

The untapped potential of “beautiful and well-made” consumer goods on international markets

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- ◆ **Made in Italy: a success story** Italy is among the top 10 in the global ranking of exporting countries, coming in the seventh place. This position applies to a highly diversified basket of goods: Italy comes at the very top in terms of balanced distribution of exports among the various products. When we restrict the focus just to consumer goods, Italy comes third after China and Germany.
- ◆ **What does the label “Beautiful and well-made” (BBF) stands for?** The concept of ‘beautiful and well-made’ as an expression of Italy’s uniqueness (BBF, from the Italian expression “bello e ben fatto”, literally translated as beautiful and well-made) embraces all those products that exemplify Italian excellence in terms of design, attention to detail, high-quality materials and careful manufacture.
- ◆ **BBF is worth €86 billion...** BBF products represent 15.6 per cent (2018, last available figure) of Italy’s total exports and are spread across all the main sectors of Made in Italy, although predominantly in the so-called three-Fs – Fashion, Food and Furniture. Italian products of excellence go mainly to advanced markets, which overall take up some three quarters of them, equivalent to just under €70 billion. The remaining quarter is exported to the emerging countries, which owing to their rapid growth (both demographic and economic) and despite their still lower weight, offer relatively greater scope for expansion, even though the risks remain higher.
- ◆ **... and has an untapped potential of nearly €45 billions more in the future** This potential is calculated by estimating how much current market shares could increase with respect to those of competitors similar to Italy as regards production cost structure and product quality.
- ◆ **The implementation of the three following strategies to reach the potential:** 1) encouraging future EU agreements to enhance trade and alleviate uncertainty due to exacerbating protectionism tensions; 2) fostering the use of e-commerce among Italian BBF brands; 3) strengthening the measures against counterfeiting of Italian BBF products.

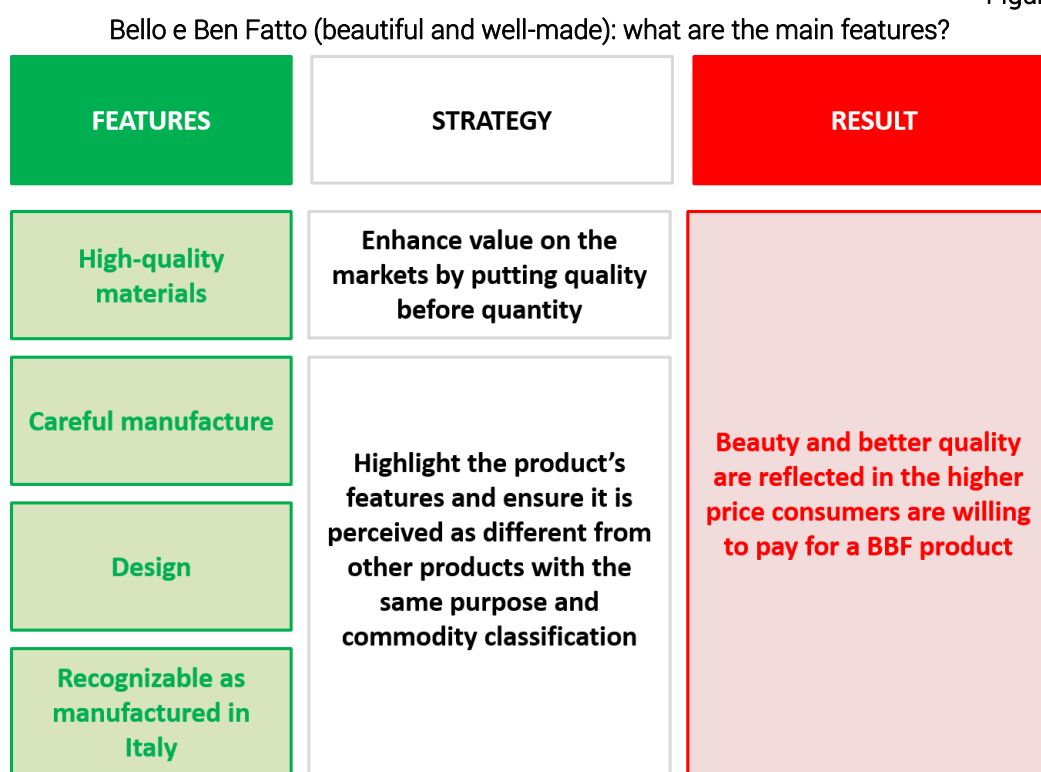
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1. What goes under the label of “Beautiful and well made”?

The concept ‘beautiful and well-made’ as an expression of Italy’s uniqueness BBF (bello e ben fatto, literally translated as beautiful and well-made) embraces all those products that exemplify Italian excellence in terms of design, attention to detail, high-quality materials and careful manufacture. Such goods exist in all branches of production, but the majority of them can be found in sectors more closely linked to aesthetics and creativity. In this respect, BBF is the most recognisable expression of the Made in Italy brand, encompassing the best-known features of the Italy’s cultural heritage, traditions, landscapes and works of art and helping to build an image of Italian manufacture (Figure A). In this respect, BBF products not only represent a large share of Italy’s world exports, they also drive all Italian exports as their value goes way beyond the purely economic one.

