LOCAL ECONOMIES AND GLOBALISATION

This document was prepared by Mr. Andrew Davies, Consultant to the OECD, from written and oral contributions to the conference on “Local Development and Structural Change: A New Perspective on Adjustment and Reform”, held in Paris on 3 and 4 May 1993.

The views expressed are those of the authors, and do not necessarily reflect the opinions of the OECD. This Notebook is made available to the public on the responsibility of the Secretary-General of the OECD.

Copyright OECD 1995
Applications for permission to reproduce or to translate all or part of this material should be made to:
Head of Publications Service, OECD, 2 rue André-Pascal, 75775 Paris, Cedex 16, France
# TABLE OF CONTENTS

INTRODUCTION .................................................................................................................................... 4  

CHAPTER 1. THE INFLUENCE OF STRUCTURAL ADJUSTMENT ON LOCAL ECONOMIES AND LOCAL LABOUR MARKETS .............................................................. 7  
  Structural adjustment and the distribution of economic activity ...................................................... 7  
  Globalisation and the local economy ............................................................................................... 8  
  Globalisation and the local labour market ...................................................................................... 9  
  The significance of location .......................................................................................................... 10  
  Roads to competitiveness ............................................................................................................. 11  
  The choice of the “High Road” .................................................................................................... 12  
  Advantages of local economies .................................................................................................. 14  
  The situation in Eastern Europe ................................................................................................... 17  

CHAPTER 2. THE CONTRIBUTION OF LOCAL APPROACHES TO BUSINESS, EMPLOYMENT AND ECONOMIC DEVELOPMENT .................................................. 19  
  From local initiatives to tentative regional strategies .................................................................. 19  
  The assessment of process versus measurable outcomes ............................................................ 23  

CHAPTER 3. BUILDING LOCAL CAPACITIES ........................................................................ 25  
  The role of local capacity-building ............................................................................................ 26  
  The community in the new local development process .............................................................. 26  
  The role of business ................................................................................................................... 27  
  The role of finance ...................................................................................................................... 29  
  The role of education and training .............................................................................................. 30  
  The importance of networking ................................................................................................... 32  

CHAPTER 4. A NEW ROLE FOR GOVERNMENT? ................................................................. 34  

CHAPTER 5. CONCLUSION ....................................................................................................... 38  

BIBLIOGRAPHY .......................................................................................................................... 40  

ANNEX ........................................................................................................................................ 41
INTRODUCTION

Never before has the complexity and interwovenness of OECD economies been so evident. The three central themes of this report -- structural adjustment, territorial development and employment creation -- are intimately connected and it seems that sustainable progress in any one of these areas requires progress in all three. The current policy paradigm means that there is no easy trade-off between, for example, the speed of structural adjustment and employment creation that would allow us to make major progress on one of these objectives while ignoring the others.

The OECD has long been concerned with the question of structural adjustment -- some 15 years ago the OECD started its work on what was then called *Positive Adjustment*. Who would have thought in the early 1980s, while in the midst of adjustment problems in the steel, coal and shipbuilding industries, that we would today be addressing adjustment problems in the computer and micro-electronics industries, and the financial sector, which were then assumed to be paths for future prosperity? The reality is that adjustment is stimulated by international exchange and foreign investment; the development of these two phenomena makes this possible but also makes it continuous.

Economic change and adjustment are essential to the continuing prosperity of OECD economies. The two key forces driving this process are technology, which makes change possible and competition, which ensures that the change is implemented. Together these forces help to determine the kinds of goods and services that are produced, the prices at which they are sold, and which type of employment is generated.

In the recent past, technological change has both accelerated and become more radical. Even in the most flexible of economies, it is difficult to absorb these changes quickly enough, because often neither the skills, the organisational forms, nor the management strategies are yet appropriately adapted.

The second driving force is more and more intense competition. Changes in competitive forces have important consequences, such as changing locations of production, promoting flexibility in the production process; rewarding physical proximity between firms, their suppliers and their customers. Under this so-called post-Fordist system of production, the countries and regions most likely to flourish would be those with relatively dense, knowledge-intensive networks of private firms and public institutions, with the capacity to generate new small- and medium-sized enterprises and foster a culture of entrepreneurship.

