

## Italy

### I. Current National Security Situation

Currently Italy views itself as a medium sized power participating in the grand security alliance of NATO and in the European process of integration. At the same time, Italy intends to assume a higher profile and greater responsibilities in the geographic areas in which it has immediate security interests. The region including the Mediterranean as far as the Persian Gulf, Central/Eastern Europe, the Balkans, and Turkey with a push in the direction of the Caspian Sea area and Central Asia is seen to be the nerve center of future European stability and of Italy's interests.<sup>1</sup> The Italians do not see themselves acting alone in any regional confrontation but rather as part of a community of European nations acting together to resolve issues and differences that will disrupt the political and economic stability of Europe.

In the absence of any direct threat to its national security, Italy has chosen to declare a series of issues that are significant to its national interests.<sup>2</sup> Italy has a strong geo-strategic interest in bringing Russia back into the international community through a stronger bilateral partnership. Italy is also committed to stabilization in the Balkans to prevent further fragmentation. Italy's strategy in the Persian Gulf is based on containment of Saddam's threatening ambitions by constant surveillance on Iraqi programs and by maintaining Italian military capabilities in a state of readiness for possible intervention. Italy has also embarked on a strategy of normalizing relations with Iraq's neighboring countries such as Iraq and Turkey. Italy regards the Middle East as an area filled with dangers and uncertainties.

#### *Armament requirements*

To meet these needs, Italy has embarked on a major defense reform to create a "New Defense Model." The objective is a well-balanced military force that is small in size but high in quality, to include adequate strategic mobility and logistics autonomy for out of area operations and appropriate capabilities to permit easy integration with allied or coalition forces. Because of Italy's geo-strategic position in the Mediterranean, the threat from possible attacks by ballistic missiles and weapons of mass destruction (especially from the Middle East) is an important concern. Since Italy is not a nuclear power that can invoke deterrence to forestall attacks, effective air and missile defense is viewed to be an essential element of Italy's future military force posture.<sup>3</sup> In addition to general modernization of its land combat and naval systems, Italy also needs to provide greater sustainability and force protection for its forces in out-of-area operations.<sup>4</sup>

Italy's naval strategists have further argued that, with the Cold War over, it is necessary to focus on naval projection in the Mediterranean. Since Italy's naval forces are becoming obsolete, a major modernization program is required. This program should include a second light carrier with amphibious capabilities, two anti-air warfare frigates, a

new generation of multi-role frigates, eight additional coastal ships, and modernization of the helicopter fleet.<sup>5</sup>

The Kosovo campaign also demonstrated to Italy the difference in military capabilities between the United States and Europe, especially in strategic mobility assets and strategic and tactical intelligence systems. This means that Europe (and Italy) must focus on those fields, as well as on increasing cooperative development efforts with the United States. Italy believes that the US will remain the leading country in high-technology for many years.<sup>6</sup>

### *Defense budget*

In 1997, Italy's military expenditures were \$22.7B (1997\$US) compared to \$22.7B (1997\$US) in 1991.<sup>7</sup> This level placed Italy 8<sup>th</sup> in the world in 1997.

Projected defense procurement expenses for the 15 years starting in 1998 are about \$70 billion, of which \$50 billion will be spent on major defense end-item programs. This establishes a requirement for average yearly allocations of approximately \$4.5 billion for armaments.<sup>8</sup>

## **II. National Defense Industrial Base.**

There are currently three main players in Italy's defense industrial sector: the state owned Finmeccanica Group which controls about 70 percent of Italy's defense and aerospace industry, the private-owned FIAT Group and the Marconi-Italiana Group which is a subsidiary of the new UK defense giant BAE Systems.

### *Finmeccanica*

Finmeccanica, owned approximately 65 percent by the Italian government, has about 28,000 of its 60,000 total employees dedicated to defense related work and had 1997 defense and aerospace billings of nearly \$3.5 billion. About 65 percent of Finmeccanica's annual revenue comes from defense and aerospace, and two thirds of the annual revenue is from export markets.<sup>9</sup>

Alenia Aerospace is the largest of the Finmeccanica subsidiaries with 1997 revenues of over \$1.9 billion.<sup>10</sup> Most of that is concentrated in the EF-2000 Eurofighter program and the start of a new C-130 transport version in conjunction with Lockheed Martin and other avionics systems partners. Alenia Difensia is the second largest Finmeccanica subsidiary with 1997 sales of approximately \$2 billion. Difensia's main product lines are: radar, missiles, naval artillery and radar systems, and avionics. Alenia Spazia with 1997 orders of approximately \$688 million is focused on the international space station to support the European Space Agency (ESA) and NASA requirements, the SICRAL communications satellite for the Italian military, the European Helios 1 military observation satellite and other communications satellites for commercial applications. Agusta, currently a

helicopter and systems company, is the smallest of the subsidiaries with 1997 orders of \$526 million.

