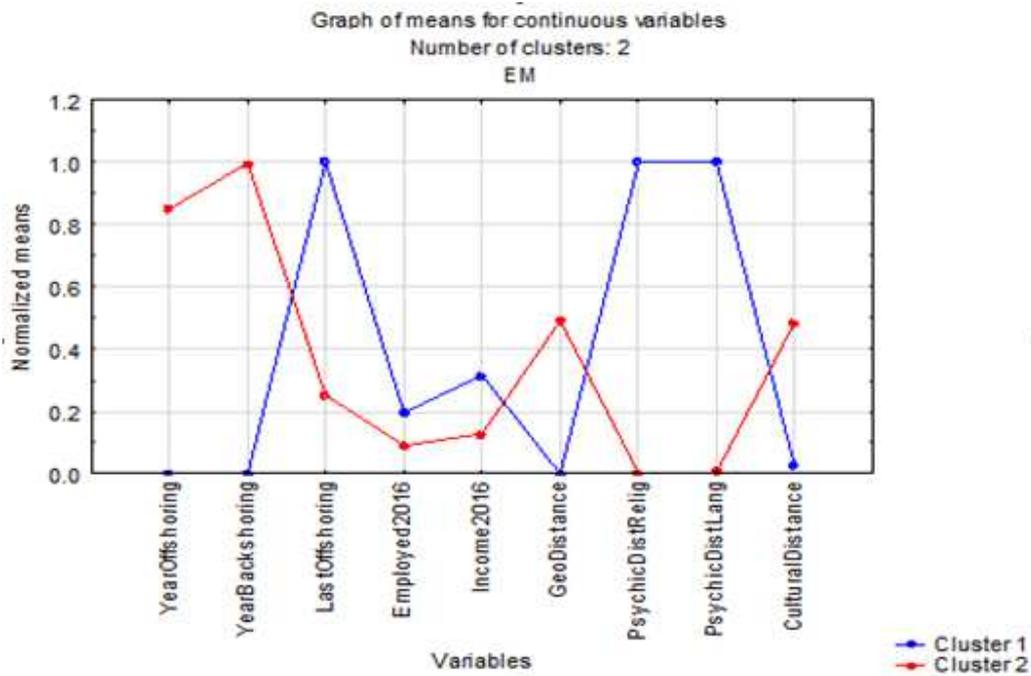
In order to identify the optimal cluster number, having a missing data in the database available, it was decided to use the Expectation-Maximization method. The Expectation-Maximization (EM) is a modern approach to the treatment of missing data, it has become known thanks to the works of Dempster, Laird and Rubin (1977) has been gradually improved (McLachlan and Krishnan, 2007; Meng and van Dick , 1997; Oakes, 1999). The technique is to estimate the parameters on the basis of the observed data, and then to estimate the missing data on the basis of these parameters (phase E). Then the parameters are again estimated based on the new data matrix (phase M), and so on. This process is iterated until the estimated values converge (Barbaranelli, 2003).

The figure below shows how the likelihood varies with the number of clusters, that is, what is needed to establish the "optimal" number of clusters.

In the moment in which the convergence of the EM algorithm is reached, the partition of data can be obtained thanks to the posterior probability using the MAP (maximum a posteriori rule) rule which assigns the observations to the group with the highest posterior probability. The data partition in groups is then made by classifying the *i-th* observation to the group.

Both graphs state and validate the existence of two groups within the database.