Structural changes have thus strongly influenced the geographical distribution and physical form of economic activities and in turn they influence the growth paths of regional and local economies. With the globalisation of the economy some local areas have become centres of innovation and have internationalised their activities; others, however, have been left behind.

Over the past decade or more, Member countries have engaged in wide-ranging programmes of structural reform for the purpose of making national economies more responsive to market forces. All OECD countries have been involved in this process, though there were considerable differences between
them in the content, timing and extent of reforms. Numerous studies conducted in the OECD attest to the success of these reform measures. As wasteful protectionist policies that impeded development are dismantled, rising incomes expand the markets available to all -- providing gains through greater product variety and fuller realisation of economies of scale. Thus, although the agenda for structural reform is far from complete, reforms undertaken to date have benefited both the countries initiating the changes and the broader international economy.

Yet adjustment involves costs for society that are not always equally shared. Inevitably, these costs give rise to concerns -- concerns which have become acute in a context of slow growth and high and prolonged unemployment. The recent interest in "globalisation" and its impact on employment is but one example. Here, the temptation in recent years has been to revert to protectionist policies in all their myriad forms -- policies that had seemed thoroughly discredited by post-war experiences.

As stated in the OECD Jobs Study, stimulating job creation mechanisms and dealing with the unemployment problem require simultaneous action in different policy areas, ranging from macro-economic policy to social, labour market and territorial development policies. The urgency of this task is underlined by the massive unemployment now directly affecting 35 million people, and indirectly affecting many more, in the OECD area.

There are at least two major additional reasons for the growing concern with poor employment performance. Firstly, the costs involved go beyond losses in output, affecting the skills, motivation and the future prospects of the unemployed themselves. Secondly, the problem risks provoking precipitate and counter-productive policy actions, undercutting the foundation upon which post-war economic prosperity has been based.

The requirement for more dynamic and responsive economic development efforts needs to be addressed by policymakers. Policies will need to reinforce market mechanisms while simultaneously modernising institutions and increasing their capacity to contribute to sustained improvement in the welfare of citizens.

In this context a contribution is required to ensure that the local and regional dimension of structural and employment policies is better appreciated.

In spite of the fact that the OECD is above all known as a centre of analysis of macro-economic issues, it has taken an increasing interest in this spatial dimension of economic problems. To this end, Territorial Development Service was created in 1994 bringing together units dealing with regional, local, urban and rural issues.

Within this Service, the LEED Programme has focused on the relationship between the process of job creation, entrepreneurship, new business creation and business expansion. In ensuring effective policies to help localities and regions manage the process of adjustment, create new employment and provide the conditions for sustainable development and modernisation, the work of this Programme has emphasised the following key findings:

- **A climate favourable to enterprise must be created:** The basic prerequisite for the process of new job creation and economic renewal (new firms, new products) is a sufficient supply of entrepreneurs and a long-term climate conducive to entrepreneurship and enterprise at the local level.
- **Home-grown enterprise is a key to lasting success:** Few businesses make major locational changes; the expansion of new and small businesses is therefore crucial to long-term development.

- **Corporate networking and the interaction between large and small firms help success:** The interaction between a business and its market -- often world-wide -- is well understood. Of equal importance is the interaction between the business and the locality where it creates and produces; this interaction is not nearly as well understood.

- **Economic growth and greater equity reinforce each other:** In a knowledge-based economy, there is no inevitable conflict between growth and equity.

- **Public policy must adapt to respond to the diverse geographical impacts of economic change:** The employment and unemployment consequences of economic restructuring are most acutely felt at the local level: Centrally-designed public programmes rarely take into account geographic diversity and therefore fail to effectively reach their targets. While national economies are often adversely affected by the restructuring of single industries or groups of industries, individual regions or towns can be devastated by such changes. Governments should take into account the local and regional impacts of these problems in designing policy.

- **Decentralisation helps:** In the course of the 1980s, decentralisation policies have been adopted that seek to attribute new responsibilities to the local and regional authorities and to representatives of the private and the associative sectors. Now is the appropriate time to start assessing the consequences of decentralisation.