### *Fiat*

The second major participant in Italy's defense industrial base is the Fiat Group. Fiat has about 8,800 employees with orders of approximately \$1.7 billion in its aerospace and defense business sectors. Fiat accounts for about 30 percent of Italy's defense industrial sector. Fiat's strategy is to act as developer and producer of major defense subsystems using technologies already developed for other applications to keep costs down. Because of the magnitude of the required investment, Fiat does not intend to develop complete defense systems that will have to compete in a shrinking market, but rather to remain a specialist in niche areas that can be supplied to everyone. Thus Fiat does not even have a dedicated defense division. Fiat's defense business accounts for 3.9 percent of the revenues of the Fiat Group. Even though this is a small percentage, Fiat views this to be an important element to be maintained and supported in the future.<sup>11</sup>

Fiat's defense and aerospace business is organized into several major product lines.<sup>12</sup> Fiat Avio is Italy's largest aircraft engine industry. It is involved in designing, developing and producing engines and transmissions for military and commercial fixed and rotary winged aircraft. Avio also produces solid rocket fuel motors, fire control systems, ammunition and warheads for missiles and rockets, and vehicle training simulators. Fiat's Iveco Military Vehicles Division develops and builds tactical and logistics vehicles and is partnered with OTO Melara to develop and produce wheeled and tracked armored fighting vehicles.

### *Others*

Marconi Italiana is the Italian Branch of GEC Marconi with orders of \$909 million and 7,000 employees, 80 percent of them in Italy. The company develops and produces communication, EW, radio navigation, avionics, military computer, satcom and IFF systems.<sup>13</sup>

The remaining major organizations in Italy's defense industrial base include Fincantieri, whose Naval Shipbuilding Division is responsible for designing and building both surface vessels and submarines, including all of the major ships in the Italian Navy. Another company, Elettronica, specializes in electronic warfare systems design and production.

### *Italian Global Top 100 Defense Industries*

In 1991 Italy had two companies in the global top 100 defense industries as measured by annual defense revenue. Those two companies had a combined defense revenue of about \$961M (1991\$US).<sup>14</sup> By 1999 that number had dropped to one (Finmeccanica), but with an increased revenue of about \$1.2B (1999\$US).<sup>15</sup> The largest Italian company (in terms

of annual defense revenue) ranked 28<sup>th</sup> globally in 1999, compared with 65<sup>th</sup> globally in 1991.

### **III. National Armament Strategy**

Italy's armament strategy is one of procuring defense systems for its armed forces largely from indigenous manufacturers or from those foreign firms with which Italian industry has cooperative development and production arrangements. As of 1997, Italy had 25 active defense cooperation agreements including 15 with non-NATO countries.<sup>16</sup> Important cooperative ventures with the other European Companies include the Eurofighter 2000, the Horizon Frigate, the Mu-90 Lightweight Torpedo, the NH-90 Helicopter program, and the Future Large Aircraft (FLA).<sup>17</sup>

At the same time, since 1991 Italy's defense budget, in real terms, has declined steadily. This has led to decreases in R&D and delays in nine major armaments programs including the EH-101 heavy helicopter, the second batch of A-29 attack helicopters, the Sicral military communications satellite, and the Ariete main battle tank. Available funding has concentrated on programs that are more advanced or for which there are international obligations (Eurofighter 2000, the Horizon air defense frigate, and the Future Anti-Air Missile System under joint development with France).<sup>18</sup>

Italy also has recently turned to imports to support a newly-reorganized Armed Forces designed to cut manpower by 25 percent and simplify the command structure in order to create a lower-cost more mobile force. A limited purchase of new C-130J transport aircraft from Lockheed-Martin is desired until the European Future Large Aircraft becomes available. Italy also has assessed the US E-2 Hawkeye early-warning aircraft as a candidate to support naval operations.<sup>19</sup>

#### *European armaments cooperation*

Italy strongly supports the development of a consolidated European armaments process. The urgency for a consolidated European approach stems from the creation of large defense industrial companies elsewhere and from increased global competition. Italy supports the efforts of the thirteen Western European Armament Group (WEAG) countries to eventually create a European Armaments Agency (EAA), recognizing that there are still many obstacles. These include the political issues associated with surrendering some aspects of national economic, social, and security plans to a European structure. LT Gen. Alberto Zignani, Italian National Armament Director, will become the president of the WEAG starting in January 2001.<sup>20</sup>

In November 1996, Italy, along with France, Germany, and the UK, became signatories to the establishment of the Organization Conjointe de Cooperation en matiere d'Armement (OCCAR) to handle selected multi-national programs. One major aim of OCCAR is to create European synergism and standardization with respect to acquisition procedures, policy standards and product standards.<sup>21</sup> Italy views OCCAR to be an important first step toward the creation of the EAA.<sup>22</sup> Subsequently, Italy became a

signatory to the 1998 Letter of Intent with four other countries (France, Germany, the UK, and Sweden) to pursue better conditions of defense-industrial integration.