Figure 20: Graph of continuous variable means



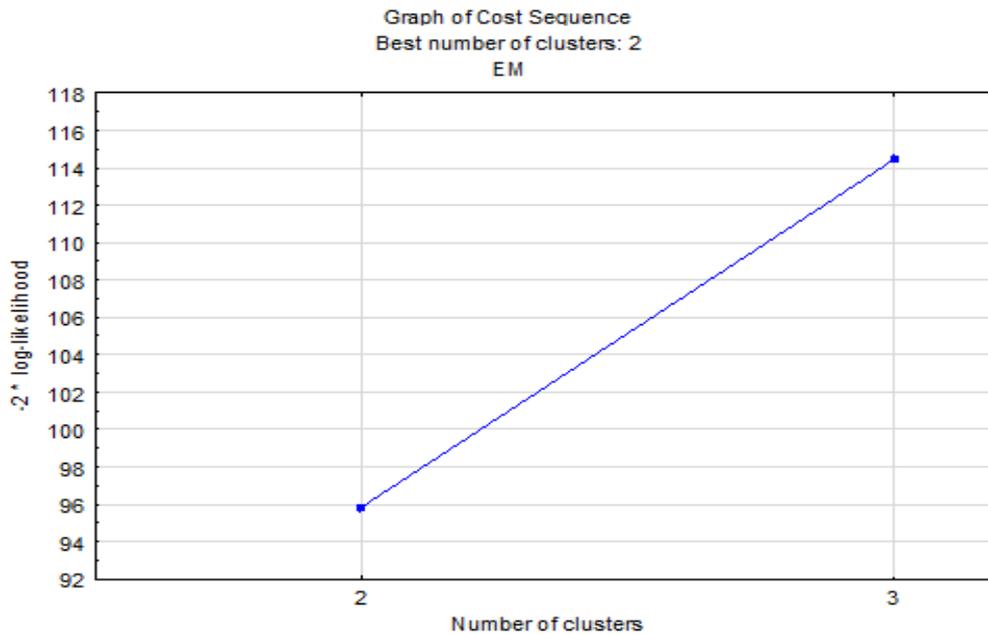
Source: Own elaboration

The graph shows the scaled cluster means for all continuous variables.

The Figure 21, instead, describes the error function (average distance of the observations in the test samples to the centroids of the cluster to which the observations were assigned) on the different cluster solutions.

It seems that the error function quickly passes from the 2-to-3-cluster solution and then "flattens".

Figure 21: Graph of cost sequence



Source: Own elaboration

The underlying probabilistic model EM provides for 2 groups. The 2 groups are reasonable because they identify the a priori empirical evidence.

For Cluster 1 the most interesting features compared to the second are the geographical distance and a number of employed greater than the Cluster 2. The Cluster 1, at the same time, presents values of distance in cultural and psychic terms that are less than the latter. The duration of the offshoring is not very indicative because they tend to be in line with the global sample rates in both.

Figure 22: Variables means for cluster

Cluster	Last offshoring (in year)	Number Employed (2016)	Geographic distance from home region (in km)	Psychic Distance (religion)	Psychic Distance (language)	Cultural Distance
1	14,1	1005	4991	-0,065	0,039	2009,08
2	13,73	798	4734	-0,013	0,220	2311,72

Source: Own elaboration

3.5.2 Cluster features

The backshoring cases of the first cluster are those made by geographically distant countries (for example China). At greater geographical distance corresponds a greater psychic distance in terms of diversity of religion within countries.

Examples of the first group include cases such as Armani. Giorgio Armani Swiss Branch closes after 20 years. The company intends to transfer the majority of its employees to its Milan site, completely closing the Mendrisio site where it opened an administrative centre twenty years ago. Despite wages higher than the source country, Mendrisio has attracted fashion companies because of tax advantages. Recent changes in local taxation have considerably reduced the attractiveness of the region.

Pasell, a supplier of some large companies such as Whirlpool, Indesit and Candy, in 2004, started a factory in Wales to deliver Indesit, but when the customer moved elsewhere in 2009, the company was forced to close and return to Italy.

Martini & Rossi is a consolidated Italian company that produces alcoholic beverages. The company is part of the largest Bacardi-Martini group with around 8,000 employees worldwide. At the beginning of 2016, the company closed the Mollet plant near Barcelona to move production near Turin. The company offered an alternative to its Spanish employees (including their transfer to Italy). According to various sources, the European market suffers from a decrease in alcohol consumption and the Italian plant has an unused production capacity.

In fact, Teknit repatriated production to better manage the markets of Northern Europe. It has chosen to pursue a just-in-time logic.

The companies belonging to this group can be classified as belonging to a model of companies that have decided to return to produce in their country of origin mainly due to the high geographical distance. Since, in spite of this, in this group the differences in terms of religion and language and in cultural terms in general in foreign countries have influenced the choice of backshoring in a less intense way compared to the second group of companies. In fact, the motivations that have driven the companies belonging to cluster 1 are mainly to a firm's global reorganization.

Cluster 2 is strongly characterized by variables of distance weaker than the other in terms of psychic distance on the side of language differences within countries. Some examples are Prada and Falconeri (Calzedonia Spa).

Prada, an Italian company renowned for its fashion products, intends to invest in four new factories in Italy in the regions of Tuscany and the Marches to be part of its production. The main objective is to reduce time-to-market and improve production control. Made in Italy is the reason why he decided to return from Romania in 2004 after 18 years spent abroad.

