

The role and performance of business groups in industrial districts. Evidence from Italy.

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Abstract

The main aim of this paper is to analyse the presence and performance of business groups in industrial districts. Previous studies have demonstrated that business groups are more widespread within industrial districts given the possibility to mobilize the district productive resources and growth through the acquisitions of firms within the district. Empirical investigations on Italian industrial districts have also stressed the increasing heterogeneity of district firms and the general tendency towards the concentration of district output in the hands of a few larger firms. Most of these firms are organized as business groups. We expect that business groups increased their relevance within industrial districts during the recession period that followed the international financial crisis of 2008. This is because groups may benefit from the diversification of activities carried out by controlled companies and the possibility to share financial resources between them (internal capital market). At the same time, the location within specialized areas, such as industrial districts, influences firms' organization and performance. Groups in industrial districts are expected to be less diversified and more spatially concentrated than groups outside industrial districts. This may reduce the effect of diversification in transferring resources from high performing to low performing firms within the same group. For this reason, we expect to find performance differences not only between stand-alone companies and those belonging to groups, but also between business groups located or not located to industrial districts. The paper uses a novel dataset of Italian business groups developed using ownership information about joint stock companies taken from the AIDA database. This allowed us to build a map of Italian business groups in 2012. Moreover, from the AIDA database we obtained financial and economic data for companies belonging and non-belonging to groups for the period 2005-2012. Data refers to about 155,000 Italian joint stock companies, of which 28,000 belonging to groups. We use panel data models to compare the performance of companies and groups and to analyse the characteristics of groups within and outside industrial districts.

1. Introduction

“Business Group” is defined as a set of legally independent firms controlled by the same person(s) through ownership ties. The vertex of the group can be an individual or a group of people, often belonging to the same family (Almeida and Wolfenzon, 2006). In the following paper, we will adopt this definition of business groups, and therefore, we will neglect other forms of relations among firms based on other ties other than ownership. We are aware of the importance of these forms of relations among firms. According to literature, the growth of business groups would depend on several reasons. In emerging markets, business groups represent a necessity to overcome the difficulties deriving from the lack of financial institutions and incomplete markets. In fact, firms belonging to business a group could take advantage with internal movements of capital, without referring to external financing, but it is true also in developed markets.

Although there are many research studies on business groups in emerging economies, this phenomenon is widespread all over the world. From the latter empirical analysis of the Italian National Institute (ISTAT), in 2012, Italian business groups are more than 90,000. Istat refers to business groups in all sectors of economy. The business groups are markedly polarized in a few large structures with significant economic weight and many small groups. Regarding the presence of manufacturing firms in Italy, the presence of business groups is not peculiar only for larger firms (Iacobucci, 2004).

The groups with at least 500 employees account for only 1.5 %, but they weigh in terms of employees to 57.6 %. 75.5 % of the groups has a primary structure (1-2 companies active); those with more complex structures (more than 10 companies) are the minority but they play a decisive role in terms of employment, with nearly two million employees (Report of Istat, 2012).

Italian industry is characterized by the presence of industrial districts. The literature on industrial districts has focused on the agglomerative advantages associated with the co-location of productive units within a bounded geographic area (Brusco, 1982; Marshall, 1920). Empirical investigations on Italian industrial districts have showed the increasing heterogeneity of district firms (Cainelli et al., 2006). The literature agree on a tendency towards the concentration of district output in the hand of a few firms (Cossentino et al., 1996; Lazerson and Lorenzoni, 1999).

Most of these firms are organized as business groups. The role and the importance of business groups within Italian industrial districts have been analysed in previous literature (Balloni & Iacobucci, 1997; Brioschi et al., 2002; Dei Ottati, 1996b; Iacobucci, 2002). The main limit of these studies is that from a theoretical point of view, they do not identify the general relationship between the presence of business groups and the development of industrial districts.

Furthermore, as the literature on industrial districts suggests, the spatial concentration seems to have a stronger role within “traditional” clusters.

Starting from this previous research works, the present paper tries to analyze the role and the performance of Italian business groups within industrial districts and non-district areas and Italian stand-alone firms during the period 2008-2012. Furthermore, we intend to investigate if business groups increased their relevance within industrial districts from 2008 to 2012. This is because groups may benefit from the diversification of activities carried out by controlled companies and the possibility to share financial resources between them (internal capital market). At the same time, the location within specialized areas, such as industrial districts, influences organization and performance of firms.

Groups in industrial districts are expected to be less diversified and more spatially concentrated than groups outside industrial districts. This may reduce the effect of diversification in transferring resources from high performing to low performing firms within the same group. For this reason, we expect to find performance differences not only between stand-alone companies and those belonging to groups, but also between business groups located or not located to industrial districts.