Italian industry believes that it can offer solid technical expertise, modern and in some cases advanced production facilities, developed infrastructures, and relatively low labor costs. Italy's model should be that of a niche player not unlike that of Singapore or South Korea.<sup>23</sup> Broad areas of Italian strategic competency include helicopters, defense electronics, space, and aeronautics.<sup>24</sup>

Italian defense industry and the defense ministry have also argued that Italian political consistency and support for Italy's new defense industrial strategy in a broader European context is urgently needed. Specific requirements, to be done in conjunction with the other European governments, include: unification of procurement policies and procedures, synchronization of pricing and standards associated with government procurements; unification and liberalization of the European internal market; and unified regulations governing defense exports.

One of the major factors motivating these needs is the consolidation that has already occurred in the United States, creating the large defense giants Lockheed-Martin, Boeing, and Raytheon. These companies can operate in a single domestic defense market and a single regulatory system, and also have the working capital to operate globally.<sup>25</sup>

#### *Arms import level*

In 1997, Italy's import level was \$430M (1997\$US) compared with \$430M (1997\$US) in 1991.<sup>26</sup> This level placed Italy 24<sup>th</sup> globally in arms imports.

#### **IV. Perspectives on the International Arms Export Market**

Since 1992 the reduction of Italy's defense budget has created an urgency to turn to exports as a means of keeping supporting Italian defense industrial infrastructure. In the past, Italy has been a major exporter of armaments. In the 1970's and early 1980's Italy achieved significant success in the export of naval vessels. In subsequent years, however, due to a series of political, legal, financial and technological factors, Italy became progressively unable to maintain its previous market positions against the competition.<sup>27</sup>

#### *Causes of decline*

Italy's defense export profile declined significantly over the last fifteen years under three principal influences. The first was Italy's current export regulation, Defence Export Law No. 185. This was passed in 1990, triggered by political decisions to withdraw Italian commitments to provide naval forces to Iraq in the mid-1980's. The law contains many ambiguities and a complex set of approval and reporting procedures. The four years it took to pass the law also created a waiting period that curbed Italian defense industry's international activities.

The second factor of influence was the abrupt decline in international demand, coupled with the changes in global defense industries and markets that followed and the new era of a buyer's market supported by strong international competition. Italian industry was not prepared for the new market requirements and furthermore was the weakest of the European defense industries. The third factor was the glacial pace of transformation of the Italian Armed Forces to meet the new security conditions.<sup>28</sup>

### *Arms markets*

Currently the United States is Italy's main customer. In addition to the United States, Italy's top five arms export clients are the UK, France, Germany, the Netherlands and Sweden. Most sales are concentrated in the sectors of aircraft, heavy armaments and missiles. This concentration is a worrisome feature to Italian exporters who see that the key to a healthier and more resilient arms industry resides in a significant expansion of exports into the non-NATO countries. Even with relative large volume of defense sales, Italy is the weakest among the four main European arms producers.

Both the Italian defense ministry and Italian industry are also actively pursuing new external markets. Finmeccanica has developed a cooperative relationship with Russian defense industry, signing an agreement in November 1995. The agreement initially focused on helicopters, jet trainers, and avionics, but is planned to be extended to include aircraft manufacture, satellite communications systems, defense industry conversion, radar technologies, and electro-optic sensors.<sup>29</sup> The Italian armaments director has also visited Israel to explore the possibility of high-technology defense industrial cooperation. And, unknown to the Italian armaments ministry until it happened, Augusta separately signed an agreement with Israeli Aircraft Industries to bid on the Turkish attack helicopter procurement.<sup>30</sup>

Part of Italy's new arms export initiatives focus on the training market. For example, in 1999, the Italian and Russian governments signed an agreement for joint development of an advanced trainer aircraft by Aermacchi SpA, the Yakovlev Design Bureau, and Sokol. The aircraft would be sold on the global market. The trainer reportedly can train pilots to fly the Russian Mig-29 and Su-27, the French Mirage-2000, and the US F-15 and F-16 fighters. The new trainer is competing in the short term against a trainer designed by Russia's VPK MAPO to supply the Russian Air Force.<sup>31</sup>

