THE ITALIAN CHAMBER OF COMMERCE AND INDUSTRY FOR THE UK

Twenty-Seventh Banking and Industry Conference Debate

"Foreign Direct Investment: Italy and U.K."

SviluppoItalia

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The Savoy, London

THE ITALIAN CHAMBER OF COMMERCE AND INDUSTRY FOR THE U.K

"Foreign Direct Investment: Italy and U.K."

Honorary President	The Italian Ambassador *H.E. Giancarlo Aragona*
President of the Chamber of Commerce:	Dott Leonardo Simonelli Santi
Chairman of the Conference:	Professor Robert Leonardi *London School of Economics and Political Science*
Panel:	Mr John Studzinski *Chief Executive and Co-Head Corporate Investment Banking and Markets HSBC Bank plc*
	Cav Lav Avv Luca Cordero di Montezemolo *Presidente Confindustria*
	Mr John M Sunderland *President Confederation of British Industry*
	Dott Carlo Salvatori *Presidente Gruppo UniCredit*
	Sir George Mathewson, CBE, LLD, FRSE *Chairman Royal Bank of Scotland Group*
	Ing Massimo Caputi *Amministratore Delegato Sviluppo Italia SpA*
	Ms Susan Haird *Deputy Chief Executive UK Trade & Investment*
Guest of Honour at Lunch:	Prof Dennis J Snower *President Kiel Institute for World Economics*
	In association with Il Sole 24 Ore

Sviluppo Italia is the Italian Agency for Enterprise Creation and Inward Investment Development. The Agency's mission is to promote, speed-up and spread development throughout the Country to boost national competitiveness by means of three lines of action:

- **Business Creation and Development**
- **Support to the Public Administration**
- **Inward Investment Development.**

As for the latter, in July 2004, Sviluppo Italia, in cooperation with the **Italian Trade Commission**, created **INVESTINITALY**, to promote foreign investment in Italy offering a single and reliable **reference point** to current and new investors intending to set up or expand their business in Italy.

Investor Services

InvestInItaly supports companies throughout the investment process: from the first informative contact to location scouting to the set-up phase, from incentive negotiation to Public Administration dealings and after-care assistance. All of these services offered are free of cost and are strictly confidential.

The Location Agreement

InvestInItaly avails of an innovative financial tool aimed at facilitating foreign companies looking to set-up or expand their business in Italy, especially in the South.
Managed by Sviluppo Italia, the Location Agreement - entirely dedicated to foreign investors - provides investors with a turn key support package guaranteeing: implementation timeframe, incentives, availability of infrastructures and industrial areas, support for R&D and training activities, tailored assistance from the business plan implementation to the set-up.

An International Network

InvestInItaly relies on an international network of offices located in the main investor countries. This network consists of 9 Italian trade Commission information desk and a pool of selected partners, including consultancy companies, merchant banks, and intermediaries specialised in investment promotion, assisting prospective investors individuating the most suitable location opportunities.

InvestInItaly Head Office:
Via Calabria, 46
00187 Rome - Italy
info@investinitaly.com
www.investinitaly.com

Contacts for the United Kingdom:

Business Development Services
Tel. 0044 (0)28 90330515
Fax 0044 (0)28 90242597
uk@investinitaly.com

Information Desk
Italian Trade Commission
14, Waterloo Place
London – SW1 Y 4AR
Tel. 0044 (0)20 73890300
Fax 0044 (0)20 73890301
london@investinitaly.com

Photographs of the Events

General view of participants at the Conference

H. E. Giancarlo Aragona

Professor Robert Leonardi Chairman of the Conference

Some members of the Panel of Speakers

H.E. Giancarlo Aragona at the lectern and members of the Panel of Speakers

Dott. Leonardo Simonelli Santi President of the Italian Chamber of Commerce & Industry for the UK

Cav. Lav. Avv. Luca Cordero di Montezemolo

The Panel of Speakers

The Chairman of the Conference and the Panel of Speakers

Mr John Sunderland

Dott. Carlo Salvatori

Some members of the Panel of Speakers


The Panel of Speakers


Sir George Matthewson


“ Ing. Massimo Caputi


Dott Carlo Salvatori at the lectern and the Panel of Speakers


Sir George Matthewson at the lectern and the Panel of Speakers

Three members of the Panel of Speakers

Professor Dennis J Snower Guest of Honour

Participants at the Conference

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H.E. Giancarlo Aragona, Cav. Lav. Avv. Luca Cordero di Montezemolo. Mr John Sunderland and Dott. Leonardo Simonelli Santi

A general view of participants of the Conference

Staff of the Italian Chamber of Commerce & Industry for the UK

Proceedings of the Conference

Leonardo Simonelli Santi

Ladies and Gentlemen, a very warm welcome and a few remarks on this year's conference so as not to take precious time away from our speakers.
We have reached the XXVIIth edition of our Banking and Industry Conference and maintaining interest alive, in this traditional event, is not an easy task. It is essential to have an interesting subject for discussion and eminent members on the panel.

This year we have focused on what we think is an essential and critical aspect of international economic cooperation: foreign direct investment.

To make foreign direct investment possible, there must be reciprocal long term trust on the side of the host country, which commits financial support and the future of local employees to the hands of foreign investors. These investors must feel that the host country has a secure and competitive environment for production in order to commit the necessary risk capital. It is a situation, as Prof Francis Fukuyama has explained, where a network of trust is essential for global economic and social development.

Furthermore, our Chamber of Commerce developed its own expertise on the subject beginning in 2002 with the publication of a biannual survey on Italian investments in the UK. These reports, which have shown the importance for the British economy of more than 600 Italian related companies (with 53,000 employees, generating 12 billion pounds in turnover), have been received with interest so that we are planning a third edition in 2006.

We have been able, therefore, thanks especially to the help of our friend Alessandro Roselli, UK Delegate of the Banca d'Italia, to provide you with some Foreign Direct Investment data, which you have on your seats together with other material of interest.

At the Chamber, we are quite aware that today's scenario is not the most favourable for the economy and indeed international tensions, specific national problems and even natural disasters, may increase perplexity towards good opportunities for cross border cooperation.

We strongly believe, however, that international cooperation is the way forward to solve the problems generated by increased differences in the distribution of wealth. In fact although there has been rapid economic expansion, due to technological development, world economic resources have been mainly utilised by the few, while the ecological negative consequences have been shared by everyone.

The task to satisfy the need for a sustainable economic and social growth is a difficult one and requires many capable leaders.

Luckily we have been able to find representatives of this rare breed for our conference, and I would like to thank our speakers for joining us and sparing their valuable time.

Our speakers are of international stature and have much experience of subject of the Conference. We have two leaders of the industrial world, Mr John Sunderland, President, CBI and Avv Luca di Montezemolo, President, of Confindustria; two well-known and highly esteemed bankers, Sir George Matthewson, Chairman of the Royal Bank of Scotland and Carlo Salvatori, President of Gruppo UniCredit.

After their presentations there will be a question and answer section and the panel will be joined by Ing Massimo Caputi, Managing Director of Sviluppo Italia SpA and Mrs Susan Haird, Deputy Chief Executive of UK Trade & Investment.

Their biographical details are in your programme.

We are also very fortunate to have Prof Dennis J Snower PhD as our Guest of Honour at lunch, when he will be formally introduced. I would, however, like to thank him for allowing us to distribute material from the Kiel Institute for World Economics of which he is President.

And, we are, of course, delighted to have Professor Bob Leonardi, of the London School of Economics and Political Science, and Director of the Social and Economic Cohesion Laboratory, as our Chairman. We have been friends for many years, and he has been kind enough to invite me to many lectures he has organised at LSE.

As usual, my role is very limited because I think we have to take full advantage of the presence of our speakers and our audience. Therefore before giving the floor to Professor Leonardi, it is my pleasure to introduce H.E. Giancarlo Aragona, our Ambassador, who will say a few words.

Thank you.

Giancarlo Aragona

Thank you very much Mr Chairman and a very warm welcome to the distinguished guests on the panel and to all those present here today.

As Mr Simonelli has just said, the banking conference, established over a quarter of a century ago, constitutes an important annual forum in addition to institutional meetings for an in-depth appraisal of the economic relations between the United Kingdom and Italy. Having been present at last year's meeting, I am confident that this forum, this year as well, will prove conducive to informal and businesslike discussions.

This year's topic is particularly stimulating and challenging. To talk of foreign direct investments means to focus on a country's capacity to project its industry beyond the national borders and to involve foreign industries in the development of its own economy. It is, as you well know, a complex issue which puts under the spotlight the essential features of the national productive system and, in more general terms, the country's capacity to adapt and cope with the pressing challenges of internationalisation.