Falconeri is an Italian fashion brand currently owned by the Calzedonia Group. Falconeri was founded forty years ago but was acquired by Calzedonia during the 2009 crisis. While for Calzedonia, the group adopted a relocation strategy for most of the production, in the case of the Falconeri brand, it opted for the backshoring. The "Made in Italy" tag is advantageous for the image of the product, while the return to Italy offers better access to high quality Italian materials.

These are the companies that in recent years have realized the advantages that backshoring would offer both the improvement of the quality of the brand and of the product, both in terms of savings on logistics and production costs. This last feature seems to characterize this cluster: due to the long duration of offshoring (14 years) and the probable management difficulties (due to its high cultural and geographical distance), we can not speak of correct strategic errors through backshoring but rather long-term strategic corrections that could be the repositioning of costs. Despite the high cultural and language distance, the psychic distance in terms of religion is lower than the first group. With respect to the psychic distance, the cultural distance seems to be more perceived by managers and therefore directly influences the choice of backshoring.

Argo Tractors, Artsana, Fiamm, these are just some of the companies that belong to this group. The companies found are of medium-sized, which operate all over the world and belong mainly to the machinery and electrical engineering sector. The relocation strategy was implemented in 2000, through direct foreign investments. Despite this type of investment, the relocation has been of medium duration: over 14 years. Among the countries where the results come from, we always find China and Eastern Europe, but also Portugal, Sweden, Great Britain and Turkey.

The reasons for backshoring respond to strategies that pursue Made in Italy.

Bonfiglioli Italia and Faac come to Italy because of logistics costs.

Beghelli, which started investing in the Czech Republic from 2013 to return production in the Bologna area mainly due to logistical problems that have become progressively more significant due to the slowdown in the market.

Another case that falls within this group is that of the historic tuna prodigy in Portugal (with the Portuguese trademark "As do Mar"). General Conserve. Portugal, although part of Western Europe, has a different culture from Italian. Backshoring in Sardinia was dictated by the logic of quality.

Fiamm chose to close the structure in the Czech Republic, due to high inefficiencies: low productivity, high salaries and high staff turnover. The company has decided to invest again in the historic plant of Montecchio Maggiore (VI), equipping it with a highly technological and cutting-edge plant, destined for the production of large storage systems, a rapidly expanding market. The plant in Abruzzo has also been upgraded, with a number of employees between 220 and 330.

Stinga Spa (formerly Global Garden Product) closed the Swedish plant to concentrate R & D and production at the Castel Franco Veneto plant.

Azimut-Benetti, a leading company in the production of yachts, has instead brought part of the production in Italy, previously delocalized in Turkey.

Tod's, Natuzzi and Safilo respectively belonging to the fashion, furniture and eyewear industry are large companies that operate globally and have consolidated international experience. The great fashionistas moved in choosing to approach the local strangers in 2000. All three chose Romania as their target, benefiting from lower labor costs. Safilo and Natuzzi, on the other hand, moved first, at the beginning of the 1990s, choosing instead to invest directly. The reasons for the return to Italy are all linked to the quality of the product: Natuzzi wants to produce high-end products in Italy to exploit the Made in Italy factor, while Safilo's strategy wants to return to Italy most of its glasses, even medium-range ones, to benefit from highly qualified personnel and obtain high quality products. The three great fashionistas certainly did not reveal the fact of the delocalization of production; some quality standards that foreign third parties can not maintain are difficult to maintain. Back in Italy, know-how and crafts that only in this

country can be found. The return of production takes place mainly through investments to expand existing plants or to build new ones. In this way, the quality control of the product is much higher.

Marco Palmieri, Chief Executive Officer of Piquadro, has been renamed by some newspapers as an "ambassador" of backshoring, and many have cited the Piquadro case as a classic example of the phenomenon. In fact, the company decided in 2013 to bring part of its production in Italy from China, but the motivations are many: quality is important for the company, the Made in Italy and the Italian craft experience, but what seems having triggered the choice to make backshoring seems to be the constant increase in labor costs in China, justifying a re-evaluation of the location of the product and the choices of location of the product, especially the higher end.

