

# **Is the influence of Industrial District on Internationalization Strategies eroding after globalisation? Evidence from a traditional manufacturing industry.**

## **Abstract**

This study provides insight into the impact of industrial districts on firm international strategies, in the particular context of one traditional manufacturing industry: the Spanish home-textile industry. Using a sample of 128 manufacturing firms, the paper shows how location influences intensity of exports and acceleration of exports and imports. However, our findings evidence how these influences are diluted in recent years as the home-textile industry is more involved in the global arena. Therefore, the results of the article may contradict some arguments on exploring the advantages of the district in the firm's international strategy, in particular, first, on questioning the capacity of the district to prevent international sourcing, and second, on pointing out its vulnerability to the threats created by the growing integration of the world economy.

**Key words:** districts, exports, imports, textile industry.

# **Is the influence of Industrial District on Internationalization Strategies eroding after globalisation? Evidence from a traditional manufacturing industry.**

## **1. Introduction**

The increasing engagement of firms in export and import activities has been one of the more visible answers to the constantly changing dynamics of the global environment. Nowadays, exports and imports play a vital role in company strategies and their importance is expected to grow further as markets become increasingly globalized. As a consequence, the investigation of the elements that are critical to firms' export success has been the focus of scholarly research for the last two decades (Katsikeas, Deng & Wortzel, 1996). However, research has paid less attention to the importing side. A review of 271 studies of internationalization shows that the vast majority of the empirical studies (89%) have concentrated on export behaviour and performance with very few adopting a dyadic approach (4%) (Lye and Hamilton, 2001). Nowadays, this imbalance is somewhat surprising given the importance and growth of international outsourcing (UNCTAD, 2004). In fact, in many cases, the export success is even conditioned by the international sourcing strategy of the company (Overby and Servais, 2005).

On the other hand, a substantial amount of empirical research has been developed, concentrating on the effect that various external and internal forces have on determining firms' international performance (e.g. Cavusgil and Zou, 1994; Moen, 2002). Although significant progress has been made in understanding the effect of a firm's internal factors on international performance, knowledge of the external

determinants is contradictory and warrants further research ( Madsen & Servais, 1997, Johanson & Mattson, 1988). Factors like geographical agglomerations, networks of firms or participation of local institutions have been traditionally discussed in the literature (Molina-Morales and Martínez, 2003). To date, only limited efforts have sought to explore how geographical agglomerations might favour the intensification and acceleration of firms' international strategy. Moreover, the exploration of their influence has been mainly viewed in isolation from other geographic-based trends impacting business- most notably the rapid progression of the globalization of world markets (De Martino et al., 2006). In spite of theoretical and empirical developments, generally speaking, research still consider the “industrial district effect” as static, without investigating the evolutionary patterns of industrial districts as globalization increases.

Therefore the aim of this paper is twofold. First, it aims at contributing to a better understanding of how geographical location influences the performance of the international strategy in both sides: exports and imports. To what extent do the “industrial district effect” affects import and export activities? Second, it analyse if this effect is permanent or change as firms and markets are more involved in the global arena. To what extent the “industrial district effect” is reinforce or strained by globalization? In this vein, we adopt recent claims of Becattini (2002: 489) when he asserts “...I view *districtualization* or conversely *de-districtualization*, as the constant modulation in time and space of a set of processes, and not as a punctiform event...” Moreover, the majority of studies in this field have been based on non-random case studies that describe successful stories in terms of district firms. So, we enrich this approach here using empirical evidence based on firm-level data in the specific context of one traditional manufacturing industry: the Spanish home-textile industry.

This industry is very interesting to study as with the elimination of quotas after January 2005 is facing many challenges.

The article is structured as follows. The next section of the paper develops theory and hypotheses. We then outline our study setting and methodology and present results. Finally, we point out the main conclusions and suggest implications for managers and policy makers.