Figure A



BBF products encompass all the consumer goods of excellence that Italy is able to export at high prices (Figure B). BBF describes a whole group of products that offer a distinctive Italian value added, thereby achieving higher prices than competitors’ goods on the international markets. Such a group is identified through a succession of phases that are described below.

Starting from this initial perimeter consisting of final goods, we can identify the subset of BBF products simply by focusing on the aggregate of all the goods that Italy sells abroad with the benefit of a ‘quality premium’. Specifically, BBF goods are those whose average unit value (AUV) is equal to at least the 75th percentile of world distribution (i.e. the highest quartile). A few

examples suffice to clarify the concept of BBF: high-quality food products made using fish, wine and other spirits; essential oils or other cosmetic products; hides and leather industry goods such as bags, gloves and belts; Made in Italy clothing, spreading the BBF emblem around the world via the fashion industry; household goods that rely increasingly on elements of good interior design; furniture, lamps and even mattresses; yachts and boating products, often incorporating other BBF goods which they constantly showcase; and also watchmaking and other high-tech and precision instruments sold directly to final consumers.

The procedure to delimit the perimeter of BBF starts by observing the individual six-digit Harmonized System codes from the 1996 edition; from these we exclusively select those categories of goods that are considered final consumer goods according to the Broad Economic Categories (BEC) classification. Finally, the BBF perimeter is defined by considering only those goods that Italy manages to export with average unit values equal to or greater than the 75th percentile, i.e. in the highest quartile (Figure C).

Figure B

BBF: consumer goods of excellence exported by Italy

(Hypothetical frequency distribution of car exporters by level of average unit values)

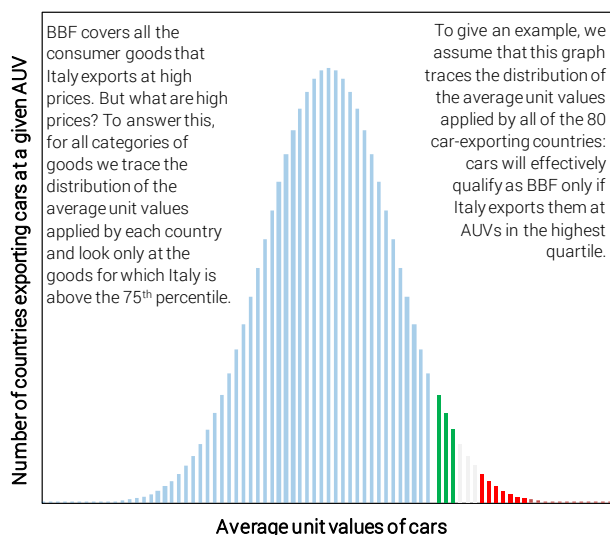
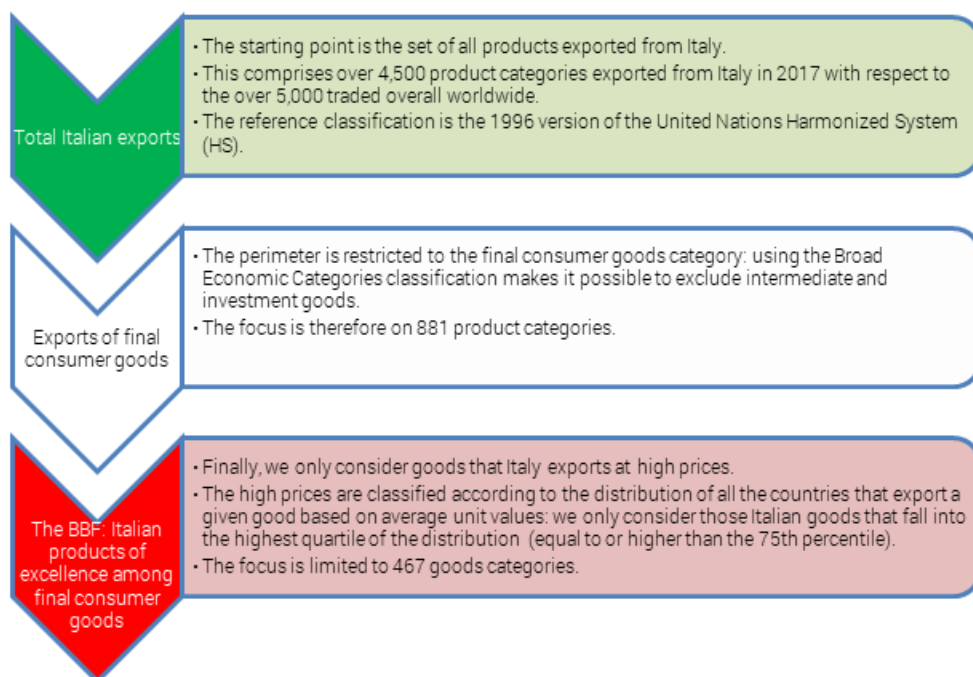