Italy's Alenia also has a joint venture with Lockheed Martin to produce C-27J Spartan tactical transports. Twenty seven aircraft have been sold to the Italian Air Force with additional purchases being considered by Australia, Greece, Switzerland, Malaysia, and Poland.<sup>32</sup>

Italy has signed 43 bilateral cooperative agreements in the last few years. These include not only the NATO countries, but also those of Eastern Europe, the Middle East, North Africa and the Asian-Pacific region.<sup>33</sup> The Asian-Pacific market is one of Italy's main targets. Recent naval customers include Malaysia, Thailand, Australia, and South Korea.

Italy has currently committed 55 percent of its defense investment funds to help develop international cooperative programs.<sup>34</sup>

### *Export controls*

A significant risk to Italy's defense industry in terms of its ability to expand its participation in the global armament system lies in the complex approval process for the transfers of Italian arms to most non-NATO countries. Italy's arms export rules establish a long and complex approval process and this puts them at a disadvantage vis-a-vis their European competitors. As an example of how constraining Italy's export regulations are, Italy cannot authorize a partner in a joint cooperation program to export a final product. This means that Brazil, for instance, could not export the AMX light fighter with which it is engaged with Italy in a co-production effort without receiving Italian approval.

These regulations, among the most restrictive of the European nations, prevent the Italians from being considered reliable partners in arms transfer agreements, joint ventures, and co-production agreements outside of the NATO community. NATO has learned to accommodate the Italian export regulations although such accommodation has cost Italy significant participation in the development of some systems for export to consumers outside NATO.

Italy has also experienced problems stemming from US export control regulations. In June 1999 Alenia Aerospazio signed a contract with Eutelsat to deliver the Atlantic Bird I satellite to orbit by June 2001. Subsequently, Alenia contracted with China's Great Wall Industry Corporation to launch the satellite. US suppliers experienced delays in providing needed satellite components to Alenia because of US export control procedures. This has prompted Alenia to start to switch to European or Japanese suppliers.<sup>35</sup>

### *Reevaluation*

In 1998, the Italian defense ministry began to rethink the entire situation of Italian defense exports, resulting in the identification of several problems that are currently trying to be resolved. These are: difficulty in participating in European defense integration, whether via government-to-government agreements for cooperative developments, industrial mergers and acquisitions, or coordination of defense export policies; industrial difficulties stemming from the complexity and ambiguities of the export approval process; and inconsistent interpretation of export regulations by successive Italian governments, causing problems with fulfilling agreements previously made. Since then, some new procedures have been introduced to simplify the export process, the government has become involved in the development of offset packages to meet the requirements of international competition, and Italy strongly supports European defense integration. However further streamlining is still required if Italy's defense industry is to maximize its participation in the global defense market.<sup>36</sup>

### *Arms export level*

In 1997 Italy had an arms export level of \$0.7B (1997\$US), compared to \$0.34B in 1991 (1997\$US).<sup>37</sup> This placed Italy 8<sup>th</sup> globally.

## **V. Transformations in the Defense Industrial Base**

To promote efficiency in armaments, part of the Italian defense restructuring effort has combined several armament related functions into a new combined General Defense Secretary and National Armaments Director (SG/DNA) with responsibility for both defense industrial strategy and the armaments process. One of the challenges is to create an industrial strategy that will maintain key Italian defense capabilities. This implies that the Italian defense industrial base must have the resources and freedom to be effective in competitive global markets, to include active pursuit of international cooperative activities. In turn, the defense industries must be structured efficiently, be flexible in their ability to meet market demand, have an efficient commercial support network, and be involved in several well-conceived alliances with leading foreign industries. One of the missions of the SG/DNA is to actively promote international industrial cooperation, especially involving the high-technology sectors.<sup>38</sup>

Italy's has also prepared a grand design for defense consolidation: sector oriented joint ventures that cut across borders but still safeguard the strengths of its national industry. This has resulted in several joint ventures established as test cases for Italy's defense consolidation strategy.