It is quite evident that the potential growth of foreign direct investments depends to a significant extent on the state of health of the respective economies and of the international economy. Like other economies in Europe, Italy is at present going through a difficult phase and needs to confront and address an unfavourable situation by relaunching growth and competitiveness. The country is well aware of this and the government and the other relevant players are actively engaged to this end, with the contribution of private business and their social partners.

Recent improvements in the data concerning GNP, employment, exports and the stock market are positive and encouraging signals. Other major European countries too have suffered a slump in their economies. Even the UK is experiencing a dull turn in its economic growth which has been buoyant these past years.

There is no doubt that, against this background, the attraction of foreign direct investments presents a challenge, but it is also a way to contribute through internationalisation to the relaunching of the economy. The protagonists of this challenge in Italy and in the United Kingdom will take part in today's debate. They are the leaders of the confederations of private enterprises and the heads of the agencies responsible for the promotion of foreign direct investments. They will talk to you in detail about this topic and will illustrate possible lines of action.

This morning we have read in the British newspapers that the United Kingdom has overtaken China as a recipient of direct foreign investment, thus becoming the second recipient in the world after the United States.

We must strive to achieve a more balanced bilateral flow of foreign direct investments. If it is true that in the past years Italian investments in the United Kingdom have registered a positive trend, suffice to mention Finmeccanica, Merloni and others. It is also true that the percentage of British investments in Italy, vis-à-vis the total of UK investments abroad, though improving, is still low. It is quite evident that the scales are unevenly weighted and that, from this viewpoint, there is significant scope for improvement. I am aware that this depends in part on the perception that the Italian business environment presents rigidities. I will not deny this fact, but I wish to emphasize that a lot has been done to make our system more business friendly, in particular in the labour market area and in the higher education sector.

I therefore hope that today's debate will enable the participants to understand more clearly the realities of our two countries and identify practical responses and recipes for action.

In renewing my warm welcome to all present, I express my best wishes to the panellists for a fruitful and successful conference. Many thanks.

Robert Leonardi

Good morning.

In opening the conference and the presentations, I just wanted to add a few points. You have received a dossier of data on investments in the UK and in Italy. What I wanted to do now is to present to you some comparative data to show where the UK and Italy are in relation to the rest of Europe, the United States and Japan, and to make three basic points. That is, that for foreign investment, in terms of outward investment and inward investments, we have to consider the international context and some of the important phases of this changing international context that we have witnessed during the past 20 years.

The first point is the impact of globalisation in terms of the liberalisation of trade at the world level. If we look at certain parts of the world, such as Europe, which mainly concerns us today in this conference, we have seen during the past two decades the creation of new conditions for the market and for trade. Here we have seen that with the creation, or the run-up, to the single market and the consolidation of European trade after 1993 there have been two surges of foreign investment (FDI) in preparation for the single market and once the single market was created. That double surge was repeated again as the enlargement of the EU toward central and eastern Europe was being prepared and after it took place.

If you look at the Central and Eastern European countries (CEECs), there is a significant surge after 2000, in terms of when it becomes clear that these countries are coming into the European Union. Therefore the conditions for business have stabilised, interest rates have come down, and there is more solidity to the monetary system. Once they enter in 2004 there was another increase or surge in foreign investments in the CEECs. These patterns suggest that we have to look at the changing "institutional conditions" affecting the market that create surges in investments. So the question is, do we have further changes in the institutional and market conditions that then can create, in the future, new surges in FDI in Europe?

We also have a change in investment conditions with changes in comparative advantage. In terms of software we have seen the phenomenon of India that has a comparative advantage in the production of software, therefore creating the bases of a surge of investments in India. In terms of a comparative advantage in industrial capacity, this is the case of China.Therefore these two local changes in India and China have helped to mobilise surges in global investments

A second point that is important and which is the topic of this conference, involves the internal competitive conditions that exist within countries. Given these "institutional" and "global" elements discussed above, we have to turn to the local conditions and whether the local conditions are favourable for the attraction of investment. These conditions can be confined to just the national language, and this is one of the factors that we have seen in spurring FDI in the UK and especially Ireland. Then we have the legal conditions, in terms of: is it clear what the obligations are in terms of the investor's camp? Can the investor collect on credits; is there the presence of a skilled workforce, and there exists agglomerations of firms in the investor's sector of specialization? What we have seen in Europe is that we are moving towards a concentration of certain types of businesses in particular areas.

The third point I want to discuss is the role of "local conditions" in stimulating investments. From an investor's point of view, is it easy to set up an enterprise and to create a factory to export one's products from a local area to larger markets in the country, Europe or the world? Both in the UK and in Italy there are special enterprise zones where there is an attempt, in a pro-active manner, to make these areas much more attractive than other areas in the country for investment. As a result, what we get is an increase in investment in these areas and in countries offering an attractive package of incentives for foreign investments.

The UK is one of Europe's leading places for investment. If we compare the UK to Italy, in terms of the foreign capital stock, in the UK it represents one third of GDP. If we look at the same figure for Italy, it represents one tenth. Therefore, we can argue that Italy is under-invested from the point of view of foreign investment. Another way of looking at it is that there is a still a lot that can be done in the Italian case. So, the question is how can we configure the conditions so that investments in Italy will increase and, from the UK point of view, how can we configure the conditions in order to maintain the present level of investment?

I just wanted to say one more thing in terms of trade. When we talk about investments, we also want to make sure that these goods can flow freely across borders. If we look at the UK and Italy in comparison to other countries in the European Union, we see that, basically, Europe is an open market. Both for the UK and for Italy, in terms of imports and exports, more than half are directed toward other countries in the European Union. Therefore Europe is the context within which trade and investment takes place.

John M Sunderland

Good morning Ladies and Gentlemen. As the first British speaker today, can I welcome particularly those of the delegates who have come, as I know many have, from Italy. It is a great pleasure both to welcome you to the UK, to London and indeed to this rather splendid room in The Savoy hotel.

I understand that the Italian Chamber of Commerce and Industry in the UK dates back to 1886 and is one of the oldest of the 66 Italian Chambers of Commerce around the world. I think that underlines the length of the history and economic association between our two countries.

Today the economic ties between them are just as important. We both have diversified industrial economies with roughly the same total and per capita output. Italy is the eighth largest global market for British exports and around 1,800 British companies operate in Italy through subsidiaries and/or joint ventures. Of course, there are many major Italian investors in the United Kingdom including Fiat, Pirelli, Candy and Benetton, just to name a few.

Yesterday a delegation of Italian businessmen and women led by Luca di Montezemolo, the president of Confindustria, met with a number of their British counterparts to discuss particularly the issue of market liberalisation and competitiveness, an issue of great interest and concern to both of us. We found we had a very common, shared view of the necessity for liberalisation and we agreed on a number of practical measures which we could take to further open our markets, which will be to our combined mutual interest.

It is not just manufacturing either. Away from commerce, the relationship between Italy and the UK is just as strong. About 2.5 million British visitors go to Italy each year and just over 1 million Italians visit the UK. Italy is an important partner of the United Kingdom, both in the bilateral context and of course as members of the European Union, NATO and the G8.

Prime Ministers Blair and Berlusconi have pledged to enhance their joint contribution to meeting European and international challenges. A specific recommendation was that, and I quote, "The UK and Italy will co-ordinate the proposals for simplifying European legislation as part of the wider EU regulatory reform agenda." A mission I am sure that all of us in business would applaud given the extent to which we suffer. The herniating mass of regulations that seems constantly to emanate both from Brussels and from within our own countries, and the commitment of the United Kingdom and the previous EU presidencies of Holland and Luxembourg to try and reduce this burden on businesses, is something we welcome and something I know both our Prime Ministers share as an objective. Of course, following the CBI Confindustria bilateral yesterday, we reaffirmed our shared objectives on these issues and I think we are making progress on them.

Now, you may not be aware that 2005 is the 40th anniversary of the Confederation of British Industry. We have reflected on the changes that have occurred on the issues which have challenged and confronted business over the last 40 years on a number of occasions during this last year, but if we had to choose one word that summed up the critical change over that period of time, then it would, of course, be globalisation.

It is fitting that the theme of our conference today is foreign direct investment. The surge in the level of global foreign direct investment perfectly illustrates the impact of globalisation. Just 20 years ago, in the early 1980's, total world foreign direct investment stood at $58 billion. By the turn of the millennium that figure had grown to $1,200 billion. Midway through the Twentieth Century, world exports constituted only 8% of global GDP. Approaching the millennium, that figure had surged to over 25%.