To demonstrate and analyze these points, the paper uses a novel dataset of Italian business groups developed using ownership information about joint stock companies taken from the AIDA database. This allowed us to build a map of Italian manufacturing business groups in 2012. Moreover, from the AIDA database we obtained financial and economic data for companies belonging and non-belonging to groups for the period 2005-2012. Data refers to about 155,839 Italian joint stock companies, of which 28,168 belonging to groups. We use panel data models to compare the performance of standalone companies and firms in groups and to analyse the characteristics of groups within and outside industrial districts.

The paper is organized as follows. The second section reviews the existing literature on the performance of business groups compared to stand-alone companies and the role and development of industrial districts and their relationship with organization of firms. The third section discusses the data and methodology used at firm and business group level. The fourth section illustrates the main empirical results. Finally, the fifth section presents the conclusions.

2. Literature background

The recent literature has showed that the phenomenon of business groups is not specific to large firms but it is widespread in many countries, both emerging markets (e.g Bae et al., 2008; 2002; Fan et al., 2005; Ferris et al, 2003; Gopalan et al., 2007; Khanna & Yafeh, 2007) and developed market. The latter aspect is emphasized by some authors (e.g Gorodnichenko et al., 2009; Hamelin, 2011; Khanna & Yafeh, 2005). “Business groups are common in many countries, especially in emerging economies” (Samphantharak, 2003). Indeed a business group is a corporate organizational form pervasive present both in developed and developing markets (Bianco & Nicodano, 2006). Other authors (Belenzon et al., 2013) underline the considerable presence of business groups, both in developing markets and in developed economies.

The growth and the development of this organization derive from different reasons.

There are several papers that analyze the performance of business groups, but many of them are empirical works and they do not pay much attention to different peculiarities of business groups. It is important to consider not only if a firm is an affiliated one, but also the features of the group, such as ownership and control rights of controlling shareholders, the number of affiliated firms within the business group, laws and regulations to which the group is subject (Samphantharak, 2003).

We also have to consider that in the real world external capital markets are imperfect, for this reason external finances are more costly than internal funding. These market imperfections are evident in emerging economies, where, as said above, financial markets are underdeveloped, there is a lack of the institutions and firms are more subject to financial constraints than those in developed countries.

There are several studies that showed a lower performance of affiliated firms compared to independent firms (Bae et al., 2002; Claessens et al., 2002; George & Kabir, 2008; Joh, 2003; Lins, 2003); this is more evident in large groups. The lower performance of affiliated firms, compared to independent firms, is justified by the profit redistribution from high performing firms to low performing firms.

Some authors (e.g Almeida & Wolfenzon, 2006b) argue that one of the reasons for the lower performance of affiliated firms can be that standalone firms, having less available resources, invest them in more profitable projects; while affiliated firms, benefiting from the greater amount of internal resources, invest also in less profitable projects.

Conversely, Hamelin (2011), considering a panel of French SME, shows a positive performance of affiliated firms. However, the specific level of performance of affiliated firms depends on country-specific characteristics. It is not easy to find common institutional features among countries (developing and development). For example we can notice an efficient contract enforcement in Israel or in South Korea, but poorer in Philippines, Brazil and Argentina (Khanna & Yafeh, 2007).

Khanna and Yafeh (2007) argue that in diversified groups, the performance of affiliated firms can result good, but we should analyze the specific country: in fact, in emerging markets, it is easy to find cases of diversified groups in which affiliated firms' performance is destroyed. In a recent work, Almeida et al. (2015) show that belonging to a business group let firms transfer cash from low-growth to high-growth firms, but they don't mention the phenomenon of tunneling, because this transfer of resources is not relative to the position of the firm (i.e top, intermediate or bottom of the pyramid).

It is evident that the empirical evidence depends on the specific features of the country and the time-period in which firms belonging to a business group are considered.

While the literature about business groups and their characteristics is variegated, until 20 years ago there were only a few studies analyzing the evolution of industrial districts and their relationship with firms' organization (Balloni & Iacobucci, 1997; Bianchi and Gualtieri, 1990; Brusco et al., 1996; Dei Ottati, 1996c; Nuti and Cainelli, 1996). The main limits of these studies were:

- 1) Their findings refer to specific industrial districts or regions, so it was difficult to generalize the results.
- 2) Only some of them analyze the relationship between industrial districts and the presence of business groups within them (Balloni & Iacobucci, 1997 ; Brioschi et al., 2002).