### *Restructuring Finmeccanica*

Finmeccanica began the transformation in 1994 when it took over the state-owned Ente Partecipazioni e Finanziamento Industrial Manifatturiera (EFIM) Group. This Group included Italy's major helicopter manufacture, Agusta, an electronics company (SMA), the sensor company Galileo, the light artillery maker Breda, and the naval arms and armaments producer OTO-Melara. To assimilate these capabilities, Finmeccanica created a new management structure dividing its defense operations into three groups: helicopters, avionics and equipment, and armaments.<sup>39</sup> This acquisition gave Finmeccanica control of about 70 percent of Italy's defense industry. As a part of the acquisition, the Italian government also guaranteed to Finmeccanica a stable order flow, sustained R&D funding at previous levels, financing of restructuring costs, and help promoting exports. One of the government's rationales in establishing Finmeccanica as the single Italian missile manufacturer was to posture Italy to play a more active role in the anticipated restructuring of Europe's missile industry.<sup>40</sup>

Finmeccanica is also heavily engaged in the commercial market. In 1994, defense revenues accounted for only 17 percent of the company's total revenues. After restructuring was completed in 1995, Finmeccanica began to focus on export sales, with a goal of rising to a level of 70 percent of its annual defense revenues coming from the export market. To support this goal, Finmeccanica depended on a change in government



policy that will relax the restrictions on export sales that are automatically prohibitive to countries no longer embargoed by the United Nations. The planned increase in export sales was expected to come from four major operating companies: Agusta (helicopters), Otobreda (ordnance and vehicles), FIAR (avionics and systems), and Alenia (aerospace, especially tactical missiles). Finmeccanica's international business strategy focuses on joint ventures rather than mergers with larger European groups for fear of eventual takeover.<sup>41</sup>

In 1995 Finmeccanica's parent state-owned company, Istituto per Ricostruzione Industriale (IRI) was heavily in debt. This led to considerations within the Italian government to split or sell Finmeccanica, which is one of the most attractive IRI assets. IRI viewed the most attractive option to be the split of Finmeccanica, privatizing the civilian sector elements to generate revenue while keeping the defense and aerospace businesses under state ownership. Finmeccanica leadership opposed this plan, arguing that future survival depends on maintaining a diversified civil-military high technology business base.<sup>42</sup> Nevertheless, in May 1997 IRI announced intentions to divide Finmeccanica's assets into three companies (Alenia Aerospace, Alenia Defense, and Agusta) and privatize them separately.

This action led to the prompt resignation of Finmeccanica's CEO, Fabiano Fabiani, arguing that this step would lead to the "transformation of its best industrial properties into subsidiaries of competing foreign groups."<sup>43</sup> The IRI approach was diametrically opposite to the consolidation initiatives that Fabiani had been pursuing over the last three years, although in pursuit of the same declaratory objective—to facilitate international agreements. Italian defense industry analysts expressed concern that the reversal would increase costs and inject delay, which in turn may prevent Italy from full participation in European-wide consolidation and restructuring.<sup>44</sup>

In 1998 Finmeccanica's leadership argued that she had been able to maintain her competitive position in radar, missiles, naval weapon systems, satellites and fighter aircraft. At the same time, she urgently needed to pursue four priority areas: partnership entry into the Airbus consortium; completing the GEC-Marconi joint venture arrangement; integrating Agusta with either Westland or Eurocopter; and concluding a space-sector alliance with either the Matra-Marconi Space-DASA or the Alcatel-Thompson-Aerospatiale groups. These were seen to be strongly interrelated measures to both insure Italian participation in the major European consolidation initiatives and also to motivate Italian industry to achieve the level of modernization and efficiency associated with the high standards of the UK.<sup>45</sup>

#### *Further restructuring complexities*

As European defense industries reacted to the opportunities presented by merger and privatization potentials, new complexities arose for the Italian defense industry. In December 1998, a merger between GEC plc (UK), Marconi Electronic Systems, and Alenia created Alenia Marconi Systems (AMS), (equally owned by GEC and Finmeccanica). Finmeccanica's strategic agreement with GEC-Marconi established the

basis for cooperative alliances in defense electronics, missiles, and other weapons systems activities. The team is especially strong in surface-to-air missiles. Finmeccanica is strong in platform development and production and GEC is strong in systems integration.<sup>46</sup> The 50-50 joint venture, Marconi-Alenia, comprises two separate companies and would be incorporated in The Netherlands.<sup>47</sup>

After the merger was completed, British Aerospace purchased the defense elements of GEC, including its ownership of half of AMS. The result was BAE Systems, the first European defense giant. Some Italians reacted negatively, arguing that this is the kind of action that will threaten to absorb Italian defense industry into larger conglomerations based on financial investment considerations rather than on preserving national elements. In reaction, Finmeccanica began negotiations with British Aerospace to repurchase its share of AMS.<sup>48</sup> As a result of further discussion and agreements between Finmeccanica, BAE Systems, and Aerospaziale Matra, the missile systems capabilities of AMS were internally transferred to a Matra BAE Dynamics. In return for AMS received the surface-based radar, land, and naval systems capabilities of BAE Systems. This action further consolidated the European missile industry. It also resulted in a new position for AMS as the largest C2, radar, and systems integration company in Europe.<sup>49</sup>