The rise of emerging economies including, most obviously, China, India, Russia and Brazil, and their role in the future world economy is well documented. They all, especially China, benefit from increasingly skilled, but low cost labour. They have an appetite for hard work and risk and they are free from much of the mass of regulations that constrains the way we do business in Europe. China for me is the Twenty-first Century equivalent of Victorian Britain and its economic potential and ambition is an awesome combination. Just as ours was in the Nineteenth Century.

As you know, China regularly reports year on year economic growth of up to and occasionally over 10% per annum. It is currently the seventh largest economy in the world, but by 2020 it is forecast to be the second, leapfrogging the United Kingdom and Italy in the process and second then only to the United States.

The numbers for India are almost as impressive. Recent economic growth has averaged over 6% and is forecast to remain at that level. India is the world's largest beneficiary of off-shoring, accounting for 80% of the global business process outsourcing market. Its pool of skilled labour is impressive and provides one quarter of the world's software engineers. Between them, China and India account for over one third of the world's population, so in business terms it is wrong to view them simply as a low cost, producing, competitive threat. They represent a significant and clearly rapidly growing market opportunity.

So how should Europe respond to these challenges and opportunities? I believe the majority of British business is pro-European. That is not a political view, just a statement of fact about where our economic interest lies. Europe accounts for around 50% of our exports. That compares to less than 20% for the United States, but right now the impasse over the European treaty leaves Europe at a cross-roads. There is a heart and minds battle to be won over the future direction of Europe. The old European social model is not working. The economic difficulties that have beset many member states in recent years including sluggish growth, high unemployment, despondency about the future, all these are wake up calls that reinforce the reality of global competition.

We need to revisit the origins of the Europe that we signed up to. We must redefine our relationship with the rest of the world; position ourselves to win, to compete more effectively. The way to react to globalisation is not by the European commission attempting to act as some modern day King Canute against a rising tide of globalisation. Free trade has to be the only sustainable long term solution.

Now, I am hesitant to raise the EU's handling of Chinese textile exports in this audience, because I know that it is a sensitive issue, but it does illustrate the point. It resulted in around 18 million items of clothing, from jumpers to underwear, languishing in warehouses and containers across Europe. This was the new Commission's first real test of its free trade credentials and it has not covered itself in glory. There are some southern European countries that need to realise that WTL rules apply to them just as much as to developing countries.

We need to be outward looking to respond to global competition. To refocus on those early ideals: market liberalisation, completion of the single market, an end to subsidies and the promotion of open competition, and of course to regulate only where there is a need to do so.

The internal market, supposedly completed in 1993, has to become a reality to enable true competition and the free movement of goods, services and people throughout the Union. It particularly includes the opening up of the services market, which is a key sector in the EU and accounts for around two thirds of total European Union GDP and of course it includes, relevant to today, the completion of the single market in financial services. These are the only sustainable ways to respond to the challenges of globalisation.

In closing, can I say how much I hope that the UK and Italy will continue to work effectively to embrace globalisation, encourage the promotion of free trade in Europe, as well as in the rest of the world, in order that we can create the optimal environment in which all of our businesses can prosper.

Thank you.

Luca Cordero di Montezemolo

Publication of the transcription of Luca Cordero di Montezemolo's speech has not been authorized by the author.

George Mathewson

Thank you very much and could I start by thanking the Italian Chamber of Commerce and Industry for the United Kingdom for this opportunity to speak to you this morning.

Today I want to focus on one specific aspect of cross border investment, perhaps a somewhat different aspect from that which has occupied some of the other speakers. I want to focus on patterns of portfolio equity investment and their implications for the largest European companies.

I first became Chief Executive of the Royal Bank of Scotland in 1992. Getting to know your shareholders meant essentially getting to know a handful of British life assurers and pension fund managers. Overseas investors in those days owned just 13% of the British stock market. Today those overseas investors make up the biggest single investing constituency for British companies. In RBS' case, US investors now account for 19% of an institutional shareholder register and Europeans a further 14%.

You can find a similar pattern worldwide. Institutional investors have, over the last decade, substantially increased their holdings of foreign bonds and equities. The biggest movement has come in the Eurozone because, as you would expect, the arrival of the Euro has eliminated the currency risk for an Italian institution investing in Germany or vice versa. American and Japanese pension funds and, to a lesser extent, mutual funds also are similarly investing hard percentages of their portfolios in non-domestic equities. There has, in short, been a noticeable reduction in what economists would call the home equity bias: the tendency to hold too much of your portfolio in domestic shares when more international diversification ought, at least in theory, to achieve a higher expected return for the same level of risk.

When you consider the possible explanations for the home equity bias, this reduction is understandable. I have already mentioned the introduction of the Euro which is a limited currency risk for a good many investors. At the same time, regulators have removed or softened some of the investment restrictions imposed on both life companies and pension funds; although some countries still limit the percentage of foreign equities a life company may hold.

Globalisation has also reduced the average trading costs of international assets, above all the costs of obtaining adequate information about companies in other markets. But I believe we can and should go much further. I believe that despite the progress that has been made, the overall picture is disappointing and in fact threatening to large European companies.

Certainly European companies are not attracting as much investment from the world's largest pool of equity capital as portfolio theory would suggest they ought to. US institutional investors account for half of all the world's funds under management and the US stock market accounts for about half of total world stock market capitalisation. But US investors hold only about 13% of their portfolios in foreign equities, not 50%. So even if foreign investors now own 33% of the British stock market, that still leaves them under represented in British company share registers. I suspect this also applies in Italy. The last figures I saw suggest that foreign investors owned only around 15% of the overall Italian stock market, which is about as much as the public sector owns in Italy. Although, I do note that public sector ownership has been falling steadily, particularly since the energy companies have been privatised.

Now, although academics have spent a good deal of time on the home equity bias, this is not just an academic puzzle. The impact on European companies is real. In effect, we are prevented from gaining full access to the largest pool of capital in the world. At the same time, our own stock markets in Europe remain fragmented. The US stock market has a total market capitalisation of well over $16 trillion and 99% of this is accounted for by just two stock exchanges. Europe, by contrast, has a market capitalisation of $11 trillion spread across at least 20 stock exchanges. The three largest exchanges account for less than two thirds of the total. As a result, our cost of capital rises and our relative valuation falls.

So what should we be doing about all of this? The first thing to say is that there is still plenty of work to be done in reducing the costs of cross border trading and equities. Charles McCreevy, the European Commissioner for the Internal Market, recently indicated that he is starting to get impatient with the lack of progress on improving the way in which securities are cleared and settled across borders. Cross border clearing and settlement of share trades is still as much as six times as expensive as domestic clearing and settlement and there is plenty of scope to cut the cost substantially.

While I am on the subject of trading costs, I must take this opportunity to say a word about the additional handicap that the UK inflicts on itself in the form of our exceedingly high stamp duty. For all share trades that cannot claim a specific exemption, the UK levy stamp duty at a rate of 0.5%. That is much, much higher than any other large developed economy. Absurdly, one major effect of this high level of stamp duty has been to spur the growth of a thriving gambling industry in the UK. It is more cost effective to trade British shares through a spread bet which enjoys favourable tax treatment than through the stock exchange. Hedge funds do a lot of their equity trading through derivatives such as contracts for difference, which also avoids stamp duty.

Now, it might seem that half of 1% would not be enough to make a huge difference. Yet, even quite small increases in trading costs can lead to a significant difference in valuation. For a share that trades just once a year, getting rid of stamp duty would give rise to a 5% increase in value. In practice, turnover in shares has increased so rapidly, that the gain for many companies would be much greater. The impact of stamp duty seems likely to be even more pronounced on newer smaller companies that might be thinking of listing their shares on the stock exchange for the first time, than it is an established company such as RBS. It is hard to square that with the government's professed commitment to stimulating entrepreneurship.

Happily, such a high rate of transaction tax is uncommon in the rest of Europe and I am pleased to learn that Italy has avoided the UK's mistake and does not levy stamp duty at least till share trade is conducted on the stock exchange. Even for off-exchange trades, the rate is much lower than ours, but with clearing and settlement costs still high, trading costs remain one of the obstacles to the creation of a pan-European equity market and one of the handicaps under which European companies must labour. Many of them can be readily tackled with the right will, but alongside trading costs, there are other barriers rooted in the behaviour and mentality of investors and these barriers will be much harder to shift.

