

Clustering

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Clustering is the phenomenon whereby firms from the same industry gather together in close proximity. It is particularly evident in industries like banking. Banking centres in cities such as London and New York have thrived for centuries. Hundreds of banks cluster there, close together and within easy walking distance of each other. This makes it easier for customers to choose between them, and might be thought to act against each individual bank's best interests.

Economists explain clustering as a means for small companies to enjoy some of the economies of scale (see article) usually reserved for large ones. An isolated greenfield site in a depressed region where government grants are plentiful may bring a young company immediate benefits. But in the longer term the young company may be better off squeezing itself onto an expensive piece of urban real estate in close proximity to a significant number of its competitors.

By sticking together, firms are able to benefit from such things as the neighbourhood's pool of expertise and skilled workers; its easy access to component suppliers (Toyota's suppliers generally cluster round the mother company's factories, wherever they may be); and its information channels (both formal ones like trade magazines and informal ones like everyday gossip in neighbourhood bars). In early industrialised England clusters were common. Staffordshire was the home of many potteries—so many that the region is still known today as "the Potteries". The town of Nottingham was home to many lace-makers, Luton to hatters, and so on.

Modern high-tech clusters often gather round prestigious universities on whose research they can piggyback. Silicon Valley is near Stanford University, for example, and similar high-tech clusters are gathered around MIT near Boston in the United States and around Cambridge University in Britain.

One of the most famous clusters is that of the Hollywood film industry. When the big movie studio system broke up in the 1930s it fractured into a large number of what were essentially small specialist firms and freelancers. Clustering around Hollywood allows each of these small units to benefit as if it had the scale of an old movie studio, but without the rigidities of the studios' wage hierarchy and unionised labour.

In some cases, the ancillary services that grew up to service industrial clusters have remained in position and developed into vibrant new industries long after their original client industry has faded. Near Birmingham in Britain, for instance, the cluster of car-industry service firms that grew up when that city was a force in the industry has become an important element in the development of Formula One and other specialist vehicle businesses.

That clustering is not a phenomenon whose time has passed is demonstrated by California's Silicon Valley. New IT and internet firms continue to gather there in spite of the high prices of local property and the danger of earthquakes. Ironically, they find that much of the most valuable information that they obtain comes not electronically but from face-to-face meetings.

Michael Porter (see article), a professor at Harvard Business School, has looked recently at this seemingly paradoxical revival of industrial clusters. In theory, he says, location should no longer be a source of competitive advantage in an era of global competition, rapid transport and high-speed telecommunications. The world's increasingly global businesses should by now be above and beyond geography. Yet clearly they are not.

Porter gives several (non-silicon) examples, including the wine-growing industry in northern California and the flower-growing business in the Netherlands. The Netherlands would not be the natural first choice for anyone starting a flower-growing business today were it not for the fact that the business is already there. This is a huge competitive advantage for a new entrant, who can benefit from such things as the sophisticated Dutch flower auctions, the flower-growers' associations and the country's advanced research centres.

CLUSTERING. **The Economist**, New York, Aug. 24th 2009. Disponível em: <www.economist.com>. Acesso em: 26 ago. 2009.

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