Subsequently, both of the new large European defense giants, BAE Systems and EADS, offered to form a military-aircraft joint venture with Finmeccanica's Alenia Aerospazio subsidiary. As a matter of policy, Finmeccanica did not intend to join either company directly but rather intended to emphasize partnerships targeted to specific industry sectors.<sup>50</sup> According to defense industry analysts, the BAE Systems offer was not based on a 50/50 joint venture because of the unequal size of the two companies, whereas the EADS offer not only proposed a 50/50 split, but also offered Finmeccanica an equity share of EADS.<sup>51</sup> Finmeccanica subsequently decided to accept the EADS offer, judging that it would better support Italy's objective of improving its domestic defense and aerospace industry. A part of the EADS offer was the opportunity for Finmeccanica to acquire a 5 percent equity share of the commercial Airbus Consortium.<sup>52</sup>

The new company is expected to be a major player in the world defense aerospace market, with special strengths in combat aircraft, military transport aircraft, special mission aircraft, and trainers. The new company will have at least three subdivisions—Italian, German, and Spanish—because of the lack of common national laws and regulations governing transnational corporations. Additionally, the new company has been approached by the Greek Hellenic Aerospace Industry (HAI) with an offer to have it acquire a 49% equity share of HAI (which has also been offered to Dassault).<sup>53</sup>

### *Privatization*

Although Italy already has accomplished a significant reorganization of the defense industrial sector, there are two main weaknesses: the fraction of public ownership is still too high, and the overall size of the sector is small when compared with other European countries.<sup>54</sup> To better support the process of European consolidation, there has been a clamor throughout the industry for full privatization of Italy's defense industry. As a

precursor to this, several Finmeccanica subsidiaries have engaged defense industries in France, Germany and the U.K in cooperative agreements for joint bidding as well as production without the direct involvement of the Italian government.

### *European consolidation*

As significant cross-border consolidation began in Europe, Italian defense industry leaders became concerned about being left out. In the early 1990's, the fact that Italian defense industry concentrated on internal restructuring had put them behind as companies in the other countries began to focus on cross-border teams. At the same time, they realized that their companies were less attractive to the consolidated European companies because of their eroding revenue base. They concluded that in order to remain attractive partners, their strategy must specialize in specific areas of excellence in order not to become overextended.<sup>55</sup>

With these concerns in mind, Italy is moving aggressively to try and create relationships between the Italy's defense industry and those of the other European companies. Ministerial level discussions have concentrated on the relative role to be assigned to national defense industries and corporate discussions are taking place between Italian industry and European-wide firms. Domestic actions in Italy are focused on creating the supporting administrative and procedural regulations and processes. A major concern is also the preservation of Italy's technological base within Italy. At the same time, the need for a European-wide approach is seen to be essential.<sup>56</sup>

In parallel Italy believes that she must increase the technological level of her defense industry to demonstrate that she can be an effective participant in the European consolidation process. This means that either the Italian government must raise the magnitude of defense-industrial investment or significant levels of foreign investment must be secured.<sup>57</sup>

## **VI. Risks and Concerns**

- Since 1992, the reduction of Italy's defense budget has created an urgency to turn to exports as a means of preserving her defense industrial infrastructure.
- Italy is concerned about being left out of European cross border mergers, while at the same time fearful of relationships that could result in takeovers and subsequent loss of technological capability to Italy. As a result, Finmeccanica's international business strategy focuses on joint ventures rather than mergers with larger European groups for fear of eventual takeover.
- Italy believes that the new transnational companies emerging from the European defense industry consolidation will not be able to operate efficiently unless and until the defense requirements, policies, and procedures of the European countries are standardized.

- Italy's arms export rules establish a long and complex approval process and this puts them at a disadvantage vis-a-vis their European competitors and prevent the Italians from being considered reliable partners in any agreements of arms transfers as well as joint ventures and co-production agreements outside of the NATO community. Italy herself has also experienced problems stemming from US export control regulations.