## **2. Theory and hypotheses**

### *Industrial districts, international strategy and globalization*

Several studies have underlined the importance of location as key drivers of innovation and competitiveness (e.g. Porter, 1990, Steinle and Schiele, 2002). Indeed, while globalization has led to companies being configured on an international scale- with supply chains restructured across countries- geographical proximity still remains a critical feature of industrial development. Going back to Marshall (1920), by agglomerating, firms can benefit from location externalities and take advantage of specialized labour and knowledge inputs; or as recent firm strategy researchers suggested (Foss, 1996; Grant, 1996), firms located in clusters or Industrial Districts (ID) benefit from strategic resources, systemic organizational routines and collective knowledge. Competitors outside the ID will face higher costs when recruiting and relocating highly specialized employees and when transacting with suppliers and researchers. They will find it difficult to imitate the complex routines involved in the infrastructure of the district and will face more imperfect information than district firms when assessing the value of industry resources and innovation opportunities (Pouder and St. John, 1996)

But, what exactly do we mean by “industrial district”? The concept underlying ID goes back many years and goes by many different names, including “clusters”, “agglomerations”, “hot spot” and others (Cortright, 2006). Porter (1990) defines clusters as geographic concentrations of interconnected companies and institutions in a particular field. Alternatively, Rosenfeld (2002) considers a cluster as a spatially limited critical mass of companies that have some systematic relationships to one another based on complementarities or similarities. According to Beccatini (1991) an ID is a socio-territorial entity characterized by the active presence of both a community of people and a population of firms in one naturally and historically bounded area. Many others have offered their own variations, but the general idea underlying these definitions is that an ID is a group of firms and related economic actors and institutions located near one another and that draw productive advantage from their mutual proximity and connections (Cortright, 2006). Although, it is probable impossible to agree as a single, universal definition, it may be possible however to agree in the range of characteristics that identifies an ID: divisible production process, transportable product or service, a long value-chain including multiple distinct competencies, innovation-intensity and volatility of markets (Steinle and Schiele, 2002). Another important feature that characterizes an ID is the peculiar combination of competition and cooperation that occurs among the agents in the district, and which reduces the cost of using the local markets. From this point of view, for the firms located in an ID, the environment acts as a collective good as the external economies only benefit the local industrial network. The geographical proximity, the common cultural identity and the social ties facilitate fertilisation of ideas and knowledge exchange (Costa-Campí and Viladecams-Marsal, 1999). Considering these characteristics, Dei Ottati (2002) differentiates the economic

organization of an ID from that of large vertically integrated firm. In an ID, opportunism is discouraged, uncertainty is faced by flexibility and ambiguity is overcome by dividing and distributing the economic process and by splitting entrepreneurial functions.

Further empirical research on ID shows the implications of this model of organization over firms' competitiveness. For example, Molina (2001) and Signorini (1994) found higher performances for industrial district firms than for external firms. Bell (2005) demonstrated that, after controlling for networks effects, industrial district firms were more innovative than remote firms. However, the relationship that has centred most of this empirical stream is how ID can improve firms' foreign competitiveness (e.g. Porter, 1990; Costa-Campi and Viladecans, 1999; Becchetti and Rossi, 2000, Mariotti, 2004; Belso-Martínez, 2006). In general terms, these studies proved that those firms located in an ID dispose of a series of advantages that allow them to have a better international performance. Even so, the majority of this research adopts a partial view of the internationalisation as it only uses the propensity to export as a proxy that reflects the level of competitiveness and internationalisation of the companies. The approach we adopt in this paper is somewhat wider as we analyze timing and propensity of both export and import activities.

An area open to a certain degree of empirical controversy and debate among researchers is related to the considerable variety and disparity of results usually found in terms of those factors that mainly influence the performance of the international strategy. As most of the empirical research seems to be highly context-specific, almost every author in the field of International Business has aimed at elaborating their own list of such key factors. However, relationships with other business actors have always been pointed out as a crucial ingredient of international competitiveness.

The number of relationships that a firm establishes, not only with their suppliers and customers, but also with competitors and a whole series of institutions, such as local governments, universities or financial institutions, will condition their strategies. In general, this web of commercial, informative and social relationships which directly or indirectly connects the different members of an industrial district defines what we understand by a network (Johanson and Mattsson, 1988, D'Cruz and Rugman, 1992). This fact is the essence of the “*Italianate*” ID (Markusen, 1996) in which bonds of trust and associational links among relatively equal firms and institutions help drive economic activity. The relations established with the other members of the ID allow access to new experiences, resources and knowledge which could not have been obtained by acting in isolation. These factors can have a leverage effect on the firm’s ability to penetrate international markets (Welch, Welch and Wilkinson, 1998). Therefore, in those firms located in an ID, we will expect that the relationships that the entrepreneurs/managers may have established with the members of the ID will mitigate the unfavourable effect of being small and therefore will favour the international strategy.