In this cluster there are companies that have decided to repatriate pre-delocalized production activities like Diadora for the second time. Italian company producing footwear, t-shirts and other items such as backpacks and bags. The Diadora office is located in Caerano di San Marco, in Veneto (Italy). According to President Moretti Polegato, Diadora plans to restore 10% of its production activities in Italy from 2017 onwards. The goal is to produce 100,000 pairs of footwear by the end of the year and will cover 7-10% of production across all product lines over the next three years. The rest of the production is still produced in China, Thailand and Vietnam. Currently, 5% of production produced by national production and by Italian suppliers. Polegato said that having the national production line is very positive for a company like Diadora that aims at product innovation. Furthermore, "Made in Italy" offers Diadora a unique quantification and allows Diadora to monitor the carbon footprint to control the environmental impact of the production chain. Today there are 6 employees in the rewinding system and a 9-year increase is expected.

Within this cluster, for example, is the case of And Camicie, a brand of Columbia Spa, a company in the province of Venice that produces shirts between Italy, Romania and China. Columbia has a long history of relocation, since it has been producing in Romania since 1995 (for over 18 years). However, in 2013, the possibility of entering into a contract with an important Chinese group that, among other things, manages a large number of shopping centres, has prompted the company to return the production of

clothing to this channel in Italy. This is because, for Chinese partners and their growing middle class customers, it is essential that the product is an original "Made in Italy" with the guarantee of quality and the prestige that this brand implies.

The companies belonging to this group, characterized by greater psychic and cultural distance indices than cluster 1, can be classified as belonging to a model of companies that, in line with Schulte's model, in evaluating an offshoring project, have irresponsibly calculated all kinds of costs that would be transferred to a foreign country rather than another. In this process the error that is often committed, however, is to make a calculation only on the basis of the most visible and tangible cost entities, such as those resulting from a smaller geographical distance, and therefore neglecting all those elements that indirectly however affect corporate spending.

The identification of this model allows reasonably to consider, the psychic distance as a hidden cost to all effect, less visible, but not less important than the cultural distance.

It is no coincidence that the 'Made in' effect is the reason that has driven companies belonging to this model to return to Italy.

3.6 Remarks

The lack of an official database of backshoring cases, the low number of the sample and the availability of incomplete data have prevented the construction of a real analysis model.

The identification of 2 models through the EM algorithm has allowed to consider, reasonably, the psychic distance as a hidden cost to all effects, less visible, but not less important as the cultural distance.

Companies often return to produce in their source country still have little perception of those factors that disturb the information flow between the company and the target market stopping at a mere consideration of geographical and cultural distance.

From the data it emerged that the perception of psychic distance, both in terms of religion and language, is not yet fully taken into account by managers in choosing to end the offshoring process. Since, as confirmed by the literature, they influence the choice of

delocalization rather than the choice of backshoring. Compared to the psychic distance, the cultural distance seems to be more perceived by managers and therefore it can be affirmed that it directly influences the choice of backshoring and therefore be included among indirect costs and hidden costs.

3.7 Value and limits of the research

The results achieved, as discussed in the previous paragraphs, are certainly of good descriptive value as they provide a picture of types of backshoring in Italy. The research was entirely focused on backshoring implemented in the Italian territory. Compared to other existing work on the topic (in particular Fratocchi 2013, 2014), it wanted to deepen the analysis and to enter into the merits of business choices in terms of motivations, psychic and cultural factors, timing of backshoring operations in Italy.

Compared with other studies that tend to evaluate variables one at a time and analyze them disconnected (Fratocchi 2013), this work goes in the direction of consider all the useful dimensions at the same time to have the overall view of the phenomenon. This approach therefore tends towards identifying several backshoring processes, and takes into account the entire delocation and relocation cycle. However, it is important to note that there are also some important limitations in this research related to the sample and to the explanatory variables adopted. First of all, the size of the sample, even if satisfying given the research method that it was necessary to employ, does not allow for more complex quantitative analyzes than the one reported here and also limits statistical significance to some of the information obtained through the cluster analysis. In addition, it was not possible to deepen the analysis of the economic and financial aspect by looking for indicators that could measure the success or failure of backshoring operations, as aggregate economic results (at balance sheet level) do not allow to evaluate in a timely manner choices that have a product or component line effect. An article by Gray *et al.* (2013) has, in fact, highlighted the great difficulty that would be encountered in conducting such an analysis: trying to obtain analytical data from secondary sources is practically impossible. A search through surveys would make it very difficult to distinguish a decision error from real costs, and a controlled experiment would prevent

from capturing the richness of the context and the path dependency of location decisions. However, the authors suggest that it would be possible to obtain quality information on multiple backshoring decisions by a single company if backshoring phenomena will continue to increase or may be implemented in the US context where multinational corporations are located much larger than the average Italian company.

