



# Local agglomeration, entrepreneurship and the 2008 recession: Evidence from Italian industrial districts



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## ARTICLE INFO

### Article history:

Received 16 November 2015

Received in revised form 1 March 2016

Accepted 15 March 2016

Available online 23 March 2016

### Keywords:

Industrial districts

2008 recession

Agglomeration effects

## ABSTRACT

We investigate whether the impact of recessions on entrepreneurship is affected by the presence of industrial districts, a source of local agglomeration economies. Using Italian Labour Force quarterly data from 2006 to 2011 and a “difference-in-differences” approach, we show that the share of entrepreneurs in local labour markets where industrial districts are present has declined more than in comparable areas after the beginning of the 2008 recession. The estimated negative differential effect ranges between 4.8 and 7.9% in absolute value. We examine alternative explanations – including differences in industrial specialisation and composition, access to credit propensity, exports, population density and the composition of talents – and conclude that our result is consistent with the intense social interactions typical of industrial districts, acting as a multiplier that amplifies the response to shocks.

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## 1. Introduction

Economic recessions have ambiguous effects on entrepreneurship. On the one hand, they decrease potential business income and wealth, thereby reducing the incentive to start or stay in business. On the other hand, they restrict employment opportunities, and consequently increase inflows into self-employment as alternatives to inactivity and unemployment (see Fairlie, 2013). Do these effects vary with local economic conditions and in particular with the presence of agglomeration economies?

There is ample evidence that these economies affect economic activity and entrepreneurship, because of the presence of consumer/supplier linkages, entrepreneurial and knowledge spillovers and labour market pooling. Rosenthal and Strange (2004), Glaeser et al. (2010), Combes et al. (2011), and Combes and Gouillon (2015), review the effects of local agglomeration on economic performance.<sup>1</sup> Glaeser and Kerr (2009), identify as drivers of the geographical concentration of entrepreneurs: (i) demographic differences such as education and age; (ii) differences in natural resources; (iii) agglomeration economies.

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<sup>1</sup> Ciccone and Hall (1996), are among the first to study the relationship between local density and productivity, showing that the former positively affects the latter. More recently, Delgado et al. (2014), report that the presence of regional clusters – groups of closely related and complementary industries operating within a particular region – has positive effects on regional economic performance.

Delgado et al. (2010), argue that the presence of a cluster of related industries in a location can foster entrepreneurship by lowering the cost of starting a business, enhancing opportunities for innovation and enabling better access to a more diverse range of inputs and complementary products. The co-location of companies, customers and suppliers also increases the perception of business opportunities (see Porter, 1998).<sup>2</sup>

Less is known, however, about the effects of agglomeration economies on how entrepreneurs react to recessions. Previous work by Guiso and Schivardi (2007) sheds some light on the issue, but it focuses on employment rather than entrepreneurship. In this paper, we look at the 2008 recession and at industrial districts, a source of local industrial agglomeration characterised by the prevalence of small and medium sized enterprises operating in the manufacturing sector, strong product specialisation, proximity and substantial social interactions. Silicon Valley, Route 128, the so-called Third Italy (Bagnasco, 1977) and the City of London (Inkpen and Tsang, 2005) are well-known examples of this type of industrial agglomeration.

<sup>2</sup> As argued by Minniti (2005), everything else being the same, the larger the number of entrepreneurs that the potential entrepreneur observes in the local area, the lower the ambiguity she experiences. By observing others, she acquires information and skills. Throughout this process her social environment becomes important, and her participation in a broadly defined network helps her to define the contour of the set of her entrepreneurial tasks. The existence of a significant number of entrepreneurs also legitimizes her activity and enables her to exploit a number of established routines. Areas with a higher density of entrepreneurs have a stronger entrepreneurial culture, which encourages entry.



Fig. 1. Map of the Italian industrial districts (grey areas).  
Source: Istat, 8th Census of Industries and Services.

Previous literature indicates several factors as candidates to explain why the effects of a recession on entrepreneurship could vary across areas that differ in their degree of agglomeration, some insulating local entrepreneurs, and some others favouring the propagation of the crisis. On the one hand, as remarked by Guiso and Schivardi (2007), the intense social interactions within entrepreneurs that characterise industrial districts are likely to amplify the responses to shocks, because of the *social multiplier* and of information spillovers (see also Glaeser et al., 2003). Alternatively, higher local agglomeration may favour the entry of entrepreneurs by developing a culture of risk taking and reinforcing social models that individuals imitate. When the tide raises all boats, increasingly less talented individuals may be attracted into entrepreneurship. When a recession hits, these individuals are more likely to be swept away.