Important as clearing and settlement of transaction taxes may be, a market is not a trading platform. The two things are fundamentally different. A market is a collection of individuals whose behavioural patterns are determined as much by institutional and cultural factors as by transaction costs. One such factor that has typically added to the home equity bias is the choice of benchmark against which fund managers' performance is assessed and all-encompassing growth of index linked trading.

One of the traditional means of measuring managers was to see how their performance stacked up against other managers. That form of benchmarking reinforced the sheep-like tendencies that are so prevalent in the fund management industries and encourage managers to build portfolios that look very much like a norm, very much like the average. That sort of peer group benchmark has been steadily falling out of favour, but investment mandates that measure performance against a stock market index can also lead towards a home market bias. It is quite natural for a US investor to benchmark against a US index such as Standard and Poor's 500.

In many cases, funds explicitly track the index. The actuary Watson Wyatt in its pensions and investment survey found that the value of assets managed by leading passive managers had more than tripled between 1996 and 2003, but index-tracking funds often follow domestic indices. This leads to a domestic concentration in portfolios. Even so-called active (and I use that word advisedly) investment managers are still constrained by stock market indices. Most long only managers are, to a greater or lesser extent, index huggers, prevented from deviating too far from the index against which they are benchmarked by their fear of underperforming. Pension consultants have in many cases advised an increase in allocations to alternative asset classes including hedge funds, private equities, corporate bonds and commodities. Nevertheless, many pension funds remain restricted in their overseas equity investments, not because regulations compel them to do so, but because this is how they choose to interpret their investment mandate.

The consequences for European companies are real and serious. Liquidity is reduced leading to a higher cost of capital for companies. Individual companies meanwhile may be over or under valued depending on their inclusion in particular indices. It leads to some interesting examples.

In 2000, for example, when Vodafone bought Mannesmann, managers with a UK equity mandate had to buy more Vodafone shares to reflect its increased weight in the UK index. Of course it also meant for a while (until Vodafone's price fell) that Vodafone constituted more than 10% of the UK index. Many fund managers whose mandates restricted them to holding no more than a tenth of their portfolio in any one company were therefore unable to buy as much as they would have wished. If you had structured the deal differently, and Mannesmann had taken over Vodafone, which would still have resulted in exactly the same industrial company and which in theory might well have been conceivable because they were about the same size, the same managers would have had to sell Vodafone shares as they would no longer have been in the UK index. It's absurd.

A more recent example is Shell's corporate restructuring. Shell, at least theoretically, located its headquarters in the United Kingdom. The restructuring left the underlying businesses unchanged, but because its headquarters were theoretically located in London, it sharply increased the groups waiting in the FTSE All-Share and FTSE 100 indices prompting some substantial buying from index tracking funds. Again, it is not based on any industrial rationale.

I might add that it further unbalanced the FTSE indices as props for the UK economy. The sixth largest companies in the FTSE 100: BP, HSBC, Vodafone, Glaxo, Shell and RBS, now account for 46% of the total market capitalisation of the index, and all six have substantial overseas businesses. In our own case, we are probably one of the least overseas, 37% of our operating profit now comes from outside the United Kingdom. That creates a further problem for investors. Because domestic stock market indexes are poorly correlated with national wage growth, their own liabilities may be poorly matched.

The spread of index tracking then, whether it is explicit or the sort of index hugging that arises when fund managers try to avoid under performing against their benchmark, has, I believe, contributed to keeping the home equity bias alive. So while European companies are steadily globalizing, the fund managers who invest in our shares remain much more parochial in their outlook.

I have to say that sometimes it is hard to avoid the impression that they do not want our businesses to compete globally. If you even contemplate investing overseas, you set up a chorus of complaint. Shareholders say that if they wanted to invest overseas, they could do so for themselves. Yet the fact remains that they do not do so.

So why does all of this matter? The answer is that it increases the cost of capital to European companies. As long as European companies have to raise capital in a series of fragmented national markets, and cannot gain access to a global pool of capital, they will be at a disadvantage to the United States. The European Commission financed a study in 2002 by the consultancy of London Economics. It found that full integration of European financial markets would lead in most European countries to a reduction of more than 40 basis points in the cost of capital. Potential gains in the United Kingdom, because of a punitive stamp duty, are even larger. Another study by Oxera, the economics consultancy found that abolishing stamp duty would lead to a fall of between 62 and 75 basis points in the cost of capital for British companies.

As long as our cost of capital remains higher than it ought to be, there will be investment projects that get turned down as unprofitable, there will be new companies that choose not to float on the stock market. Acquisitions on a global scale cannot be made against United States competition. I believe that the consequences for the European economy are serious enough to deserve attention, unless we wish all the larger companies in Europe to gravitate to New York.

Thank you.

Carlo Salvatori

The fact that a significant number of countries have recently opened their doors to the market economy has considerably boosted and expanded the market globalisation process.

Consequently, the flows of foreign investments have become increasingly important – and have also become key to understanding the evolutionary dynamics of many countries' economies.
The purpose of these notes is to make some brief considerations on the most recent trends of foreign investments within the EU – also presenting an extremely rapid review of a typical cross-border deal in the banking industry, featuring, as its leading players, UniCredit and HVB.

It is not totally superfluous to highlight the fact that the existence of a tight correlation between the development of foreign direct investments (FDI) and the economic growth of any given country has long been fully demonstrated.
In empirical terms, if we look at average annual GDP and FDI growth in the last 15 years in the world's main economies, this correlation in fact emerges very clearly indeed.
Based on my experience as a banker, I have realised that FDIs always play a positive role in aiding economic growth above all when given conditions exist – such as, for example, a skilled workforce and adequately developed financial systems.
I have also been able to see how this positive contribution to growth applies both to the countries making the investments and to those receiving them.
Based on close observation of companies that decide to invest abroad, I have further seen that they generally pursue two objectives largely considered complementary, i.e. they seek to increase:

1. The efficiency of their production cycles, and
2. Their products' penetration in given foreign markets.

Direct presence in a foreign market in fact provides tangible benefits. Such benefits relate not only to use of lower-cost production factors but also to production sites' greater physical closeness to markets that, even though today they are primarily production locations, are set, in increasingly short time spans, also to become attractive outlet markets.

Focusing attention now on the other side of FDIs, i.e. on the countries receiving the investment flows, I am firmly convinced that the direct presence of foreign companies in a country helps to achieve strong relaunch of its competitiveness.
More specifically, an increased presence of foreign players can lead to tangible benefits, i.e.

1. Creation of new jobs
2. The spread of new skills and know-how, helping to improve local enterprises' efficiency and productivity
3. Improvement of transport and communication networks permitting better domestic and international economic integration
4. The possibility of access to and comparison with other approaches to work organisation and business management.

FDIs – inasmuch as they are one of the main channels reinforcing economic interdependence (together with international trade in goods and services and financial interaction) – are able to trigger a sort of virtuous circle benefiting all those involved.

This largely explains the growing attention dedicated by many countries to creating conditions able to attract foreign investors – and also explain the race they have started in international markets to establish themselves as target countries for inward FDI flows.

As regards this, I would like to mention the issue of the openness of Italian markets to foreign investors. This issue is often surrounded by a heavy concentration of extremely severe and negative assessments - sometimes resulting in explicit accusations of a scarce propensity to accept foreign investments.
If, however, one observes the ratio between total FDIs (both inward and outward) and EU and Italian GDP, it emerges that the differences are not all that significant.
Further analysis of the data also reveals that both Italy and the EU are net investors, as the flow of outward FDIs exceeds the inward FDI flow.
Undoubtedly there are countries, such as the UK, that stand out for a much higher incidence of FDIs on GDP – but it also has to be considered that, if they are not properly set in context, these data are not perfectly comparable.
A partial explanation of the lower level of FDIs in Italy in effect lies in the intrinsic characteristics of the Italian industrial system.
Statistically speaking, FDIs in fact tend to increase in those economic systems featuring a greater presence of large companies, a major portion of intangible assets, and high capital intensity.
The Italian system, on the contrary, features a much smaller average company size than that of the other major European countries plus the prevalence of activities with low capital intensity.