Figure C

Delimiting the perimeter of BBF in three steps



2. BBF exports: recent trends and key competitors

BBF products have recovered rapidly compared with the pre-crisis period

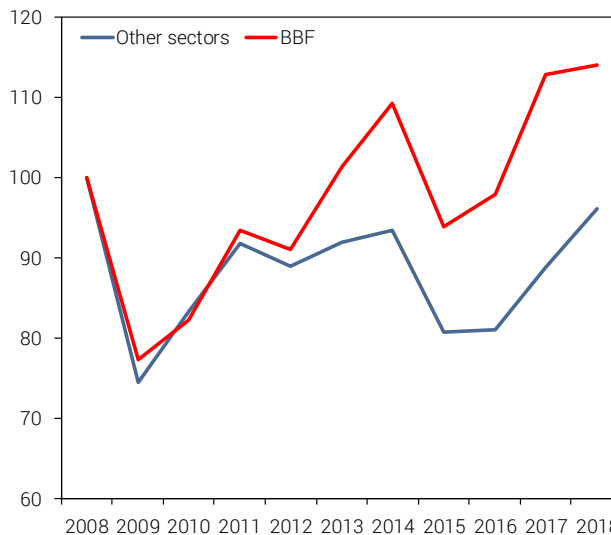
Starting in 2011, high-end consumer goods exported from Italy have recovered more quickly than other goods. While in 2018 other Italian export sectors were still at 96 per cent of the peak level recorded in 2008, the BBF aggregate was already 14 per cent higher than the pre-crisis export level (Figure D). The more rapid recovery may be due to the different type of target consumer for BBF goods. The target customer is typically upper middle class, a customer base that has continued to grow thanks to demographic and economic trends in emerging countries.

In general, this type of goods is intrinsically less affected by the consequences of a fall in demand during a crisis, because the target consumer has a higher income on average. The five emerging markets with the largest number of wealthy consumers are China (175 million), India (70 million), Russia (30 million), Brazil (28 million) and Indonesia (23 million). Overall, the market consists of more than 460 million potential consumers.

The key to success? Quality over quantity

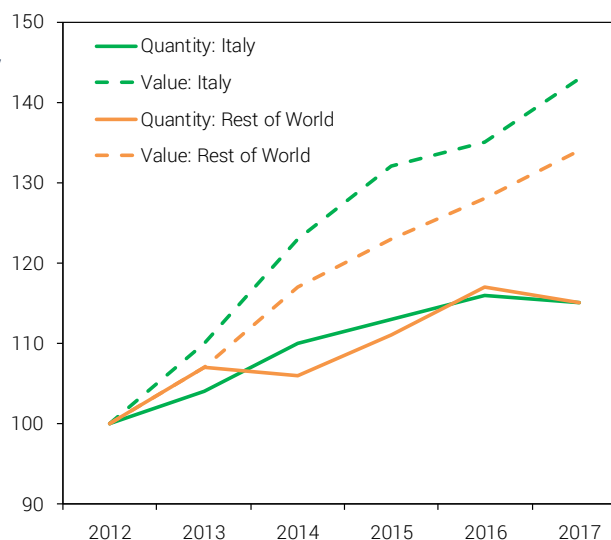
The results obtained in the BBF sector are mainly due to the quality of the goods. These goods are often produced in limited quantities or as niche products and are intended for a more informed type of consumption that is less dependent on the elasticity of demand with respect to the price. These goods, while comparable in terms of functionality and merchandise category to other goods sold at much lower prices, are perceived as having a value that makes them distinct and

Figure D
The reactivity of BBF products after the crisis
(Italy, exports in billions of current dollars, 2008=100)



Source: calculated by CSC and the Manlio Masi Foundation based on UN-Comtrade data.

Figure E
The higher quality of BBF products
(Exports: current dollars and quantities in tonnes: base year 2012=100)



Source: calculated by CSC and the Manlio Masi Foundation on UN-Comtrade data.

incomparable, and are often associated with an emotional value that tempers any reasoning based solely on economic rationality. Figure E illustrates the trend in BBF exports in terms of quantity and value over the period 2012-17 (including the global BBF market, which is the sum of BBF exports produced by each country). Setting the value for 2012 at 100, exports of Italian BBF products performed much better in terms of value than BBF exports from the rest of the world over the entire period, while the trends were similar with regard to quantity. To the extent that average unit values reflect a 'quality effect', this outcome demonstrates that, during the reference period, Italian exporters increased the average value of their BBF products in comparison with the rest of the world. Against a backdrop of intense international competition, this greater ability to 'set the price' is associated with an increase in the quality of exports.

Which are Italy's main BBF competitors? To answer this question, the perimeter of the foreign BBF market must first be identified in order to compare it with Italian BBF exports. The same products found in the Italian BBF sector are exported by many other countries to international markets; however, these products do not always fall within the country's BBF sector (i.e. products with an AUV above the 75th percentile of the price distribution for that product) and therefore may not directly compete with Italian BBF products. What makes BBF products immune from stiff competition in terms of volume, especially from China, is the distinct qualitative element which places them in a market context that differs from that of the other products that are formally classified in the same merchandise category. In fact, these products make their own market in protected niches that have a limited number of competitors, sold mostly in advanced countries with cost structures that are more similar to that of Italy.