As for the variables, the cases of companies analyzed are very heterogeneous and it is possible that, considering the different reasons behind the offshoring and backshoring processes, the variables are less significant.

In addition, it might be interesting to conduct a *duration analysis* with the aim of highlighting the determinants of the duration of offshoring operations of Italian companies before embarking on backshoring. This kind of analysis has already been carried out by Ancarani *et al.*, (2015) for USA and European companies, it would be interesting to apply it to Italian backshoring cases and to compare the characteristics of the companies that have returned and those that have continued their stay abroad.

3.8 Conclusions

In this chapter we have illustrated a quantitative empirical research carried out in order to comprehensively summarize the forms in which backshoring phenomena occur in Italy. In the search, data and information were collected for 59 companies divided into two clusters. The analysis and description of the clusters has thus allowed to highlight some comprehensive backshoring models for Italian companies that have emerged naturally from the analysis and have not been imposed a priori. The research has the value to consider the characteristics of the different clusters in a global way and to divide the cases on the basis of the generally accepted process, not limited to individual variables.

In particular, looking at the influence of the psychic and cultural distance on the basis of the market landscape, it can be concluded that companies entering new markets must adapt to a foreign culture and to have a greater perception of psychic distance levels. When the cultural and psychical distance levels are high, the outsourcing company can not operate effectively in the foreign market. The implications for executives are to

properly assess the differences that may exist between the source country and foreign organizations because it is crucial to choosing the appropriate strategy in the offshoring decision. In order to make accurate decisions on offshoring, a thorough assessment of the degree of similarity is required. Very often however, the sense of strangeness affects the company for the absence or limited knowledge of the foreign country and its culture. The perception of psychic distance and cultural distance translates into what Himer defines the *liability of foreignness*, all those factors that disturb the flow of information between the company and the market: differences in language, culture, political system, development industrial and religion (Johanson and Valhne, 1977).

Companies perceive the distance, not only geographic and cultural, but also psychic with the foreign countries they relate to and look for standardization or adaptation patterns in multiple situations. If search for such methods fails, companies revisit their strategies, backshoring is the result of this business strategy review process.

The data collected mainly reflects the situation of Italian companies that seem to perceive cultural distance as a large and multidimensional phenomenon but have not yet reached a sufficient level of understanding and maturity regarding the psychic distance.

The analysis takes into account among other variables: the time between the time of offshoring and backshoring and the psychic distance between the parent company and the branch.

In relation to time, as suggested by literature analysis, backshoring cases occurring after a short time than offshoring might indicate strategic mistakes, while return processes that take place after many years may result from changes in strategy or contextual conditions. In any case, it is important to remember how the course of time is not "neutral" compared to the organizational learning processes in the company. In particular, organizations tend to "forget" (Easterby-Smith and Lyles, 2011) knowledge that is not coded or difficult to transfer from one worker to another: new routines and new ways of working replace old procedures, which are removed from the organizational memory. During the offshoring process, this process of removing previous knowledge could be exacerbated by time and distance. Consequently, the effectiveness of the backshoring process depends on the company's ability to design and implement mechanisms for transferring accumulated knowledge from a part of the enterprise

(foreign affiliate) to other parties (the parent company or the home work is transferred), for example through training and support processes involving new and old workers.

In relation to distance, the benefits of proximity to the development of organizational knowledge and to favour coordination between the various parts of the enterprise have long been studied (e.g. Malmberg and Maskell, 2006; Johnson, Siripong and Brown, 2006). Distance has always been treated as a complex concept, relative not to its geographical, but also cultural, economic and linguistic aspect. This also adds to the perception of differences in language, culture, political system, industrial development, religion (psychic distance). Indeed, if the geographical distance reduces the possibility for people and organizational units to interact, the cultural distance could hinder the transfer of knowledge between the various parts of the enterprise as a result of misunderstandings and perceptions of errors; the psychic distance could disturb the flow of information between the company and the destination country abroad.

For these reasons, an excessive distance between the parent company and the branch office may have been damaged by knowledge of the enterprise. As a result, the effectiveness of the offshoring process could be affected by the distance between the foreign country where the company relocated and the home country and resulted in backshoring.

The results suggest that few companies have complete information in the decision-making process. Unless there is an urgent requirement for a relocation decision that encourages decision-makers to delay decision-making until it can assimilate more information. A fully informed relocation decision - or at least, as fully as possible, given the time constraints, may be more beneficial to the long-term partially informed decision today. A structured delay can ensure that decision-makers have timely, accurate and complete information (Hartman *et al.*, 2017).