But, how do we measure this strategy? This theoretical concept is essentially complex and multidimensional. Here, we would just claim that any effort in its operationalization should be multidimensional. As we have seen, the majority of research on ID considers that the key variable is the existence of a high percentage of exports (*intensity*). However, with the start of the new millennium, the number of young firms experiencing rapid internationalisation seems to be increasing and, therefore, a better understanding of this process would appear to be important for both researchers and practitioners (Shrader, Oviatt and McDougall, 2000). Therefore, the specific time lapsed between the moment when the firm develops its first international

activity and the moment when it was born (*speed*) adds some new information about the international performance of the firm. Moreover, we distinguish both sides of internationalization: import and export activities.

### *Hypotheses*

Most of the research has focused on the influence of the ID on the *intensity* and *speed* of exports. An efficient system of formal and informal exchange of complementary information can substitute the lack of internal resources needed to overcome fixed information costs and to provide additional services necessary to sale in foreign markets (Becchetti and Rossi, 2000). Meeting the demand of sophisticated local customers, cooperation between firms and their suppliers and competition with other district firms leads to innovation (Porter, 1990). On one hand, there is exchange information and knowledge about new processes and products with suppliers. On the other hand, firms competing with others in the same ID, they will be motivated to differentiate themselves from rivals. These reinforced processes of innovation in turns favours district firms to be more competitive in global markets than firms from the same industry but located outside the ID (Porter, 1990). Additionally, as competition is so high in an ID, district firms will look at less competitive international markets earlier than non-district firms. Bechetti and Rosi (2000) evidence how the characteristics of the ID are the basis of higher performance and export intensity of firms located in industrial districts. Pla-Barber and Escriba (2006) have shown a substantial influence of the network of relationships with customers and competitors in the acceleration of the process of internationalization.

Therefore, we hypothesize:

*H<sub>1a</sub>: In the context of one particular industry, the intensity of exports will be significantly higher for industrial district firms than for non-district firms.*



*H<sub>1b</sub>: In the context of one particular industry, the speed in developing export activities will be significantly higher for industrial district firms than for non-district firms.*

The influence of the ID effect on import/sourcing activities has been less explored. From a strategic perspective (Porter, 1990) it can be argued that capable, locally based suppliers and competitive related industries create a supportive web of local, flexible, efficient providers for district firms which in turn makes buying in the ID more interesting than internationally. Moreover, from a social and institutional perspective, social interaction among economic actors plays a role in enabling or encouraging the behaviour of managers (Granovetter, 1985). Managers are also consumers, citizens and members of the community. They are embedded in a social system (Uzzi, 1997). Consequently it is more difficult to make decisions that could change the nature of the relationships between the firm and the others economic actors in the district (workers, suppliers, institutions, etc.). These ID firms have translated to the local system a set of values and commitments that define exactly what is the role of the firm in the district and how the firm should behave. Therefore some decisions that change the structure of the value chain in the district such as re-localisation of the labour-intensive activities in low-cost countries, international outsourcing, and downsizing are not “allowed” or at least delayed.

Some empirical studies in the Italian Districts show how district firms exhibit a higher degree of internationalisation in terms of exports and a lower degree in terms of delocalization in comparison with firms that do not belong to the district (Centro Studi Unioncamere, 2002). This fact could confirm their embeddedness in the local context (Mariotti, 2004)

Thus:

*H<sub>2a</sub>: In the context of one particular industry, the intensity of imports will be significantly lesser for industrial district firms than for non-district firms.*

*H<sub>2b</sub>: In the context of one particular industry, the speed in developing importing activities will be significantly lesser for industrial district firms than for non-district firms.*