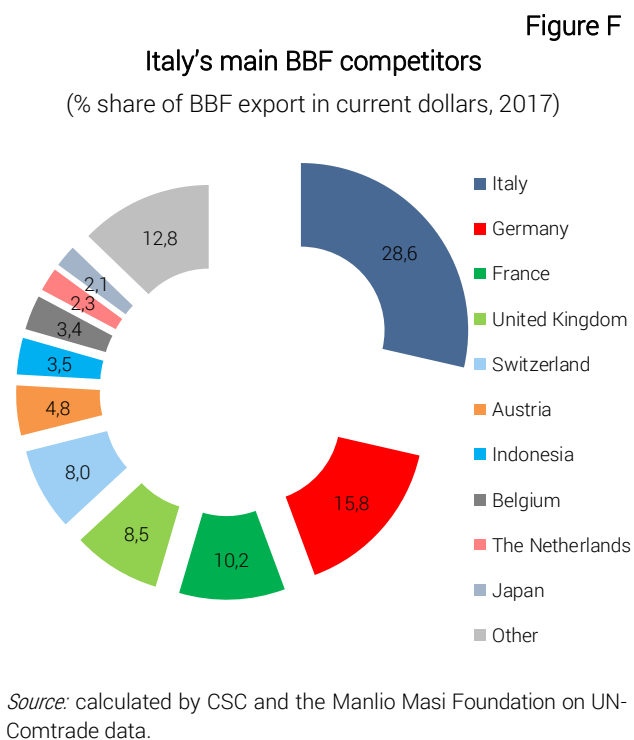
This implies that, even though two products are in the same merchandise class, there is a significant difference between an article of clothing produced with low-quality materials and one that is produced using high-quality materials and careful craftsmanship. Not only do the two products have different characteristics, but their consumption is driven by different types of considerations: the first is more tied to a price rationale while the other to the level of quality. Therefore, it is important to differentiate between competition from other countries within the BBF context (where the focus is on the final consumer, quality and the emotional value placed on the product by the consumer) from competition that stems from products that are not high-end and meet a demand that differs from that of BBF products and, hence, have a lower price point.

Figure F illustrates the market share of Italy's main competitor countries as regards the BBF products exported by Italy. Some BBF-exporting countries, such as Italy's main European partners and Japan, have a production structure that is similar to that of Italy; the only emerging Asian country that is comparable is Indonesia, especially referring to its textile-apparel and its footwear sector.

Competition from emerging Asian countries such as China or Vietnam, which in recent years has posed a big challenge for Italy's productive system, is less significant vis-à-vis BBF products. Indeed, these countries are very big exporters of the non-BBF goods considered herein and are not among the main exporters of accessible luxury products. However, this situation may change: if Asian producers are able to improve the quality of their exported

products, and start to directly compete in BBF market segments, their already developed presence in destination markets could serve as a significant advantage.

Germany is Italy's main competitor in a large number of markets. It is a country whose products have a cost and quality structure that is comparable to that of Italian products, albeit with some differences: in the boating industry and electronics sector, German AUV is higher than Italy's, while in the textile and clothing sector, Italy has the higher AUV. Compared with France, Italy instead competes in a smaller number of markets (mainly Germany, the United Kingdom and Spain), but with a similar composition in terms of sector and pricing. Specifically, it competes with France in the traditional BBF sectors: food, textile and clothing, and leather goods.



3. The potential of BBF exports

In this section we analyse the potential market for Italy's BBF exports. In this context Italy is well positioned on international markets and its BBF firms are very competitive and are often leader in their respective fields. Nevertheless, there are plenty of markets in which Italian firms are outperformed by competitors with similar characteristics. Therefore, it is important to understand how Italy can further increase its exports.

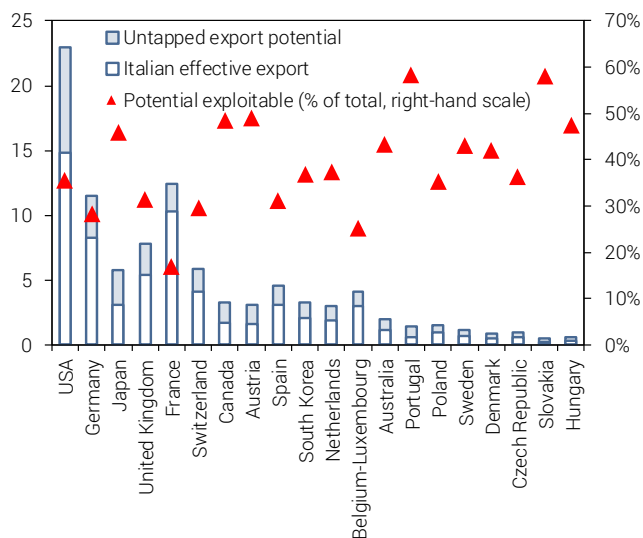
Untapped export potential: a measure of the export growth that may be achieved given the performance of Italy's most similar competitors For each of the more than 467 Italian BBF products and for each destination market, we have identified exporting countries that, having characteristics similar to those of Italy, are able to achieve better export results. The factors taken into consideration in comparing the different exporting countries are based upon the principal measures adopted in the economic literature and include per capita income, prices (average unit values), degree of specialization, degree of diversification of exports, substitutability of goods exported, market shares and geographical distance. Using this data, it is possible to construct a measure of the additional exports that could be achieved by comparing Italy's performance with that of its most similar competitors. The existence of a positive differential between potential exports and actual exports indicates that there are growth margins in penetrating foreign markets.

