The geography of manufacturing FDI location.
Evidence from Italy

Mariachiara Barzotto, *Birmingham Business School, University of Birmingham,* Edgbaston, B15 2TT, Birmingham (UK), m.barzotto@bham.ac.uk

Giancarlo Corò, *Ca' Foscari University Venice,* Cannaregio 873, Fondamenta San Giobbe, 30121 Venice (Italy), corog@unive.it

Ilaria Mariotti, *DAStU – Polytechinic of Milan,* P.zza L. Da Vinci, 32, 20133 Milan (Italy), ilaria.mariotti@polimi.it (corresponding author)

Marco Mutinelli, *University of Brescia,* Piazza del Mercato, 15, Brescia (Italy), marco.mutinelli@unibs.it

Abstract

The literature on FDI determinants indicates that MNEs allocate their investments among countries to maximize their risk-adjusted profits (Caves, 1974). These profits may depend on three groups of factors belonging to the eclectic OLI paradigm developed by Dunning (1979, 1993, 2003, 2009): (a) "Ownership advantages", that is, firm-specific factors enabling the firm to grow more successfully than competitors in the home or host countries (i.e. proprietary technology and management expertise); (b) "Location advantages", that is, location-specific factors in the host country that make it the best location for the firm to do business (i.e. cheap labor cost, growing market size, and good infrastructures); and (c) "Internalization advantages", that is, factors associated with the firm's trade-off between FDI and exporting or licensing (i.e. trade barriers, and difficulties in finding a trustworthy licensee). The main location determinants identified by both location theory and research on the "L" advantages are: (i) "traditional location factors" (i.e. labor costs and availability; labor skills and labor unionization; market size and market potential; competitiveness level and density; land costs and availability; agglomeration economies ; transportation costs and other costs – taxes and financing); (ii) infrastructures, services and intangible assets; (iii) environmental and social context; (iv) policy framework; (v) information costs.

The literature on foreign direct investments has mainly analysed the location strategies of MNEs across national borders, but there have been few studies of location decisions by foreign investors within the borders of a single country. The literature on the location determinants of inward FDI within Italy is scant. Mariotti and Piscitello (1995) in their analysis about cross-border takeovers involving Italian industrial firms in the period 1986–91, find that the spatial distribution of inward FDIs is mainly governed by information costs. Besides, Basile et al. (2005) explore the determinants of MNEs' location choices in 52 EU regions, including Italy, in 1991-1999. It results that Italian regions are doomed by the "country effect" and indeed attract less than their potential. This is mainly explained by the national policies and institutions, which might have discouraged foreign firms to plant their affiliates in Italy. Finally, Bronzini (2007) investigates the role of localization economies, urbanization economies, and of host country's size in attracting FDI within the 103 Italian provinces in the period 1997-2004. The author finds that localization economies are important in attracting FDI, while there is no evidence that FDI inflows are drawn by the sectoral diversification of the Italian provinces. Besides, localization

economies play a role mainly in the industrial sector, while within services these types of externalities are insignificant. By contrast, small firms hamper investment in both industry and services. Moreover, the presence of small firms deters foreign investment while that of big firms has no impact on foreign investors' decisions.

All the studies mentioned above have focused on the head offices' location, mainly because of data availability (Mariotti, Mutinelli, 2016). Nevertheless, the geography of FDI location is better explained by the location of the FDIs' establishments especially when the industry of investigation is manufacturing. Indeed, while head offices may privilege urban areas, and largest cities, which offer firms advantages linked to: urbanization and localization economies, market size and potential, skilled labor force availability and business opportunities, transportation accessibility, and connectedness with the rest of the world, FDIs establishments may follow different location patterns (i.e. land availability, localization economies, financial incentives, etc.), settling down in peripheral areas.

Cities, mainly global cities, contribute to a reduction in foreign investors' foreignness liability (Nachum, 2003; Goerzen et al., 2013) because they can reduce the uncertainty of foreign operations, offering global connectedness , cosmopolitanism, and the abundance of advance producer services and information (Castellani, 2016). Moreover, they also offer advantages in accessing the market, and therefore tend to attract market-seeking investments. Moreover, agglomeration economies enhance creativity (Florida, 2005) – they are the favourable location for talents and the best creative minds –, efficiency (Combes et al., 2012), and innovation (Acs, 2002). Nevertheless, even negative aspects characterize largest cities, i.e. excessive agglomeration and congestions problems that lead to higher costs and lower quality of life. This explains why some MNEs' activities (i.e. logistics) that require large areas in which to operate are mainly located outside – but near to - global cities (Holl and Mariotti, 2017). The same holds true for R&D activities that require the construction of large laboratories which is best outside global cities, in areas that are still agglomerated and which offer a quality of life that is attractive to the most skillful (Castellani, 2016). Finally, peripheral areas should attract more labor intensive activities, in which production costs are relatively higher.

The present paper enriches the debate on the attractiveness of Italy towards manufacturing FDIs by concentrating on the location of the establishments of manufacturing foreign affiliates in the 110 NUTS3 provinces at the year 2012. Data on inward FDIs, and their establishment location, are provided by the Reprint database. The paper is structured into six sections. The introduction is followed by a concise literature review on the location factors, and on the perception of entrepreneurs. Section three is dedicated to data and methodology. Descriptive statistics and econometric analysis are presented and discussed in sections four, and five, respectively. Conclusions and further research questions follow.

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