There is a general agreement that ID exhibit a life cycle, which draws from “industry life cycle” Theories (Vernon, 1966). Because of continual changes in markets, technology and competition, clusters tend to evolve continually, with some ID ebbing or dying even as new ones form and grow (Cortright, 2006). However, from a more radical point of view, some authors argue that the advancement of globalization have signalled the “death of distance” and reduced drastically the importance of localization (De Martino et. al, 2006). The rationale is that globalization weakens the intimate, embedded relationships associated with ID. As firms are more involved in the global arena, they often reduce their degree of local collaboration and interaction. Globalization eases the access to outside resources and, in turn, firms reorient their degree of intra-cluster vertical and horizontal relationships. Moreover, some researchers suggest that during periods of rapid technological change or intense global competition Industrial Districts can gain competitive advantages through selective linkages with external firms and/or clusters. Without this external interaction, the local ID could suffer from intellectual “lock in” hindering the region’s ability to successfully adapt to new changing environments and hasten their decline (De Martino et.al, 2006). This is particular the case in traditional manufacturing industries such as textile where knowledge-based inputs are not longer location- bound.

Therefore:

H3: *In the context of a traditional manufacturing industry, the industrial district effect over the international strategy will have less importance as globalization increases.*

### **3. Methods**

#### *Sample and data collection*

We collected the data from the Spanish home-textile association. Nowadays, the home-textile industry- like other traditional manufacturing industries- is considered as an example of an industry with structural problems in more advanced economies due to severe competition from low-wages countries. As a result, industrial countries are losing their comparative advantage in the production of such goods. Although for many years the Spanish textile industry was growing, the data of the last five years shows a similar –or even worse evolution- than the European average. We can observe from the data a shrinking number of establishments and employees, reduction of output, and a clear stagnation of exports.

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Insert Table 1 about here  
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The Spanish home-textile association had 570 members at the time the research was carried out. The survey instrument consisted of an extensive mail questionnaire, which was pre-tested through personal interviews with Spanish executives responsible for international operations and with academics specialized in international management. The questionnaire was mailed to senior-level managers who were most likely to be involved in the internationalization process, including CEOs or directors in charge of international operations. The use of CEOs and international directors satisfies two accepted criteria for identification of appropriate key respondents: (1)

possession of sufficient knowledge of the domain being studied, and (2) adequate level of involvement with regard to the issues under investigation (Campbell, 1955). The survey was launched during the first week of June 2005. The questionnaire was largely sent by e-mail and by fax, together with an introductory letter from the association describing the objective of our research project and emphasising the confidentiality of the responses. Questionnaires were sent out in three general rounds. After four months, we obtained a sample of 128 firms, representing 22,5% of the target population.

### *Measurement of variables*

*Industrial district.* We focus on the Spanish home-textile district. This district is located around the cities of Alcoi-Ontinyent (South Valencia). It is a natural and historically bounded area that fits Becattini's definition. This district has its roots in the nineteenth century and experienced a strong development in the period 1961-1975. Nowadays, it represents 69% of the total Spanish home-textile production. The district has a web of capable providers from supporting and related industries. Moreover, a great number of public and private institutions that offer support and services to the district firms are located in this area. Particularly important are research and public institutions (e.g. the Technology Institute of Textile, Valencian Institute of Small and Medium Sized Companies), academic institutions (the University of Valencia, Polytechnic University of Alcoi) and trade associations. We identify this industrial district following Sforzi's quantitative methodology (Sforzi, 1992), but it has also been identified as an industrial district (close to the *Italianate district* model) by a number of other studies (e.g Ybarra, 1991; Cluster Competitiveness, 1999; Piqueras, 1999).

*Export intensity* represents the share of exports in total sales for a particular firm.

*Import intensity* is the share of imports in total purchase for a particular firm. These variables are by far the most widely used indicators in empirical international business research.

*Export and Import speed* was measured by the time lapsed since the year firms were founded until the first year of exporting or importing.

Table 2 shows the correlation matrix and some descriptive statistics.

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Insert Table 2 about here  
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### *Analyses*

We used ANOVA to compare means of the international strategy measures. *t* Tests showed whether these mean values were or were not significantly different. In order to apply ANOVA analyses, original data were transformed into log. variables. These new variables follow a normal distribution.

By using the firm's address, we split the sample in two groups: industrial district members and non-members. Table 2 shows the results for the whole sample.