The United States is the market with the highest potential in absolute terms, with €8.2 billion in potential additional exports

Figure G shows the export potential for BBF in the main advanced markets. From the Figure we can observe that the high growth potential in the US largely depends on the size of the market. It is possible to increase exports to the US not just because of the characteristics of Italy's commodities, but also because a small improvement in our ability to penetrate the US market would mean a significant increase in exports. The Figure shows four other countries of interest: Germany (€3.3 billion in potential additional exports), Japan (€2.6 billion), the United Kingdom (€2.5 billion) and France (€2.1 billion). The interest in these countries derives from the fact that they are relatively large and rich, as well as close from a geoeconomic and cultural point of view.

Figure G
US key market for the high export volume, large margins of improvement in Canada and Japan

(Actual and potential BBF exports in bln of euros, 2018; the countries are listed in order of exploitable potential)



Source: calculated by CSC and the Manlio Masi Foundation on UN-Comtrade data.

The analysis points to ample potential that can still be exploited, just under 50 per cent of the total for Canada and Japan and 40 per cent for South Korea. Austria is also a country of interest (€1.5 billion in exploitable growth potential), even if it is not a particularly large market, because it is wealthy and it borders Italy. The analysis reveals that Italian exporters are under-represented in Austria, but they could attain better results given the characteristics of similar competitors. In this market, for historic and linguistic reasons as well, Italy suffers from the strong presence of Germany. It is difficult, by comparison, to assess Italy's potential in the United Kingdom, which is an important market for Italy in terms of both potential and actual exports. Obviously there is still a high amount of potential to be exploited, but the possibilities for translating this into actual exports is strongly hindered by the uncertainty surrounding Brexit and the performance of the pound sterling. Recent events give us hope that at least the uncertainty will dissipate in early 2020, but the possible consequences are not yet clear.

Overall, with regard to the advanced markets, the analysis indicates that the growth margins are larger in countries in which Italian exports have traditionally been under-represented, that is, in markets where the export potential has not yet been adequately exploited. This is often the case for relatively small markets, such as Portugal (€0.8 billion in possible additional BBF exports) Slovakia (€0.3 billion) and Hungary (€0.3 billion), to which Italy could export more given its characteristics.

Italian BBF exports in emerging markets are much less than those in the advanced markets This phenomenon is somewhat normal, and is partly due to the fact that advanced countries have larger markets in which consumers have greater disposable income, and also because of the more limited presence of Italian exporters. Figure H shows the actual and potential exports for Italy in the main emerging markets; the countries are ordered by export potential in billions of euros so as to emphasize the markets that are most promising in absolute terms.

The top emerging market for export potential is China, with €3.3 billion in possible additional exports This is due in large part to the size of the market. It should be noted that

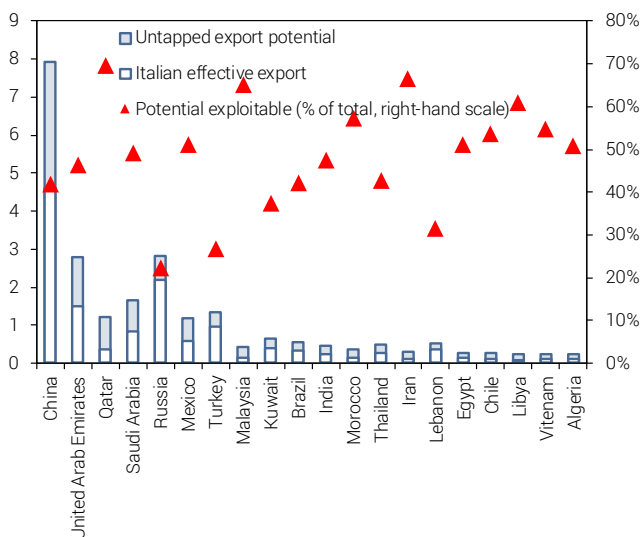
BBF growth potential is very high: it is more than 70 per cent of the amount already achieved (€4.6 billion). In comparing China with the US (see Figure H), it is worth noting that the untapped potential (i.e. the additional exports that can be obtained) reflects the difference in the economic size of the two markets: actual BBF exports to the US are slightly more than three times those to China (almost €14.8 billion compared with €4.6 billion), while the untapped potential follows a factor of 2½ (is €8.2 billion in the US compared with €3.3 billion in China). In the emerging markets, Italy still has relatively small market shares which can grow, and there are competitors with characteristics that are similar to those of Italy who have recorded better results

in exporting BBF goods. In addition, the emerging economies are often more dynamic and economic development and growth are generally higher than those of the mature economies, such that new opportunities open up year by year.