## VII. Some Observations

- Italy's strategy is one of procuring defense systems for its armed forces largely from indigenous manufacturers or from those foreign firms with which Italian industry has cooperative development and production arrangements. Nevertheless, Italy also has recently turned to imports to support a newly-reorganized Armed Forces designed to cut manpower by 25 percent and simplify the command structure in order to create a lower-cost more mobile force.
- One of Italy's challenges is to create an industrial strategy that will maintain key Italian defense capabilities. This implies that the Italian defense industrial base must have the resources and freedom to be effective in competitive global markets. In turn, the defense industries must be structured efficiently, be flexible in their ability to meet market demand, have an efficient commercial support network, and be involved in several well-conceived alliances with leading foreign industries.
- Italian industry believes that it can offer solid technical expertise, modern and in some cases advanced production facilities, developed infrastructures, and relatively low labor costs. Italy's model should be that of a niche player not unlike that of Singapore or South Korea. Broad areas of Italian strategic competency include helicopters, defense electronics, space, and aeronautics.
- One of the major factors motivating these needs is the consolidation that has already occurred in the United States, creating the large defense giants Lockheed-Martin, Boeing, and Raytheon.

---

### ENDNOTES

<sup>1</sup> Italian Prime Minister Prodi in Silvestri, "Italy's Drive Threatened by a Split Majority; Need for a Stronger Foreign Policy," *Milan Sole-24 Ore* (Internet Version, August 1, 1998).

<sup>2</sup> The issues and Italy's programs addressing them were presented by Lamberto Dini, Minister of Foreign Affairs to Italy's Chamber of Deputies, March 17, 1998.

<sup>3</sup> Gen. Alberto Zignani, Italian General Defence Secretary and National Armament Director, interview in "New Horizons For Italian Defence Procurement," *Military Technology-MILTECH*, March 1997, pp. 97-98.

<sup>4</sup> Paolo Valpolini, "Italy Seeks More Sustainability," *Jane's Defence Weekly*, June 14, 2000, p. 70.

<sup>5</sup> Alesandro Politi, "Italian Navy Leaders Plead for Decisions on Security Issues," *Defense News*, February 14, 1994.

<sup>6</sup> Gen. Alberto Zignani, Italian National Armament Director, Interview, *Jane's Defence Weekly*, June 14, 2000, p. 96.

- 
- <sup>7</sup> *Worldwide Military Expenditures and Arms Transfers, 1998*, Department of State, Bureau of Arms Control, Washington, DC, January 2000.
- <sup>8</sup> Zignani, March 1997, op. cit., p. 94.
- <sup>9</sup> Andrea Nativi, "The New Face of the Italian Defense and Aerospace Industry", *Military Technology-MILTECH*, June 1997, p. 41.
- <sup>10</sup> Unless indicated otherwise, sales figures for Finmeccanica's subsidiaries are taken from a report prepared by Finmeccanica's Managing Director, for the Italian Senate as reported by Rome Air Press, March 2, 1999, p. 359-360.
- <sup>11</sup> Nativi, op. cit., p. 44.
- <sup>12</sup> Ibid., pp. 44-46.
- <sup>13</sup> Ibid., p. 46.
- <sup>14</sup> Unattributed, "Worldwide Defense Companies Ranked by Estimated Defense Sales for 1991," *International Defense Review*, Defense '93, pp. 33-55.
- <sup>15</sup> Unattributed, "Defense News Top 100," *Defense News*, August 7, 2000, p. 14.
- <sup>16</sup> Zignani, March 1997, op. cit., p. 97.
- <sup>17</sup> General Alberto Zignani, National Armament Director, Italian Ministry of Defense, interview in *Defense News*, March 30, 1998, p. 62.
- <sup>18</sup> Giovanni de Briganti, "Financial Free Fall Cripples Italian Defense," *Defense News*, May 15, 1995, p. 4.
- <sup>19</sup> Theresa Hitchens, "Italy's Air Force Considers E-2C Buy For Early Warning," *Defense News*, November 13, 1995, p. 8.
- <sup>20</sup> Zignani, June 14, 2000, op. cit.
- <sup>21</sup> Zignani, March 1998, op. cit.
- <sup>22</sup> Zignani, March 1997, op. cit., p. 97.
- <sup>23</sup> Nativi, op. cit., p. 41.
- <sup>24</sup> Stefano Silvestri, "Military and Aerospace Technologies Key to Finmeccanica's Development Within Framework of European Defense Industry," *Milan Il Sole-24 Ore*, February 9, 1999.
- <sup>25</sup> Alberto Lina, Managing Director, Finmeccanica, in Unattributed, "Without Government Consensus, European Integration Will Falter," *Rome Air Press*, March 2, 1998, pp. 359-60.
- <sup>26</sup> *Worldwide Military Expenditures and Arms Transfers, 1998*, op. cit.
- <sup>27</sup> Michel Nones, "Italian Defense Exports: Realities and Prospects", *Military Technology-(MILTECH)*, November 1998, p.63.
- <sup>28</sup> Nones, November 1998, op. cit, pp. 60-61.
- <sup>29</sup> Briganti, May 12, 1997, op. cit.
- <sup>30</sup> Zignani, May 1998, op. cit.
- <sup>31</sup> Simon Saradzhyan, "Italy, Russia Untangle Restrictions on Trainer Development," *Defense News*, June 14, 1999.
- <sup>32</sup> Unattributed, "Italian Air Force to Buy 12 C-27J's," *Defence Systems Daily*, November 12, 1999.
- <sup>33</sup> Zignani, June 14, 2000, op. cit.
- <sup>34</sup> Gen. Alberto Zignani, in Isaak Zulkarnen, "Italian Defence Industry Shapes Up to Overcome Crisis Years," *Asian Defence Journal*, August 1999, p. 24.
- <sup>35</sup> Giuseppe Viriglio, CEO, Alenia Space Division, in Peter B. de Selding, "U.S. Export Rules May Drive Away Italian Aerospace Firms," *Defense News*, June 26, 2000, p. 70.
- <sup>36</sup> Nones, November 1998, op. cit., pp. 62-64.
- <sup>37</sup> *Worldwide Military Expenditures and Arms Transfers 1998*, op. cit.
- <sup>38</sup> Zignani, March 1997, op. cit., p. 97.
- <sup>39</sup> Alessandro Politi, "Finmeccanica Melds Efim's Companies," *Defense News*, February 21, 1994.
- <sup>40</sup> Giovanni de Briganti, "Italian Group Reorganizes After Purchases/Finmeccanica Completes Acquisition of Seven Defense Firms From EFIM," *Defense News*, January 16, 1995, p. 25.
- <sup>41</sup> Giovanni de Briganti, "Italian Industry Renaissance/Sales Rise for Rome's Finmeccanica After Restructuring," *Defense News*, May 15, 1995, p. 4.
- <sup>42</sup> Giovanni de Briganti, "Securities Watch/Fate of Italy's Finmeccanica Hinges on IRI Rescue Plan," *Defense News*, November 20, 1995, p. 28.
- <sup>43</sup> Fabiano Fabiano, CEO, Finmeccanica, in Giovanni de Briganti, "Finmeccanica Move Rocks Italian Industry/CEO Quits, Blasts Decision to Split, Privatize Defense Firm," *Defense News*, May 12, 1997, p. 12.
- <sup>44</sup> Nativi, op. cit., p. 42.