Moving on, lastly, to the banking industry, I think it right to stress that, already today, Italy features a degree of openness to foreign investors that is significantly higher than that of some of the other major European countries.
If we analyse the ownership structure of the top 4 banking groups in some major European countries, it in fact emerges that, in Italy, some 16% of equity is held by foreign players, whereas this figure decreases to 7% in Germany, 3% in France, and 2.6% in Spain.
We can therefore state that, in the banking field, Italy is already on the right road to financial integration – as desired by the European Union.
In addition, the Italian banking industry also stands out for the great attention it has shown in the last few years to taking all investment opportunities in European markets capable of creating value.
UniCredit – the banking group I have the honour of leading - is undoubtedly one of the Italian players that has moved most dynamically in this direction. It has done so in the firm belief that, only by accepting the challenge of operating on a European scale, is it possible to look ahead with a view to playing a front-stage role.

Until today UniCredit's propensity to invest in European markets has translated into a series of acquisitions of primary banking companies in Central & Eastern European (CEE) countries. As a result of its investment strategy, the Group currently controls Bank Pekao, the main privately owned Polish bank; Zagrebacka Banka, the largest Croatian bank; Bulbank, the main Bulgarian bank; the Slovakian bank Unibanka; the Romanian bank Demirbank – now UniCredit Romania; and the Czech commercial bank Zivnostenska Banka. Nor should we forget the signature in Turkey with the Koç Group – one of Turkey's largest privately owned groups – for a joint-venture partnership in banking and financial services, leading to recent completion of the acquisition o Yapi Kredi, further strengthening our presence in a country that is drawing increasingly close to Europe and has enormous growth potential.

Today, however, talking about UniCredit means above all talking about its integration with the HVB Group – a deal that, to a certain extent, has redirected European markets' attention towards the possible start of a new phase of cross-border banking mergers.
With this deal the UniCredit Group has decided to address a major challenge – creation of the first truly European bank.
Before describing it in detail, a brief strategic consideration is in order – because without it full understanding of the deal's scope would be difficult.
The integration between UniCredit and HVB implies a complex deal whose ultimate objective is not to create an entity born of the union of an Italian and German bank, but to create a player borne from the two banking groups' adherence to a model that goes beyond the concept of border and frontier. The aim is to become a player operating effectively not only in the Europe of today but also – and above all – in tomorrow's Europe.
The UniCredit and HVB merger is first and foremost a major cultural challenge. It is the challenge of talking to 130,000 colleagues in the same language – and that means not a national language but the business language that is the quintessence of different cultures and professional experiences.
It is the challenge of creating a group capable of drawing on its best internal professional skills regardless of their geographical location or business culture of origin.
Being the first truly European bank also means being capable of becoming the "first-choice" bank for all our potential customers – and not only for the 28 million customers that we will serve immediately via 7,000 branches in the 19 countries where we are – and will be in future – a domestic bank.
Thanks to these facilities we will be able to operate in these countries with the strength provided by absolute leadership – and there is no doubt that, with these starting points, the opportunity is exceptionally attractive.

I am firmly convinced that this merger is the result of the two groups' awareness that they have chosen the best possible partner for a deal of this magnitude and type.
Integration of two groups that already on a stand-alone basis feature a good degree of business and geographical reach, will create a new group featuring a strong degree of business and geographical diversification. In terms of customer segments, an important point to note is achievement of a more balanced split between retail and corporate.
The new equilibriums that will be achieved will assure new growth opportunities and, at the same time, reduction of risks, thus permitting a whole series of benefits that it would have been impossible for the two stand-alone groups to achieve.
Lastly, the new organisation based on business segment will permit achievement of synergies and economies of scale above all in those segments where volume and "critical mass" are key and indispensable factors for success.

The new group's effectiveness in the various operating segments will also be assured by the creation of common product factories that, in future, will be able to supply a vast geographical market.
As regards this aspect it should also be stated that the new group will be leader in one of the wealthiest regions of mainland Europe. Both Northern Italy – where UniCredit's business is more heavily concentrated – and Bavaria where HVB's penetration is stronger, plus Austria, where Bank Austria has a strong market share, are areas featuring levels of wealth well above the EU average.
Operating as leader in this area will also be very important for the new group because it is also a key crossroad for a large part of trade with Central & Eastern Europe countries.
Whilst a significant part of the new group will be based where there is wealth, the other important part will instead be located where there is growth.
The new Group will also be leader in the Central & East European area – an area that stands out for growth rates – both present and projected – much higher than those found in the EU. Such leadership will be unquestioned also thanks to the size of the new Group, which – in terms of both total assets and physical presence – will, as already mentioned, be more than double that of the second player in the area.
The presence in New Europe will become a key asset.
We should not in fact forget that both UniCredit and HVB – although having different business histories - have, as regards New Europe countries, made very precise investment choices, daring in many respects and also totally similar. This lays the foundation for full acceptance of the commitment that the new Group will dedicate both to countries that joined the EU last year and to those that, in future, could join it - and to those that wish to become members and already today enjoy preferential relations with the EU.
In this area, both UniCredit and HVB can count on in-depth knowledge of the individual countries and proven ability to achieve growth and profitability targets, as well as on excellent track records in integrating and restructuring the banks in which they have invested in this specific geographical area.

The new group's key business-plan guidelines have been devised in such a way as to exploit the two banks' distinctive skills, which are also highly complementary.
In UniCredit's case its major skills are in retail, private banking and asset management, and operations.
In HVB similar levels of excellence relate to the corporate and multinationals & investment banking segment.

Going into greater analytical detail, it emerges that, in the retail segment, UniCredit has above all major commercial strength based on an advanced network management model and strong product innovation capabilities, also thanks to the possibility of exploiting centralised product factories. This competitive plus is largely the merit of the S3 process, thanks to which, in early 2003, UniCredit created three banks specialised by customer segment: UniCredit Banca in Retail, UniCredit Banca d'Impresa in Corporate, and UniCredit Private Banking in the Private segment.
In Private Banking and Asset Management UniCredit can count on the great experience that comes from its control of Pioneer – a global player in asset management that boasts stringent investment discipline and quality performance.

In Investment Banking UBM is positioned as Italian leader in risk-management solutions for SMEs.
Lastly, in Global Banking Services, UniCredit boasts major capabilities in terms of cost management and process re-engineering – once again based on the substantial experience acquired both in the restructuring efforts associated with the S3 process and to management of the Group's extensive organisation in New Europe markets.

These best practices and strengths of UniCredit fit very effectively with those of the HVB Group. In the Multinationals & Investment Banking area, **HVB** in fact boasts market coverage on a European scale with a clear customer and product focus. It also features major capabilities in the provision of products in the area of structured capital-market oriented financing and risk management. Furthermore HVB is a European leader in the role of credit arranger and distributor.
The HVB Group is also very skilled in the Corporate segment in Germany, confirmed by its excellent standing in mid-corporate financing, by its clear focus on commission-based business, and by its broad product range combined with strong product innovation ability.

The value of the integration with HVB, however, goes well beyond the results of the banking players involved. The merger is in fact able to present – in totally tangible terms – a new logic for cross-border banking mergers. This is also because the great determination of both parties to create a real financial group with a strong European vocation could do much to break down resistances that often slow down, hinder or even defeat many cross-border merger attempts.
In the second place we must necessarily hope that this deal will help to initiate a new phase of financial mergers in Europe. And news of the interest expressed by many banking players in merger possibilities in recent months seems to provide indirect confirmation of this. It is not, however, a question of merely hoping for the creation of larger players than those currently active in European markets but – rather – of creating much more efficient players, capable of exploiting the great potential that a European Union increasingly integrated in the financial field is already today able to offer.

Massimo Caputi

Ladies and Gentlemen, according to the view of Presidente Montezemolo, up to a few years ago, Italy had no policy to attract foreign investment to the country. A year ago, at an event promoted by the American Chamber of Commerce, the president of this organisation stated that no US company would ever invest in Italy, given the current business environment. Of the ten points he raised as highest for improvement, many had in fact, at that time, already been addressed by a range of Italian reforms, but there wasn't international awareness of this change and there isn't now either. Starting from 2003, we have:

First, labour market reform: new laws to boost flexibility. It is a very interesting law.

Second, corporate tax reform: simplification of procedures and the tax bracket reduction. All over Europe people know that now in Italy, taxes are very low.

Third, company law reform: simplifying and speeding up procedures for establishing a business. We have an investment gain if someone will study this new law.

On the remaining areas for improvement we are today addressing this through the "Invest in Italy" project. Today I am pleased to say that the Italian context for foreign investors is progressively changing and improving, with encouraging results to date. In less than two years we have succeeded in being acknowledged as the national investment promotional agency and in putting in world investment development as a priority on the economic policy agenda.

When considering the activities of UK Trade and Investment, which is the best case in the world, and Invest in Italy on the other side, one must consider the respective years of funding. The UK began actively promoting inward investment development over 25 years ago. Invest in Italy was only set up just over a year ago, in July 2004.