The United Arab Emirates, Qatar and Saudi Arabia: BBF export potential worth almost €3 billion The growth margins for BBF exports are very high in the United Arab Emirates (€1.3 billion), Qatar (€0.8 billion) and Saudi Arabia (€0.8 billion). The Italian BBF sector could practically double its presence in terms of export volumes in these markets.

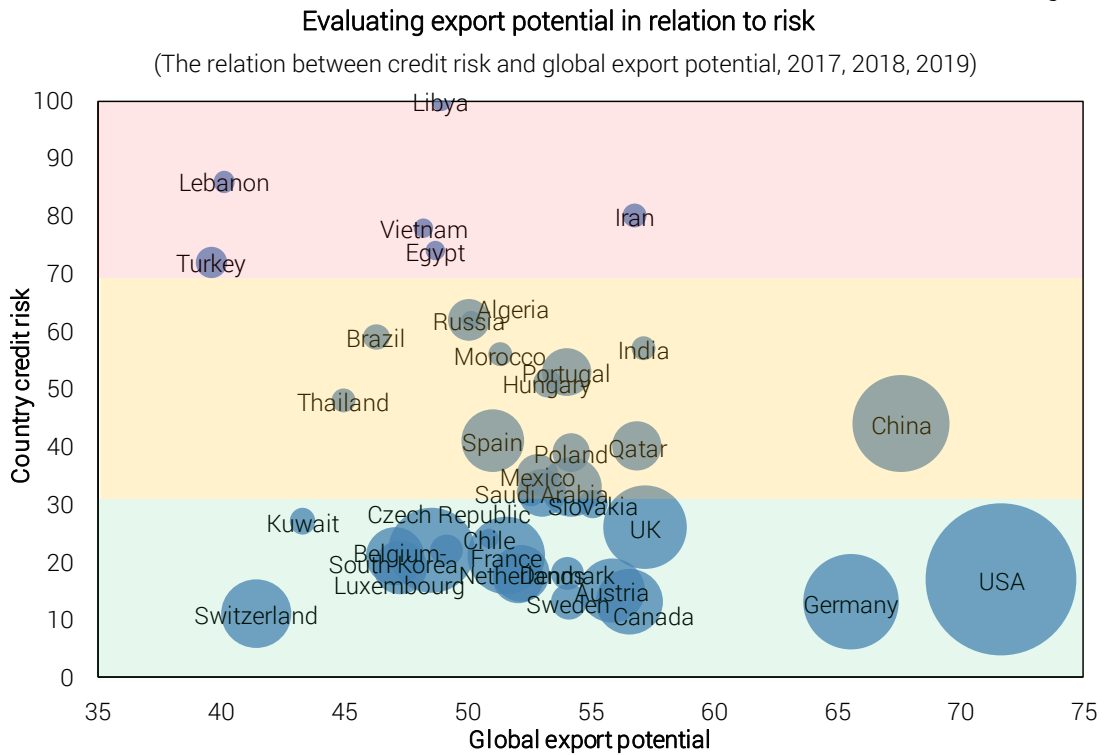
In some of Italy's key partners there are risks to achieving export potential The analysis of export potential is accompanied by an analysis of the risk that each market presents (Figure I). Clearly, this type of representation (risk-potential) aims to offer a simple interpretation of the results, and in a complex world it is important to avoid drawing clear-cut conclusions. First, the

Figure H
Large potential in China and the Middle East
(Actual and potential BBF exports in bln of euros, 2018; the countries are listed in order of exploitable potential)



Source: calculated by CSC and the Manlio Masi Foundation on UN-Comtrade data.

Figure I



Note: the credit risk indicator calculated by SACE (Italian export credit agency) is the result of the average of the risk of non-payment by sovereign, corporate and banking partners to which an Italian exporter is exposed in a given market. The indicator is based on a point system ranging from 0 (minimum risk) to 100 (maximum risk).
 Source: calculated by Centro Studi Confindustria and Fondazione Manlio Masi using data from SACE-SIMEST and ExPANd.

averages are the outcome of a variety of information. For example, while there may be certain types of risks and opportunities at the aggregate level, some partners or sectors could move against the trend. Consider China, which offers a high degree of reliability as a sovereign partner, but increased risk in the case of transactions with banks and non-financial companies because of their notoriously high debt level. A similar argument applies to Russia, where very sound public finances contrast with the possibility of problems in some corporate sectors and in the banking industry. There are other emerging countries that are important trade partners of Italy, such as Brazil and India, whose macro-economic fundamentals indicate that they are unlikely to experience the crises that overtook Argentina and Turkey in 2018, but which on the other hand need to be approached with caution. In Argentina, for example, the public debt has ballooned recently and economic growth is still weak, with all this that entails for business. In India, the banking system is experiencing problems owing to the increase in accumulated bad debts in recent years. Yet both markets are still strongly protected. The economic situation in other major destinations for Made in Italy products is fairly negative for a variety of reasons (Iran and Turkey): it will be some time before they once again offer greater export potential and less risk. The global situation is in constant flux, with the result that the outlook for some countries and sectors may change rapidly. The group of advanced countries that represent the most promising outlets for Italian BFF exports is also the group presenting the least risk.