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Insert Table 3 about here  
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To verify whether the historical context (globalization) in which the firms were created had any influence on the international strategy, two new analyses were run: a) for the firms created before 1985, b) for those created since 1985. The latter year was considered to be a significant historical watershed, as Spain joined the European Union at the end of this year. Moreover, in the second half of that decade, Spanish industry experienced definitive advancements in its level of specialisation, as of 1985, when it reached an equivalent production capacity of 96% of its consumption. This

progression came about as an overall consequence of the forceful propensity to export. Figures doubled in only a decade, substantially improving the commercial balance of the country.

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Insert Table 4 and table 5 about here  
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### *Results and discussion*

First, we analyse partial correlations. The most noticeable was that total experience was significantly correlated with years lapsed until export and import time. Older firms started to export and import later than younger firms. Nowadays, firms are likely to encounter international pressures much earlier in their existence. This result would appear to confirm recent claims (Madsen and Servais, 1997, Moen, 2002) which are based on the growing globalisation of markets and which question the relevance of experience, especially in explaining the internationalisation process of young firms located in industrial districts. On the other hand, size is not correlated with export and import intensity. Firm size is not a barrier for internationalizing firm activities: small firms could do well in international markets as long as they implemented internationalisation strategies consistent with their resources. This is especially relevant for firms located in industrial districts where the economies of agglomeration can substitute for the lack of internal resources needed to overcome the cost of entering foreign markets.

Second, we analyse  $t$  Tests. In general terms, district firms are more active in exports markets than in import markets. There is no statistically significant difference in terms of import intensity between district firms and non-district firms.

Moreover, district firms seem to show a more accelerated pattern of internationalisation than non-district firms, in both strategies: exports and imports.

However, the statistically significant relationships appear when we consider the sample of firms created before 1985. If we just only consider firms created after 1985, differences in means are not statistically different for all variables. Therefore, this provides support for hypotheses 3. Globalization is eroding the district effect on the internationalization strategies. The hypothesized positive district effect on the intensity and speed of exports seems to be less important as globalization increases. On the other hand, the influence of localization on imports is the contrary as we hypothesized. The speed of import is higher for district firms than for non-district firms, at least, for firms created before 1985. This fact could be due to learning effects. District export firms learn earlier how to deal with foreigners which in turn accelerated the process of purchasing outside. However, in general terms, the intensity of imports seems to be the same in firms located inside or outside the district. The hypothesized preventive effect of the district against international sourcing is not so important. As district export firms internationalize, they gain additional capabilities and often reduce their degree of local dependence and interaction. Therefore we can not accept hypotheses 2a and 2b.

Overall, our results show how location influences intensity of exports and acceleration of exports and imports. Moreover, the paper evidences how these influences are diluted in recent years as the home-textile industry is more involved in the global arena.

#### **4. Conclusions**

The study has sought to provide insight into the impact of industrial districts on firm international strategies. Few studies have examined the implications of being located

inside or outside Industrial Districts on the speed and intensity of both exports and imports.

The findings of the article may contradict some arguments on exploring the advantages of the district in the firm's international strategy, in particular, first, on questioning the capacity of the district to prevent international sourcing, and second, on pointing out its vulnerability to the threats created by the growing integration of the world economy.

We have show how traditional manufacturing Industrial Districts are currently strained by global pressures which are influencing their evolution and future. In this sense, the paper contributes to the literature on industrial districts' evolution showing an empirically explorative look at the economic phenomenon of districts' decline. In fact, wider analyses of data in different traditional manufacturing industrial districts (see for example, Mariotti, 2004; Amighini and Rabellotti, 2006) show a pessimistic picture: losses of jobs and rise of unemployment, losses of market shares by district suppliers, increasing transfer of specialized knowledge outside the local system, changes in inter-firm relations, social problems and so on.

Insights from the decline of Industrial Districts might be useful for policy makers in order to promote changes in favour of equilibrated *relocations* where the transformation of the local social capital in a more complex and articulated system able to sustain long distance relationships could enlarge the boundaries of the district into nodes of a wider international system. Non-local external networks may enable Industrial Districts to overcome local inertia and hence extend the district life cycle. In this vein, we will observe an increasing tendency in district firms to delocalise their production activities abroad while they will keep product design, marketing, innovation and quality control within the local system. Efficient policies supporting



these core activities could help district firms to survive. This tendency as Mariotti (2004) point out, could be seen as an opportunity for enlarging the local system through the creation of new clusters in foreign countries and specialising the original district in high value-added activities.