How far have we come in this first year? Regarding the activities covered so far, today we draw a positive balance. The implementation of the Invest in Italy project maybe consists in providing foreign investors with what they are really looking for when considering a country as a potential investment location: a single reference point, an effective one-stop shop to help them enter a specific market. The lack of this was exactly what foreign investors were previously complaining about when referring to Italy, but that was only the starting point.

To act as an effective entry point for foreign companies, we had to know exactly what their specific sectorial needs were and define a practical strategy to determine which target sectors in the countries we had to focus our efforts on. At the moment we have only five country targets.

Why choose the sector approach? It's probably not by chance that many countries have chosen such an approach. Identifying target sectors on which to focus the inward investment development efforts. When you are seeking to attract investment projects to your country, you must have a precise answer to investment needs. Only in this way can you increase your chance to compete successfully in the global arena.

What does the global arena look like today? The main observation is that the activeness of Western European countries is under heavy pressure originated by two main market strengths. First, the relocation to low cost areas both Eastern Europe and outside Europe such as China and India, that are also important markets. Second, outsourcing of activities to cost driven third parties. Our analysis of investment flows and stocks shows that pro-active sector targetting has been particularly successful in countries that are industrially advanced; countries where competition is less driven by cost cutting, but rather focussed on R&D and product development opportunities.

This was said by Presidente Montezemolo and it was also highlighted by the overall strategy highlighted in the Lisbon Agenda, which he hopes is not a dream. We are aware of the importance of acting accordingly and intend to deal with the stagnation of economic growth by making innovation the real motor for economic change of development. Therefore, we have adopted a model for our agency which is tightly connected to high-tech product development: the key to success in business today. Because of this goal, we have shared the sector approach within all 19 Italian regions and are carrying out an extensive promotional plan consisting in the organisation of relevant sectors and gains in the five target countries.

A number of other complementary measures have also been implemented. A business development network has been put into action in order to ensure the most effective direct marketing towards potential and prospective investors. We now provide a full spectrum of services along every phase of investment and business development. Project evaluation, location scouting, site visits, business set up, provisional incentives, grants and so forth, according to the European laws, management of relationship with local and national authorities, which has been a big problem until now in Italy.

Today we have a group of business developers operating both in our headquarters and key target countries to sell Italian investment opportunities abroad. Speaking about the UK, the data which my colleague gave are exact. We have developed a network of business pattern and sole relationship with institutions, but the two strategic sectors which are being targetted are ICT and biotechnology, for which we have organised sector events in London and Cambridge this year in order to raise awareness to promote focussed Italian investment opportunities. These sections are already taking shape with over 500 companies contacted to date in the UK and a significant number of leads.

Last, but not least we have set up a dedicated tool: the location agreement aimed at providing investors with customised turnkey solutions and incentives for setting up their business in Italy. The location agreement has produced significant results to date with definite investment amounting to some 3 billion Euros. The first location agreement was with a British company in tourism in 2004 for 109 million Euro investment creating 330 jobs with 44 million grants provided by us.

Of course we have only just begun and there is much work yet to be done to meet the challenges ahead. Our commitment is expected to increase and we aim to achieve greater results by focussing particularly on reducing red tape and bureaucratic complexities. That is the real problem that we have until now in our country.

Thank you.

Susan Haird

Ladies and Gentlemen, I am delighted to have this opportunity to speak at your annual banking and industry conference. Foreign direct investment is also a matter that is vital to the United Kingdom. My organisation, UK Trade and Investment, plays a very important role in this. I am therefore delighted that you have given me the chance to speak about the opportunities and benefits for Italian companies investing in the UK and to explore with you some of the issues facing UK companies doing business with Italy.

UK Trade and Investment brings together all the government services and activities supporting UK companies doing business abroad and oversees investment into this country. We are the UK's investment promotion agency, representing the whole of the UK. We provide a one-stop shop to overseas companies seeking advice and assistance in setting up and expanding their business in the UK. We work closely with our 12 partner agencies in the UK, the regional development agencies for England and the national agencies for Scotland, Wales and Northern Ireland.

For Italian companies, establishing in the UK is straightforward. The UK government actively supports inward investment from Italy. Italian companies, once they arrive, receive the same treatment as home grown businesses and of course there are no constraints on repatriation of profits into Italy or limitations on borrowing money. In addition, Italian businesses can easily find service providers in London, whether financial, legal or business consultants who speak Italian and understand their requirements. Many of them will be here in this room today.

So it is comparatively easy for Italian companies to do business in the UK and to feel at home here. My organisation has a dedicated team in the British consulate in Milan. They stand ready to assist firms with all aspects of locating or relocating a business in the UK or expanding their overseas facilities.

In 2004/5, 19 Italian companies told us they had established their operations in the UK. That created 292 new jobs and safeguarded an existing 820 jobs. The UK government sees foreign investment as essential to the long term health of our economy. Many studies have shown that it boosts competitiveness and introduces new practices and technologies. The figures show that the UK is still viewed globally as one of the best places in the world to do business.

So how do we help Italian companies? We provide a free and confidential service to companies. We put together a complete package of advice, guidance and support covering location, financial incentives, employment and market conditions, for example. We provide Italian companies with information on how to set up in the UK and we enable them to choose the best possible location for their company here. We give information about the national, regional and local incentives available to encourage investment. We offer help in contacting public authorities whether central government, local government nationalised industries or essential services like gas, electricity, water and telecommunications.

Now that I have spoken about the help for foreign investors from UK Trade and Investment, let's explore in more detail why so many companies do come to the UK. The
UK is the most favoured inward investment location in Europe, attracting about 40% of Japanese, US and Asian investment into the EU. We have much to offer overseas companies and our highly skilled, flexible, English speaking workforce provides an environment that allows business to prosper.

The UK's business environment gives every incentive for companies to grow, innovate and compete in the global market place. We have the lowest utilities cost in the European Union, our telecommunications industry is one of the most advanced in the world and we have one of the lowest main corporation rates of the world's major economies and there are no additional taxes on profits. The UK is also a global player in research and development, attracting an increasing number of international companies to fulfil their requirements here. We have a proud record in innovation and invention.

Among the major Italian companies who have already invested in the UK is Fiat, whose chairman is with us today, and who is also a major exporter from the UK. We also have Pirelli, Candy Hoover, Indesit and Benetton here together with Finmeccanica, which employs 10,000 staff in the UK and has become Britain's second largest defence company.

A study by this chamber has revealed that the stock of Italian foreign direct investment in the UK more than tripled between 1999 and 2002 from 1.5 billion to 5.7 billion. We now attract 11% of all overseas Italian investment.

I would now like to turn to investment in the other direction and look at investment from the UK into Italy. Historically, our companies have been attracted to the Italian market. Some 470 British companies have industrial subsidiaries in Italy, employing over 50,000 staff. Of these, 56% are based in northwest Italy and 25% in the northeast. There are some 250 British companies in the province of Milan alone and our investors can be found in every sector of the Italian economy. There is a continual flow of small scale investors from Britain, largely driven by merger and acquisition activity. The Turin Winter Olympics, for example, have generated great interest and have attracted some successful British architects and engineering companies.

However, with the exception of Vodafone and BG, who are developing a regasification terminal at Brindisi, we have seen few large investments by blue chip British companies in Italy in recent years. We remain committed to supporting British investors in Italy, one of the UK's most important markets, but I have to say that a number of businesses say that they are still deterred by the level and opaqueness (if I can use that word) of regulation, particularly at local government level in Italy. Confindustria and the Italian government are making great strides in tackling this problem and raising awareness of the importance of potential benefits of foreign investment to the competitiveness of the Italian economy and we heard about that in more detail earlier this morning.

We are particularly grateful in the UK to President Montezemolo with whom we have been working closely through our embassy in Rome to try to bring productive investment into Italy, for his untiring efforts. Again, we heard in more detail about those efforts earlier on this morning.

As I have outlined previously, the UK has benefitted from the increase in foreign direct investment. We welcome the benefits which growing Italian investment brings to the UK economy and the messages we hear are that Italian firms appreciate the UK business environment.

The UK government sees foreign investment as a key means of driving competitiveness in the UK economy and it has brought us very significant benefits in that regard. "Globalisation," to quote Bill Clinton, "is not policy, it is reality." Inward investment is a major driver of that, bringing capital, creating jobs, increasing technology, increasing competition and therefore competitiveness. These are crucial for businesses to adapt, survive and thrive in the globalised world we increasingly see ourselves living in.