In synthesis: which are the best markets to target? The way to achieve the potential for export growth is through commercial penetration of the countries and sectors with the greatest scope for expansion. This is a game to be played on several boards at once, with different opponents depending on the geographical areas and sectors concerned. The aim of this Report is to provide an overview of the ones worth taking on and the type of competition encountered there.

Table A illustrates, for the top five advanced countries and the top five emerging countries in terms of export potential, which sectors are the most important, which countries are Italy's main competitors in those particular markets, and what factors determine the amount of export potential (specifically: size of margin to be exploited compared with existing level, market growth, compatibility of demand structure in the destination markets with supply structure of Italian BBF products).

The driver of exports in the advanced countries is the notable presence of shared tastes and standards, reflecting very similar cultural contexts. These are also the main countries with

Table A

The countries with the greatest potential for Italian BBF products*

(Ranking of the top 5 advanced countries and top 5 emerging countries according to Italy's export potential in billions of euros)

Country	Potential (bn euros)	Main sectors	Main competitors by country/sector
TOP FIVE ADVANCED COUNTRIES			
US	8.2	Wood and furniture Tanning and leather Motor vehicles Textiles-clothing	China, Canada, India China, France, India UK, Germany, Japan China, Indonesia, India
Germany	3.3	Footwear Electrical eng. and electronics	China, Poland, Spain Belgium-Luxembourg, UK, South Korea
Japan	2.6	Textiles-clothing	China, Indonesia, India
United Kingdom	2.5	Glass and ceramics Boating**	Spain, Portugal, France Netherlands, Spain, Germany
France	2.1	Food and beverages	Spain, Germany, Netherlands
TOP FIVE EMERGING COUNTRIES			
China	3.3	Chemicals, pharm. and cosmetics Electrical eng. and electronics Motor vehicles Food & beverages	France, UK, Japan USA, Canada, UK UK, Japan Spain, South Korea, Japan
United Arab Emirates	1.3	Tanning and leather Textiles-clothing Footwear	France, India, Greece China, India, Bangladesh China, Netherlands, India
Qatar	0.8	Boating**	Germany, Bahrain, UAE
Saudi Arabia	0.8	Wood and furniture Glass and ceramics	China, Germany, USA Spain, Egypt, China
Russia	0.6	Tanning and leather Footwear	China, Greece, Germany China, Germany, Turkey

* The growth potential and the main competitors for each market are identified using the Export Potential Analysis and Development (EXPAnD) methodology of the Fondazione Manlio Masi, which was developed by Tullio Buccellato and Enrico Marvasi as part of a research project begun in 2012 and coordinated by Beniamino Quinteri.

** Data on the boating sector reflect distortions caused by transits in logistic hubs. Hence the figure for the UK may conceal purchases by other countries as well. In the case of Qatar, too, the fact that the two main exporters to this destination are Arab countries might be due to transits via logistic hubs.

Source: calculated by Centro Studi Confindustria and Manlio Masi Foundation based on UN-Comtrade data.

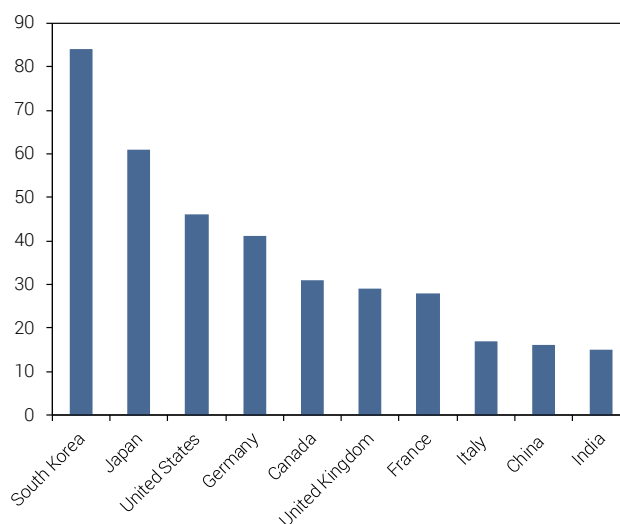
which Italy has economic, political and strategic relations, and hence particularly close geo-economic ties. The most important countries are the United States (€8.2 billion), Germany (€3.3 billion) and Japan (€2.6 billion). Among the emerging economies, the main markets are China (€3.3 billion), the United Arab Emirates (€1.3 billion), Qatar (€0.8 billion), Saudi Arabia (€0.8 billion) and Russia (€0.6 billion). The United States, China and Germany are without doubt the leading markets for export opportunities, but for different reasons: China because of its size and growth, Germany because of the compatibility between demand and supply, and the US owing to a balanced combination of both factors. The margin for improvement in exports to Japan, which is large in absolute terms, is offset by the fairly limited growth prospects of import demand.