Nevertheless, the notion that Industrial Districts reduces their degree of importance on the internationalization strategies as firms mature and grow internationally does not, however, necessarily imply that overall industrial districts interactions are reduced over time. The foundation of new business, the ratio of innovations, the establishment of a collective positive reputation or image, the development of shared values and training, etc. represents common attributes associated with industrial districts.

The limitations of our study may provide ideas for extension and improvement. First, our study has benefited from dealing with firms in a homogeneous technological setting. However, it must be stressed that single-district conclusions should be considered with caution. Further research including industrial districts with different technological features is needed to provide further empirical assessment of the district's influence on the internationalization strategies. Moreover, some factors identified in the literature as relevant on the influence on international performance such as export subsidies, innovation or modes of entry have not been considered in this study.

Despite these limitations, we consider that the paper contributes to support with a simple statistical analysis the view of a stagnant evolution of industrial district firms in a traditional manufacturing industry; it consequently illustrates an exemplary case that can help future research in this field by serving as a reference for studies with a broader scope.

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**Table 1: The Crumbling Industry Evolution 2001-05**

Aggregated indicators	UE	Spain
Export/Import	-5,2%	-16,7%
Loss of Output production	-11,2%	-23,4%
Loss of Employment	-15,2%	-19,1%
Loss of establishments	-28%	-14%

Source: own elaboration based on CITYC (2006) and INE (2006).

**Table 2: Correlation matrix and descriptive statistics**

		Mean	SD	1	2	3	4	5
1	Years since foundation (Total experience)	25,25	16,77	--				
2	Size	45,95	78,54	<b>**0,442</b>				
3	Export Intensity	35,51	28,26	-0,067	0,059			
4	Years lapsed until export	10,98	11,92	<b>**0,751</b>	<b>**0,279</b>	-0,141		
5	Import Intensity	25,03	21,71	-0,122	0,099	0,120	-0,053	
3	Years lapsed until import	13,08	11,62	<b>**0,673</b>	0,165	<b>*-0,232</b>	<b>**0,576</b>	-0,191

**Table 3: District-effect (the whole sample).**

	Mean		Statistics		N
	NDF	DF	Anova	Levene	NDF-DF
NDF: non-district firms					
DF: district firms					
Export Intensity	31,58	38,51	<b>*0,068</b>	0,134	57-75
Years lapsed until export	14,51	8,29	<b>**0,016</b>	0,575	57-75
Years lapsed until import	26,55	23,77	0,838	0,130	40-48
Import Speed	17,05	9,77	<b>***0,007</b>	0,243	40-48

$p < 0.10$ ; \*\*  $p < 0.05$ ; \*\*\*  $p < 0.01$

**Table 4: District-effect (firms created before 1985)**

	Mean		Statistics		N
	NDF	DF	Anova	Levene	NDF-DF
NDF: non-district firms					
DF: district firms					
Export Intensity	30,30	37,58	<b>**0,041</b>	0,011	39-44
Export Speed	18,72	11,91	<b>*0,077</b>	0,493	39-44
Import Intensity	22,00	21,76	0,624	0,114	25-26
Import Speed	24,32	13,19	<b>***0,001</b>	0,216	25-26

$p < 0.10$ ; \*\*  $p < 0.05$ ; \*\*\*  $p < 0.01$

**Table 5: District-effect (firms created between 1986-2005)**

	Mean		Statistics		N
	NDF	DF	Anova	Levene	NDF-DF
NDF: non-district firms					
DF: district firms					
Export Intensity	34,33	39,83	0,677	0,674	18-31
Export Speed	5,39	3,16	0,215	0,442	18-31
Import Intensity	34,13	26,13	0,328	0,484	15-22
Import Speed	4,93	5,73	0,801	0,626	15-22

$p < 0.10$ ; \*\*  $p < 0.05$ ; \*\*\*  $p < 0.01$