In closing, I would again like to thank the Chamber for giving me the opportunity to take part in this conference. I very much hope this can be the start of our working ever more closely together to ensure an increasing amount of trade and investment flow between our two countries.

Thank you.

Question and Answer Session

Robert Leonardi

First for Mr Sunderland, when he speaks about the WTO and the liberalisation of trade and the extension of free trade at world level, we need to go back to one of the issues that wase important in the admittance of China to the WTO. What was reiterated at the time was that world trade does not mean a chaotic situation, but trade according to the rules, in terms of respecting the rules. This summer we had a problem when the rules were not respected and so there was a long negotiation that took place in order to make the transition and to get the goods that were piling up in the ports out to market. What should happen and what kinds of sanctions need to be applied when a violation of the rules takes place?

The second question is for Sir George Mathewson. He presented a very good picture of the problems that we have in the European stock market, but what is the solution, in terms of what should be done in order to overcome the current limitations?

John Sunderland

Well I'm not a very great believer in sanctions. It seems to me that the court of public opinion determines these issues and the reality is that you have to negotiate your way through them, but you don't get to the problem in the first place if you observe and acknowledge the transitions that you describe.

This event was known about for nine years. Many countries in Europe planned and prepared, many businesses planned and prepared, transitioned themselves to higher added value situations and those that didn't and ignored it suddenly found themselves facing a deadline. The reality for them and the only protection for them then is being protectionist. That's simply not the way to deal with these sorts of situations.

So, my simple answer is to avoid the need for sanctions. You avoid the need for the court of public opinion by making sure you prepare for these events, particularly when you know abut them for so long in advance.

George Mathewson

I think the question was that I had addressed some of the problems with the European stock market. That isn't really the issue. I think that for large companies we really need a global market. Large companies need access to a uniform global market with global investment indices. Certainly if we had an integrated European market, it would be an improvement from our current position. The reality is that large companies are now global and they need access to global sources of equity and a European market would not really do that. However, any integration of the markets within Europe would be a plus, bearing in mind of course that local markets can still serve a function for smaller local companies.

Robert Leonardi

How do we get there?

George Mathewson

Well, I think we should stop regarding stock markets as some index of national pride. A stock market is merely a facilitation of commercial deals. It doesn't have any real value in itself.

I would like to see the integration of large companies with the United States, Europe with the United States. That would be a big plus for Europe. I don't care where the market is based. Nowadays a market is based in your computer. The New York market, the London market, it's all rubbish actually. We're discussing fatuous things. The market is you and I buying shares wherever we are.

Mario Cotto - Sanpaolo IMI Management

Carlo Salvatori, I think that you had to manage many mergers between banks in Italy. I'd like to find out what you think about the difficulties that you met domestically and I would also like to know about the current operations: how you approached them and so on. I want to find out if you found major differences with the Italian experience or were there a lot of similarities?

Carlo Salvatori

I'm happy to say that we are having less problems than we were expecting to have on the basis of what happened in the past. I have been involved in seven or eight large mergers, but the important things are not so much the technologies or the organisational side of things. They are useful prerequisites. It is useful obviously to have technological platforms that work. The organisational set ups are very important, obviously. However, I believe that a merger is mainly based on the management of people.

When we talk about people, I remember the very first merger between Banca Cattolica and Banco Ambrosiano, the cultural differences and the fact that the people were in various places in Italy were not very different between the differences that you find between UniCredit now and HBB in Germany. Now this is where you can have success or where you can have failure.

I believe and so do my aides that a car can be changed or can be repaired. Organisational set-ups adapt. There is no organisation that for years remains the same. People have souls, hearts and minds. That is the most delicate element and if you respect people, if you keep them informed thoroughly, if you involve them in the solutions for the future, then this is fundamental in order to have a successful merger.

As you know, we don't yet have full control in the markets. There are issues of confidentiality when it comes to exchanging information. Bearing all this in mind, we have already set up tens of working groups and some of the objectives have been reached. We shared a lot of objectives. We know where we want to get to. Many people have defined these objectives, not just Italians, but also Germans, Austrians and people from other countries. As I said, we are going to have some problems. No integration between banks is a straightforward project. This involves three European countries, or rather 19 European countries, so there are difficulties; there will be difficulties, but less than expected. So far, that is.

Leonardo Simonelli Santi

Hearing Carlo's answer, which also put in to evidence the regional difference in Italy, I think I have a question for practically all the members of our panel. How do you coordinate the two aspects: globalisation and the need to be local? I think in Italy this is an argument that is discussed a great deal at all levels. So, starting with Confindustria or CBI and also the two agencies, what is the set up and how is the co-ordination between the Welsh Development Agency, the Scottish Development Agency, the Yorkshire Development Agency and so forth, the ETP and the other set ups that the regions have to attract local investment?

I think this is a very delicate aspect because it would be a catastrophe if the competition, which in a way is natural, became excessive. I think there should be a kind of coordination, always remembering that it should be easier to have cooperation within the border than cross border. It's true that fortunately enough the borders of Europe are disappearing, but I think there is still the obvious factor of language. I do hope that the coordination is strong so as to allow the different levels, regional, national and European, everything working together because as it is has been said many times that Europe gains in competition through that work. Thank you.

Massimo Caputi

Italy has 21 regions that less than two years ago promoted their offering without a national coordination, whereas today we try to represent Italy with an integrated approach. The actual situation shows that about 80% of productive foreign investment goes to Lombardy, around Milan, where our offer consists mainly in services instead of grants and soft loans. This puts in evidence that in order to attract inward investment, our focus, as a priority, has to be on improving the quality and level of these services. This strategy has to guarantee the continuity of the foreign investments

Susan Haird

You put your finger on something that is challenging for any country I suspect that is involved in inward investment. So far as the UK is concerned, my organisation, UK Trade and Investment, is quite clearly the national agency for inward investment. As I said in my speech, we work with 12 partners in delivering inward investment and those are the 9 regional development agencies that represent the different regions in England and the three devolved administrations.

I fully agree that the important thing is to promote the UK as the first line of attack as it were and my organisation puts a great deal of effort into promoting the merits of the UK as a very good destination for inward investors. That done, the regional development agencies and the devolved administrations are clearly very active in seeking to bring inward investment into their regions. We seek to coordinate that activity under the UKTI banner and we seek to do that both in the UK and overseas where a number of regional development agencies and the devolved administrations will have representation.

The way we try to approach it is by asking the regions and the devolved administrations to basically think very carefully about what they are offering, to remember that the customer needs to have a coherent offering, and that the most important thing is to actually attract the inward investment to the UK. So the more the regions are able to differentiate their offerings, by saying, "We are the best place in the UK to do nanotechnology or biotechnology," or whatever it might be, the better that is.

Marco Niada - Il Sole 24 Ore

I have a question for Mr Caputi and Mrs Haird.

If you start from the standpoint that the UK is one of the most open countries, most outward looking countries in the world and Italy is still lagging behind with one of the most inward looking countries of the industrialised nations. Mr Caputi, in a word, what do you think is our worst handicap that is keeping foreign capital outside? You mentioned before that it is a question of perception; we are still behind the curve.

Mrs Haird, what do you think was the greatest factor of success in attracting capital from outside into the UK? Of course, I know it is always a combination of factors, but is there a sort of killer solution?

Massimo Caputi

Many improvements such as; the new labour market reform in Italy, the new corporate tax reform in Italy and the new company law reform, are not known. As an international report said; Italy in 47th position as a business location. This kind of analysis shows that we have to inform more intensively, underlining the various factors that make Italy an excellent business location. For example how many international companies , wanting to invest in tourism, know the level of support Italy has to offer them?

After a year and a half's work we have reached some positive results but without any doubt there are still many things to do, taking in account we have started our activities 25 years after UK Trade and Investment, 37 years after the French and 10 years after CzechInvest.

Susan Haird

Well, it's very difficult, as the question realised, to pick any one thing, and if I may I'll pick perhaps three or four that I think are really important. I think our long track record of macro-economic stability is clearly very important. I think our flexible labour markets are also very important and, linked with that, our skilled workforce. I think the UK's strengths in research and development are also very important. Finally, I think a "can do" attitude among those responsible in my organisation and the regional development agencies and the devolved administrations, "can do" in terms of, "Yes, here is a potential investor we can make it easy for you to invest here". I think those are probably the four most important things.