The first attempt to develop a general framework for analyzing the evolution and the role of industrial districts and the relationships between firms' organizational forms and business clustering is provided by Cainelli et al. (2006). They find that:

- 1) business groups are more widespread in industrial districts than in non-district areas;
- 2) the business groups located in industrial districts are less diversified than groups in non-district areas.

According to this work, it is possible to identify the evolutionary patterns of business clusters to explain the relationship between firms' organizational forms and business clustering. Moreover, the spatial agglomeration allows firms to grow and develop themselves; and eventually, they may be predominant in the spatial agglomeration and influence the evolution of the system.

Furthermore, research studies about Italian firms before crisis of 2008 have showed that firms belonging to industrial districts had a higher profitability and productivity than firms not belonging to industrial districts (Fabiani et al., 2000) and also a higher rate of product innovation (Cainelli and De Liso, 2004).

Moreover, empirical evidence (Cainelli et al., 2006) have showed a higher presence of business groups in districts rather than outside industrial districts and the business groups located in industrial districts are less diversified than groups in non-district areas.

Starting from the latter results, the aim of this paper is to analyse the role and the presence of business groups inside and outside industrial districts and also compare the performance between standalone companies and business groups during the period 2008-2012, characterized by the financial crisis of 2008-2009 and the subsequent credit crunch.

3. Data and methodology

The paper uses a novel dataset of Italian business groups developed using ownership information about joint stock companies taken from the AIDA database. This allowed us to build a map of Italian business groups and examine the performance for firms during the period. From the AIDA database, we obtained financial and economic data for companies belonging and non-belonging to groups for the period 2008-2012 in the manufacturing sector. Data refers to 155,839 Italian manufacturing joint stock companies, of which 28,167 belonging to groups. Specifically, our dataset also includes 55,909 companies belonging to groups: 28,167 manufacturing firms (mentioned above), 17,267 belonging to other sectors and 10,475 foreign firms.

The total number of observations is 183,581¹ at firm level, because in addition to those 155,839 Italian manufacturing joint stock companies, we also have considered other legal organizational forms and foreign firms belonging to the business groups. Up to now, we have available financial and economic data for manufacturing firms.

Furthermore, we consider the presence of industrial districts. To identify industrial districts we combine the Local Systems of Labour (SSL) with the code of industrial districts (extrapolated by Istat).

We expect that a) business groups increased their relevance within industrial districts during the recession period that followed the international financial crisis of 2008; and b) to find performance differences not only between stand-alone companies and those belonging to groups, but also between business groups located or not located to industrial districts.

This section analyses the presence of the business groups and standalone companies in industrial districts and outside them.

First of all, our cross-section considers 19,923 groups (only joint stock companies), and the mean number of firms belonging to groups is about 2.8.

¹ This total considers not only Italian joint stock companies in manufacturing sectors, but also foreign firms and other Italian organizational forms belonging to business groups.

Table1. Number of firms and employees of groups by class of firms declaring they belong to a group (2012).

Firms <i>per</i> group	Freq.	Freq. %	Average number of firms	Average number of employees <i>per</i> firm	Average number of employees <i>per</i> group
2	13,748	71.3	2.0	12.4	24.8
3-4	3,829	19.9	3.3	24.3	80.5
5-9	1,276	6.6	6.2	43.0	270.8
10-49	413	2.1	15.7	67.5	1126.3
50 and over	11	0.1	80.1	104.3	9311.0
Total	19,277	100.0	2.9	18.0	81.1

Table 2. Number of firms and employees of groups by class of employees of the firms declaring they belong to a group (2012).

Class of employees	Freq.	Freq. %	Average number of firms	Average number of employees
0-19	12,833	64.4	2.3	2.5
20-99	4,619	23.2	2.7	47.8
100-499	1,936	9.7	4.3	208.2
500-4999	509	2.6	10.5	1221.9
5000 and over	26	0.1	23.9	10987.8
Total	19,923	100.0	2.8	78.5

Although our dataset considers only the joint stock companies belonging to business groups, it confirms (tab.2) the previous research studies in which it is highlighted the presence of Italian business groups in firms with less 20 employees (e.g Iacobucci, 2004).

Table 3. Presence of business groups and standalone firms in industrial districts (2012).

Group	District		
	0	1	Total
0	80,923	46,749	127,672
1	40,817	15,092	55,909
Total	121,740	61,841	183,581

Group=0 denotes firms not belonging to business groups; *viceversa* Group=1.

District=0 denotes firms not belonging to industrial districts; *viceversa* District=1.

From table 3, we identify 61,841 firms that are located in industrial districts, while 121,740 firms are not in industrial districts. 73% of firms belonging to business groups are outside district, while 27% of those firms are in industrial districts.