4. The key challenges for achieving potential

The importance of virtual shop windows: Italy should increase its e-commerce sales

Although Italy is one of the top ten countries in terms of online sales, it lags behind the e-commerce sales of its main competitor countries, which are also its main outlet markets. Italy's online sales account for 17 per cent of its GDP, more in line with China (16 per cent) and India (15 per cent) than with the other advanced economies, which vary between a range of 84 per cent for South Korea and 28 per cent for France (Figure J). BBF products must be advertised on dedicated websites that are capable of highlighting the features that distinguish them from similar non-BBF products and, more importantly, from counterfeit goods. Moreover, according to the e-commerce observatory of the Politecnico di Milano, the highest online sales were for furniture, food, and fashion products, i.e. the three Fs which serve as the pillars of the BBF sector. The challenge is as big as it is inevitable.

Figure J
E-commerce: Italy ranks in the top 10, but lags far behind the advanced countries
(Total e-commerce sales as % of GDP)



Source: calculated by CSC and the Manlio Masi Foundation based on UNCTAD data.

Counterfeit BBF goods cause significant damage to Italian firms, and are an obstacle in calculating statistics

However, there is another aspect to bear in mind: oftentimes imitation BBF goods are hidden among non-BBF goods. These counterfeit goods try to fraudulently benefit from the branding and from the trust that some labels have earned from their customers. The size of the counterfeiting problem has reached significant proportions, especially in the Italian BBF sector. Indeed, Italian products are among the most highly

demanded products in the world, partly thanks to the attraction of the 'Made in Italy' brand, which consequently leads to them being among the most imitated.

According to the European Union Intellectual Property Office (EUIPO) data, counterfeiting generates more than 8.6 billion euros in damages each year, equal to 8 per cent of direct sales. The 'Italian sounding' phenomenon is especially worrisome, which is when a product is imitated – especially in the agro-food sector – through the use of a product name or type of packaging that seems Italian. This practice, which tarnishes the image of the products' quality and tricks less-careful foreign consumers into believing that they are buying an authentic Italian product, results in a loss of market share for BBF products (and also damages their reputation).

The counterfeiting of BBF goods, in addition to causing material damage to Italian firms, renders it even more difficult to measure the phenomenon itself, making it so that some of the statistics that track it are less reliable; presumably the Italian share is downward biased.

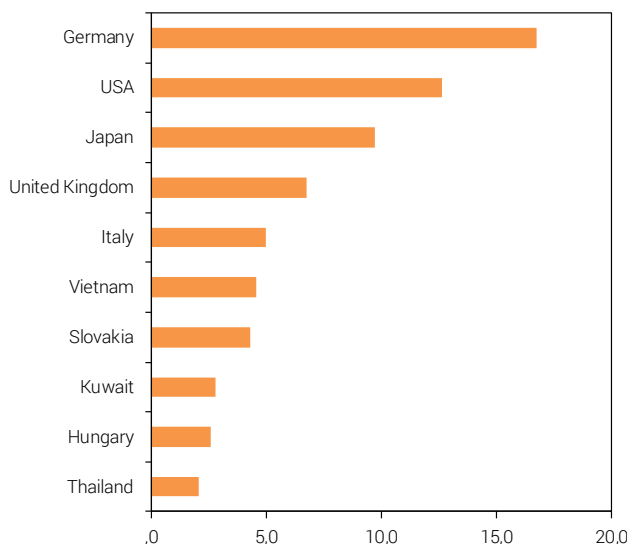
Trade tensions generate uncertainty and could be detrimental to many BBF products

Increasing protectionist tendencies threatens to harm many BBF sectors and reduce their potential export growth in many markets, first and foremost the US. A worrying symptom is the recent introduction of customs duties following the WTO's ruling, which threatens to trigger various forms of retaliation, with unforeseeable consequences. Although for now Italy is not among the worst affected countries, some products linked to the BBF sector have already been affected (for instance, Parmesan and other cheeses, citrus fruit, salami and cured meats and spirits will be subject to 25 per cent duty).

China: a priority area for improvement

Italian BBF sales in the Chinese market are strong, but our competitors are still much better. The most significant emerging market for Italian BBF products is China, which represents 13 per cent of total Italian exports to emerging countries and 24 per cent of Italy's BBF exports, thanks to the recent rise in domestic consumption. At the sector level, China mainly imports textiles and clothing products and hides and leather from Italy. In recent years, exports of motorvehicles and glass and ceramics have experienced notable growth. Figure K shows that, however, Italy ranks only fifth in the list of main BBF exporters to China, coming in after Germany, the US, Japan and the United Kingdom. Germany exports almost four times as much as Italy in BBF sectors of excellence. This result is heavily influenced by Germany's leadership in the automotive market.

Figure K
Italy lags behind in BBF exports to China
(Market shares in % of Chinese imports of BBF, 2017)



Source: calculated by CSC and the Manlio Masi Foundation based on UN-Comtrade data.