Giuseppe Vigorelli - Banca Popolare Commercio e Industria

I would like to make a contribution. The relationship between globalisation and localisation, these are two realities that are often considered in conflict. I would like to refer to a study that has been recently published in Italy. Globalisation and localisation are two very positive developments. The more globalisation advances, the more local identities are emphasized. It is not the organisation or the information system, the product or services that are the key elements; it is the human factor that plays the most crucial role. The more we feel citizens of the world, the more we will try and find our roots through strengthening our local identity. It is a very strong human impulse to go back to your roots. The two processes will go hand in hand. This is just an opinion. Let us not think that globalisation doesn't open up any opportunities and is in conflict with the local identities.

I would like to ask you a question. I know that we have so many different markets in Europe, but is there a tangible project in order to bring to Europe the setting up of a single stock market or has this project been abandoned? Thank you.

Carlo Salvatori

I fully agree with your concept of globalisation and local identities. I believe these are two conflicting elements that need to coexist. Globalisation derives from the freedom of markets in the path that has been followed by the world markets. Local identities, in the historic tradition, are made up of achievements that have led to the definition of regional and local identities. We are trying to bring these two concepts together. We want to be a global banking group and our objective is that of covering 19 countries not forgetting that our success is linked with the way that a particular region reacts and responds. We want to think globally and act locally. So, we want to be as near as possible to the local realities. I think that there is a way of bringing the two together and we hope that through this approach we can be more effective in the future. Thank you.

Nicolo' Caissotti di Chiusano – Banca Nazionale del Lavoro

I have a question for Mr Salvatori. We have seen with pleasure that foreign investments in Italian banks far exceed foreign investments in countries like Great Britain, Spain and Germany. My question is if, and this is widespread opinion, the Italian banking system is less efficient, more costly, less innovative than the banking systems in some other European countries (this is what we hear: Italian banks are more expensive, they are not innovative, they are lagging behind in relation to other banking systems, yet in our sector there are foreign banks), is their participation in the Italian banking system not felt in terms of increasing innovation or is it just a type of financial participation which has very little impact on the actual operation of the banks?

I disagree with the fact that Italian banks are less efficient, less innovative and more costly than the European banks. Ten years ago, we discovered market economy too, we found out how to operate in a market which is open to competition. I believe that the efficiency levels of Italian banks on average have gone up greatly. We believe that we are rather efficient even in relation to the best European practices. Obviously this has been greatly helped by closer contact with foreign banks. There was a quality gap up until a few years ago. We managed to bridge that gap because we were shown a path, a path towards efficiency and also in terms of use of capital. We need to use the capital correctly and the risk adjustments. Therefore you need to find better and better efficiency conditions.

Italy is a country with many different aspects, like other countries. We don't just work in Italy, we work in Europe, and so we need to be efficient in order to compete. I believe that Italian banks are ready to face international competition. Personally I am not afraid of operating in international markets.

George Mathewson

Could I start by congratulating UniCredito on their merger with HBB. On this matter of efficiency, I think UniCredito stands, frankly, like a beacon in Italy.

There is also a matter of scale and there are still a lot of consolidations to happen, probably, which should improve overall efficiencies. I also think that banking is relevant to the globalisation versus local question. It depends on the products; it depends on what your customers are. There are some products which, frankly, are global products and you deal with them on a global basis. There are other products which are delivered locally by local people. There your organisation has to organise for the local delivery of these products. In certain cultures your organisation has to recognise the effect of the culture in that particular area. I think this is the same for banks throughout the whole world. Even in the United States there are local differences which are very substantial. We own a very substantial bank in the United States and throughout the US market they have all the little problems that we have anywhere else.

Again, I would congratulate Carlo on what is the first truly European merger. I also wish him the best of luck with mergers. We did a merger with Natwest which has been extremely successful, but I have to say that I think one of the reasons it was so successful was that it was not a merger, it was a hostile takeover.

Domenic Pini - Pini Bingham & Partners

I just wanted to ask a question to Susan Haird.

You've mentioned all the advantages of inward investment into the UK. One of the problems that we've got, I think, which hasn't been mentioned, is the operational difficulties that sometimes we encounter when bringing Italian companies into the UK. The investment into the UK sometimes confronts difficulties, particularly in respect of opening of bank accounts for foreign companies where you have multi layered companies with many different types of shareholders. In order to identify the majority shareholder sometimes requires 3-4 months of investigation. In one particular case when we came across a participation by the region of Trento, it was impossible to obtain documentation from the region in order to satisfy UK money laundering regulations. So perhaps UK Trade and Investment could bring their consideration to a rather rigid process of opening accounts, which then prevents the whole business from kicking off. That's half the difficulty at the coalface as it were.

Susan Haird

First of all, let me say that wherever inward investors or potential inward investors have problems of this sort, or different ones, we are always very willing to help and indeed keen to help to try and resolve them.

In terms of the broader issue of money laundering rules and indeed other potential issues that face our inward investors, we do see a key part of our role at UKTI as being to act as the voice of inward investors in Whitehall. We do as a matter of normal practice collect the views of inward investors in a very structured way and we feed those views back to ministers and senior officials in other government departments. So, we have a number of issues that we know are of concern to inward investors, some of which would equally be of concern to domestic industry, and we do ensure that those views are fed in.

George Mathewson

I do wish from the banks' viewpoint that they listened more to you.

Alberto Bertali

I wanted to ask Mr Sunderland a question. We talked this morning about globalisation. As a manager or entrepreneur we would obviously like less regulation, but if you turn things around, the process of globalisation for countries like Italy and the United Kingdom sometimes means loss of jobs and loss of security. We just relocated from Scotland to China and 1,000 people in Scotland lost their jobs. They lost their security, their pension schemes, and so on. Some retired; some went to work, for example, in less secure jobs. Now, I'm not saying that we shouldn't do it, but it's a doubt that I have in my mind: what is the future for these people and for others that will follow?

John Sunderland

This is clearly not an easy issue, but globalisation is a reality and the reason that perhaps you are here in the UK in the first place is that we have an open, liberalised economy and we welcome the businesses that come, and we accept the reality of those that, for whatever reasons, depart.

On the issue of UK competitiveness, I will just make the observation that when I was in the United States, in Silicon Valley, towards the end of last year and every one of the half a dozen CEO's of major US corporations who I asked where, if they were investing in Europe, they would choose to invest, I can tell you that every single one said that they would not under any circumstances invest in countries like France or Germany. One American CEO, of a very, very famous corporation, in that rather pithy way that Americans have, said, "If I can't fire them, I won't hire them". So the reality is that labour is a flexible commodity.

Of course, the other side of that coin is that if you are one of those 1,000 people in Scotland, the loss of your job and the consequences for you and your family can be very profound. I think we in business have to do all we can to recognise that. At the national level, despite all the sorts of trends you're describing, the UK has full employment, we reckon that the outsourcing of jobs that has gone on to other parts of the world, particularly the East and to Asia, have actually added to our GDP because the consequences of taking those people and re-skilling them, hopefully up-skilling them to do higher added value jobs is part of the progress of our economy and society. So we tend to take a rather different view.

On the practical realities, all my experiences of labour flexibility suggest that if you work hard at it, you help the displaced people with outplacement. In other words, you help them to go out and find new jobs, new work, you help them through retraining and up-skilling. The very great majority, I'm talking about 90-95%, do find more work, but if we hide and pretend that this reality is not with us, then all we do is delay inevitably the day the consequences can sometimes be more profound. The 6,000 workers who worked at Rover in Longbridge, in Birmingham found this out to their cost. If that situation had been addressed many years previously, I'd like to think they would have been re-skilled and retrained and found other employment along time ago rather than being faced with the predicament that they were.

George Mathewson

Obviously this is a question close to my heart.

In 1981 I was Chief Executive of the Scottish Development Agency and was deeply involved in both bringing manufacturing industry into Scotland and rescuing companies, etc. and that was under the Thatcher government. At that time, employment manufacturing in Scotland would amount to between 20-25% of the workforce. Employment manufacturing in Scotland now is around 12-14% of the workforce. Unemployment is practically zero in Scotland now. Back then unemployment was in the high teens.

It is an inevitable fact that manufacturing jobs will decline in the most advanced countries. The United States, once the biggest manufacturer in the world now only has 11% of its workforce involved in manufacturing. This trend is something that is a fact. One can fight against it, one can be nostalgic for the past, but that isn't going to help the situation. The reality is that the growth of jobs in the advanced economies is in the service sectors and you are much better to go with it than to fight against it. That is why nowadays we have, in Scotland, a service dominated economy with practically zero effective unemployment compared to an economy which was dominated by the older manufacturing industries and which had a far lower standard of living than we have today.