Furthermore, excluding from groups both foreign firms and other organizational forms, we analyze only manufacturing firms belonging to business groups outside and inside industrial districts (Table 4.).

Table 4. Presence of business groups and standalone firms in manufacturing sectors (2012).

Group	District		
	0	1	Total
0	80,923	46,749	127,672
1	17,585	10,582	28,167
Total	98,508	57,331	155,839

From table 4. , in 2012, we notice that the majority of Italian manufacturing firms belonging to groups are not located in industrial districts (62.5% vs 37.5%). With reference to stand-alone companies, 63.3% of them are outside industrial districts, while 36.6% are within them.

Table 5.

Variable	Industrial district		
	0	1	Total
Italian manufacturing controlling firms	3,583	2,483	6,066
Italian controlling firms	11,920	5,336	17,256
Italian manufacturing controlled firms	14,002	8,099	21,101
Italian controlled firms	18,422	9,756	28,178

Furthermore, it results that 59% of the controlling firms are outside industrial districts, 41% within them.

Within industrial districts, we find that controlling firms (heads) are all manufacturing firms. On the contrary, outside districts, the majority of Italian controlling firms (head) are not manufacturing firms. We may argue that some of the latter ones are financial holding companies. The foreign controlling firms are 2,636.

The 63% of controlled firms are outside industrial districts, 37% within them. Instead, the foreign controlled firms are 7,839.

Up to now, we can hypothesize that Italian industrial district is more prolific for stand-alone companies than for firms belonging to groups, probably because those may benefit from a network of skills, knowledges and competences developed within districts. In the last ten years, the competitive advantage of firms depends much more on expertise and skills rather than by purely operational and productive activities.

For this reason, we believe that the higher presence of stand-alone companies within districts than groups explains the necessity of sharing knowledge and developing the competences, taking advantages of firms' network, since these firms cannot benefit of advantages typically of the business groups.

Moreover, on average, from 2008 to 2012, there are more employees outside industrial districts than within districts (see Table 10); this result is consistent with the previous empirical evidence showed by Cainelli et al. (2006). This difference, in terms of number of employees, may explain the higher presence of small firms within industrial districts (Cainelli et al., 2006).

Table 6. Average of employees working in firms in industrial districts and outside them.

Employees	Industrial districts	Outside districts
2012	45.01	61.84
2011	52.50	71.97
2010	48.75	64.63
2009	48.66	63.29
2008	67.36	68.45

4. Empirical results

First step is to investigate the relevance of firms belonging to business groups compared to standalone firms, we analyze the share of cumulative revenues from 2008 to 2012 (see table 7).

Table 7. Turnover of business groups in terms of revenues.

Share of total turnover of business groups			
	Cumulative turnover (industrial district and outside) %	Turnover in industrial districts (%)	Turnover outside industrial districts (%)
2012	76%	66%	82%
2011	75%	66%	80%
2010	73%	66%	77%
2009	72%	64%	77%
2008	73%	68%	76%

The cumulative turnover of business groups is increased from 73% in 2008 to 76% in 2012, and their relevance is higher than the corresponding standalone firms in each year. In particular, the effect of turnover is increased and is higher for business groups outside districts rather than for those in industrial districts (see column 3 and 4 of Table 7).

Therefore, in terms of revenues, business groups enlarged their presence outside industrial district and slightly decreased their share within districts.

Second step is to investigate if there are differences in performance between business groups in industrial districts and outside them, and also between firms belonging to business groups and standalone firms, during the period 2008-2012.

We use the Return on assets (ROA) to measure the performance of firms.

Tab.8 Variable used for the performance

Dependent variable	Description	Formula
Roa	Return on assets	Operating profit/ Total assets

Explanatory variables		
Bank loans	External financing (from banks to companies)	Sum of bank loans/ (Liabilities+ Net Equity)
Group	Firms belonging to groups or standalone companies	Dummy variable indicating whether a firm belongs to a group (Group =1) or not (Group=0)
District	Firms in industrial districts	Dummy variable indicating whether a firm is located in an industrial district (District=1) or not (District=0)
Level	Level of affiliated firms	Level=0→Standalones Level=1→ Heads Level>1→Controlled firms
Age	Firms' age	Year 2012 - Year of foundation
Controlled variables		
Sector	Manufacturing sectors from Ateco 2007	
Firm size	Log of revenues in 2008	

a. Performance between business groups in industrial districts and outside districts

Tab. 9. Differences in performance between firms belonging to business groups in industrial districts and outside them

Firms in business groups			
	Industrial districts	Outside districts	t
ROA_2012	.0185	.0155	-1.5876**
ROA_2011	.0309	.0257	-3.0947***
ROA_2010	.0292	.0257	-2.1394**
ROA_2009	.0177	.0164	-0.7115
ROA_2008	.0434	.0389	-2.5796***

We notice that the level of performance is better for firms belonging to business groups in industrial districts than for those outside them in all period-considered (2008-2012). The differences are significant in each year (except in 2009).