CONCLUSION

As indicated in the introduction, the aim of this thesis was to provide a complete perspective on the backshoring phenomenon at different levels of analysis, from general to particular describing the phenomenon as a whole and aggregate and analyzing the theories available in the strategic and organizational matrix literature. Provided theoretical reasoning schemes, a exploratory quantitative empirical research (cluster analysis) was carried out.

Having to draw conclusions, backshoring in Italy is a phenomenon that happens despite the context conditions being unchanged. Indeed, if there is a strong economic policy in the United States to stimulate backshoring, this can not be said for Italy. This achievement therefore drives the consideration of the single enterprise and its issues as a good level of analysis, while many of the aggregate assessments may be fruitless. In fact, there are no particularly obvious external conditions that have an effect on the company's interest to backshore, external effects are partially lost in the analysis, in favour of internal factors within the enterprise. Partly in support of this, it is noted that the choice of backshoring is, in some ways, much more weighted than the previous offshoring choices. This supports the thesis that internal assessments are more and more important than external ones: in fact, context conditions are the same for all companies or at least for homogeneous business groups, and therefore require less analysis by the individual enterprise. Internal factors, however, are *firm-specific*, and require the company to undertake more thorough analysis for accurate valuation.

The strategy of backshoring is not an immediate process, and it has many complexities related to changing the resources of a company, even if it is back in the home country. It is not a simple return on your own steps, as skills and relationships dissolve over time if these are not actively managed. However, this is not a rebuilding from scratch: the fact that backshoring choices seem to be more "360 degrees" than most offshoring choices can be linked, in fact, to the phenomenon of *organizational learning*. The international experience of the enterprise plays a key role in defining the company's ability to adapt to a changing resource base and to rebuild skills and relationships for success. Backshoring, even when made as a correction over a previous mistake, must not

be experienced as a defeat or recognition of the company's inability to be international. Conversely, backshoring is also a learning opportunity, which provides the company knowledge about to relocate, both in Italy and elsewhere. This allows to derive an important managerial implication of this analysis: beyond the localization, it is important to know how to capitalize on the experiences that have been experienced and to draw lessons for the future.

Another fact that should be emphasized is as follows: it appears that backshoring is, in fact, not purely localization choices or, in any case, not the same as other location choices. This is because the locations are not the same for each other and, above all, they are not the same for all businesses. It seems, in particular, that there is a kind of "house effect" that is realized in different meanings. For some companies there is a peculiar advantage of being 'Italian in Italy', which is deeply linked to the fact that companies always have a major history in the source country, which influences them. The impact of history can be positive or negative, and therefore there may exist firm-specific advantages or disadvantages to backshoring. In addition to this, if in the context of internationalization the phenomenon of *liability of foreignness* (Zaheer 1995, cited in Luo 2000) and the *liability of newness* (Oviatt and McDougall 1994, cited in Luo 2000) are known, it is important to note that phenomena similarly, paradoxically, they are not entirely absent even in backshoring choices.

There are, for instance, the difficulties that a company must overcome in its "return home", linked both to the peculiar history of the enterprise and to the fact that the skills and relationships, if they are lost, must also be reconstructed in the country of origin.

One last problem, then, is related to the existence of circumstances that make sure everything can not be planned. In backshoring cases, in fact, they take on some weight emerging strategies, as opposed to planned strategies. Indeed, backshoring can hardly be interpreted as a planned strategy, but is always the result of certain opportunities that are identified and acquired by the company. For this reason, the "return" operations are, in a sense, all different, as each enterprise faces different risks and opportunities, and also the way it chooses to take the opportunity is unique. There are recurring points and patterns, but each enterprise is unique in the declination of these schemes.

Recognizing the importance of emerging strategies, however, should not deter companies from investing abroad. While it is true that there are elements of unpredictability in backshoring choices, it is also true that at the far end of planning there is no chaos, but flexibility. That is why it is important to recognize the importance of contingencies in backshoring choices, so businesses are organized to have flexible and ready-to-use analysis schemes to evaluate emerging opportunities. That is, knowing how to create processes and routines that can evolve over time and adapt to dynamic circumstances.

Backshoring is a much more complicated process than others have meant, because it involves changes in resources, and requires the ability of companies to evolve, and to transfer or rebuild local skills and benefits lost over time.

The present work therefore concludes with the belief that it has offered a further contribution to the description and understanding of the backshoring phenomenon and offering research hints.

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