On the other hand, the presence of industrial agglomerations may reduce the costs of being an entrepreneur, and build a safety net of reciprocal support, thereby sustaining the ability to survive during a global recession. The literature on social capital suggests that industrial clusters are areas where the level of trust among people is higher (Putnam, 2000).<sup>3</sup> This may not only facilitate the access to credit (Guiso et al., 2004b), but also improve the economic performance of

<sup>3</sup> Social capital is the set of norms and values that creates the fabric of the society, glues individuals and institutions together and constitutes a necessary link for its governance (Soubeyran and Weber, 2002). Economic research investigating how social capital affects local economies includes Guiso et al. (2004b), who show that the heterogeneity of social capital across Italy explains the heterogeneity of financial development. Trigilia (2001) and McEvily and Zaheer (1999), find that industrial districts exhibit high levels of social capital, mutual trust and cooperation, and Molina-Morales and Martínez-Fernández (2010), argue that social capital is likely to affect the propensity of firms to innovate, and that firms in industrial districts are exposed to ties and links which are favourable to innovation.

Table 1

Economic and social characteristics of urban areas, industrial districts and other local labour markets.

	Urban areas	Industrial districts	Other local labour markets
Average years of schooling	9	8.1	8
Share employed in manufacturing	17.8	39.3	18.1
Average plant size	4.5	3.8	3.2
Average plant size manufacturing	18.6	9.7	6
Population density	1144.7	207.7	172.2
Density of employers	8.2	6.9	6.4
Index of civicness	81.7	83.2	77.2
Index of presence of mutual networks	4.4	6.5	6.6
Economic diversity	8.5	5.3	5.3
Index of specialisation in manufacturing	0.6	2.3	1.8
Number of local labour markets	11	156	519

Source: Di Giacinto et al., 2013.

local banks and facilitate access to credit, with positive effects on entrepreneurship when the local economy is in dire straits.

In our empirical investigation, we match micro-data from Northern and Central Italy, where industrial districts are particularly widespread (Porter, 1998), with local labour market indicators. We use quarterly data from the Italian Labour Force Survey from 2006 to 2011 and a “difference-in-differences” approach (DiD) to compare the evolution of the share of entrepreneurs before and after the 2008 recession in two groups of areas, industrial districts (ID) and other comparable local labour markets (OLM). Local labour markets, as defined by the 2001 Italian Census, are travel to work areas and IDs are a subset of these areas characterised by strong product specialisation and firm size homogeneity.<sup>4</sup>

We focus on men aged 35 to 55 working in the Northern and Central areas of Italy, the bulk of Italian entrepreneurship. Our estimates show that the share of entrepreneurs has declined to a larger extent after the 2008 recession in areas with industrial districts than in comparable areas. Measured in terms of the pre-treatment average share, the estimated differential effect ranges between 4.8 and 7.9% (in absolute value), depending on the estimation method and on the definition of entrepreneur being used. There is also evidence that this effect is larger among entrepreneurs with longer tenure in their job.

After ruling out as alternative explanations of our findings the differences across treated and control areas in industrial specialisation and composition, the propensity to export, access to credit, population density and the composition of talents, we conclude that our results are consistent with the presence of social multiplier effects, as described by Guiso and Schivardi (2007). In models where such effects are present, agents face a common problem in an uncertain environment and each agent has a piece of private information, which can be inferred from the actions of other agents. The possibility of observing the behaviour of others provides an incentive to delay adjustments in order to gather more information. Once someone acts, the information revealed could trigger further actions, and start a self-reinforcing process that prompts many agents to undertake the adjustment within a short time span. We believe that the intense social interactions typical of industrial districts facilitate information flows, thereby amplifying the effects of a shock in closely connected economies.

While entrepreneurship has declined more in ID than in comparable areas as a consequence of the economic recession, employment has increased relatively more. We also show that annual average flows from entrepreneurship to employment have increased after the start of recession in ID areas, and declined in other areas, with the bulk of the increase in the former areas occurring within the same industrial sector. We interpret this as a typical labour pooling effect, indicating

<sup>4</sup> A travel to work area is a group of municipalities where at least 75% of the resident economically active population works. According to the 2001 Census, Italy has 686 local labour markets, 156 of them classified as industrial districts.

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