---

<sup>45</sup> Lina, op. cit.

<sup>46</sup> Nativi, op. cit., p. 42.

<sup>47</sup> Michael J. Witt, "Italy Joins Consolidation Club with Gec Venture," *Defense News*, April 6, 1998, p.1.

<sup>48</sup> Christopher Endean, "AMS Key to Italy's Role in European Defense Industry," *Defense News*, July 5, 1999.

<sup>49</sup> David Saw, "Building a Transnational Company: Alenia Marconi Systems," *Asian Military Review*, May/June 2000, pp. 28-29.

<sup>50</sup> John D. Morrocco, Pierre Sparaco, and Michael A. Taverna, "Decision Imminent on Alenia's Future," *Aviation Week and Space Technology*, March 27, 2000, pp. 24-26.

<sup>51</sup> Douglas Barrie and Theresa Hitchens, "Suitors for Finmeccanica Await Merger Decision," *Defense News*, March 20, 2000, p. 6.

<sup>52</sup> Pierre Sparaco, "Streamlining Lends Credence to Finmeccanica/EADS Link," *Aviation Week and Space Technology*, April 24, 2000, pp. 57-58.

<sup>53</sup> Michael A. Taverna, "EADS, Finmeccanica Set Stage for Aeronautics Joint Venture," *Aviation Week and Space Technology*, July 24, 2000, pp. 137-138.

<sup>54</sup> Zignani, March 1998, op. cit.

<sup>55</sup> Enrico Gimelli, Senior Corporate Vice President for Defense Affairs, Finmeccanica, in Giovanni de Briganti, "Italians Seek Higher Profile in Merger Market," *Defense News*, May 29, 1995, p.12.

<sup>56</sup> Benjamin Andreatta, Italian Minister of Defense, interview, "Andreatta on EU Defense Industry, Blair's Stance," *Milan Il Sole*, October 3, 1998, p. 14.

<sup>57</sup> Michele Nones, "Defense Sector Seen as Entering Internationalization Phase," *Milan Il Sole 24-Ore*, March 6, 1997, p. 15.