Table 10. Roa in 2012 for business groups in industrial districts and outside them (OLS).

	ROA_2012
District	.0044818 (2.33**)
Bank loans_2008	-.0862959 (-12.50***)
Firm size	.0072949 (12.28***)
Age	-.0001406 (-2.29**)
Sector dummies	.0002318 (1.48)
N. Of obs	16,638
F test	44.98***
R square	0.0158

From table 10, we note that at the end of the period (2012) there is a significant negative relationship between performance of firms belonging to business groups (Roa) and:

- the variable “bank loans” of 2008;
- the variable “age”;

Moreover, we found a significant positive relationship between firm’s performance and:

- the dummy “district”;
- the variable “firm size”;
- while sectoral dummies show a positive coefficient, even if not significant.

b. Performance between business groups and standalone firms

Tab. 11. Differences in performance between firms belonging to business groups and standalone companies

	Standalone firms	Business groups	t
ROA_2012	.02756	.01676	9.8772***
ROA_2011	.03266	.02779	4.7713***
ROA_2010	.02955	.02708	2.4561*
ROA_2009	.01668	.01692	-0.2283
ROA_2008	.03953	.04068	-1.0497

The table shows that the differences of performance between standalone firms and firms in business groups are not significant in 2008 and 2009, probably because the financial crisis had a negative impact on both classes of firms, but from 2010 to 2012 the performance is higher for standalone firms and the differences are significant. We think that given that standalone firms cannot benefit from group support, during a financial shock only those with better performance will survive; on the contrary, business groups are expected to sustain the survival of affiliated firms, thus preventing their failure, even when the latter show a poor performance.

Tab 12. Roa in 2012 (OLS)

	ROA_2012
Group	-.0061624 (-5.12***)
District	.0015925 (1.64*)
Bank loans_2008	-.0728281 (-15.75***)
Firm size	.0053681 (14.94***)
Age	-.0003953 (-9.38***)
Sector dummies	.0002645 (3.45***)
N. Of obs	73,057
F test	327.37***
R square	0.0434

From table 12, we note that at the end of the period (2012) there is a significant negative relationship between firms' performance (Roa) and:

- the variable "group";
- the variable "bank loans" of 2008;
- the variable "age";

Moreover, we found a significant positive relationship between firm's performance and:

- the dummy "district";
- the variable "firm size";
- sectoral dummies.

5) Conclusions

The main aim of this paper is to analyse the presence and performance of business groups both in industrial districts and outside them, comparing also their performance with those of standalone firms during the period 2008-2012. This period appears interesting to investigate because it is characterized by the financial crisis of 2008-2009 and by the consequent credit crunch. Findings are in line with our research hypotheses.

First, we find that the share of the cumulative turnover of business groups is increased from 73% in 2008 to 76% in 2012; as a result, the business groups increased their relevance compared to standalone firms during the period analyzed. This increase is higher for business groups outside industrial districts rather than for those within industrial districts. This may be explained considering that groups outside industrial districts are more diversified than groups located within industrial districts; the diversification of activity helped us to compensate for the poor performance of in some sectors or markets.

On the contrary, the share of business groups within industrial districts slightly decreased during the period considered.

Second, we expected to find different performance between business groups and standalone firms, and also differences among firms belonging to business groups located in industrial districts or outside them.

In fact, we find that at the end of the period the performance of standalone firms is better than the performance of firms in business groups. This result may be explained by the fact that during the financial crisis only the standalone firms with better performance survived, since standalone firms cannot benefit from group support. On the contrary, business groups are expected to sustain the survival of affiliate firms, thus preventing their failure, even when the latter show a poor performance, in order to obtain long-term benefits. This mechanism has a positive relation with the degree of diversification of groups; as a result it is more evident for groups outside industrial districts than in groups within industrial districts.

Moreover, there are also differences in performances among firms belonging to business groups located in industrial districts or outside them. The district has a positive impact in performances of firms belonging to business groups. In general, the dummy district has a positive and significant relevance for all firms (standalones and not).

One of the limitations of this study is that we analysed economic and financial data only for manufacturing firms. Moreover, we considered as unit of analysis the individual firm, standalone and belonging to groups. However, for the latter we did not consider the characteristics of the group they belong to.

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