This report starts by examining how structural adjustment has affected the performance of local economies and how they have responded to these threats and opportunities. Regions and localities are influenced by structural change through plant closures, reorganisation and restructuring of firms, but also by growth and expansion of new activities (Chapter 1). On the basis of the experience of the 1980s, the report then tries to reveal some of the keys to successful local and regional development in an increasingly competitive environment (Chapter 2). Chapter 3 reviews some of the capacities required to design the framework for a new development policy for the 1990s, and Chapter 4 identifies the new roles and responsibilities for governments in this new policy environment. Finally, in its conclusions the report discusses some of the implications of structural adjustment for employment policies.
CHAPTER 1. THE INFLUENCE OF STRUCTURAL ADJUSTMENT ON LOCAL ECONOMIES AND LOCAL LABOUR MARKETS

Structural adjustment and the distribution of economic activity

Two decades ago, the spatial distribution of industrial activity appeared stable and self-sustaining. The assumption that economic growth and employment were guaranteed by a process of continuous refinement of Fordist mass-production processes seemed a safe one to make. Today, concurrent processes of globalisation and structural change are affecting OECD member countries so profoundly that, increasingly, policy-makers are looking away from geographically insensitive economies of scale and toward more sustainable economic development through economies of variety and external economies generated at the local level using local resources.

The traditional distribution of national economic activity followed a core-periphery pattern with densely populated industrial areas contrasting starkly with economically backward and sparsely populated rural areas. It was a globalised economy in the sense that these large conurbations competed with one another and had intercontinental commercial relations among themselves. The economies of agglomeration, infrastructural advantages and political influence enjoyed by advanced regions seemed to ensure that this pattern would continue to dominate industrial location indefinitely. However, changing modes of production and the so-called "information revolution" have meant that new areas are becoming centres for high-growth industries. This equalisation of economic activity has been accelerated by the lingering economic recession and subsequent process of restructuring being undergone by once-prosperous heavy industrial areas. Thus we are seeing a truer globalisation process with many more regions in more countries entering the marketplace, especially in Asia, and the social base of participants widening, as small enterprises increase in number and importance. The new geographic arrangement of economic power resembles a mosaic structure with no obvious centre and, at least in theory, smaller disparities between different regions.

The world is passing, however, through a transitional phase. The core-periphery dichotomy, although in decline, still persists in many areas and exists in parallel with the post-Fordist mosaic of newly industrial regions. For example, the world economy continues to be directed from the great metropolitan centres like London, New York, Paris and Tokyo. In fact, these major cities seem to be reinforcing their dominant position in the world economy, demonstrating the valuable economies businesses derive from locating close to the locus of political, financial and cultural life. And in every country there are regions that appear peripheral and seem unlikely ever to develop into a "tile" of the "mosaic".

Four broad categories of region can be distinguished within the evolving economic system: urban centres with a "metropolitan dynamic", new industrial districts, declining heavy industrial regions, and economically lagging rural areas. The first two are active constituents of the developing "mosaic" structure, while the latter two are remnants of the decaying core-periphery model.

To further complicate the situation, the mosaic as it exists constantly changes shape and composition according to the issue involved: i.e., on certain issues there is national consensus; on others, consensus is found among newly industrial districts; on others it is purely a geographical matter on which
diverse but adjacent regions act in unison. Thus, we are far from seeing an orderly mosaic of interlocking but discrete regions looking inward for external competitive strength. The reality is both more jumbled and more puzzling.

**Globalisation and the local economy**

At the same time, the process of globalisation is transforming the way businesses interact with one another and helping to define a new global economic order.

A globalised economy is characterised by a world-wide network of large enterprises sharing certain common features. These features include large-scale direct foreign investment, either overseas production plants, joint venture contracts, or holdings in component companies; significant world-wide transactions making reference to common standards and production practices; and an increasing willingness to co-operate in areas such as Research and Development, production and distribution. The emerging global network promises to produce a new industrial structure that is not directly grounded on access to the domestic market. This new global arrangement is increasingly affecting small and medium-sized enterprises and is compelling them to react to the threats and opportunities it brings. Similarly, it promises, simultaneously, to offer new opportunities to some local economies and local development approaches and severe threats to others (Porter, Kiyonari). (Please note, the names quoted are those of the participants at this conference. A complete list of participants can be found in Annexe 1.)

The links between globalisation and the local economy can be illustrated with reference to the situation in Japan. During the 1980s, the growth of direct investment in Asian countries by Japanese corporations, inspired by the effect of the strengthening Yen on export competitiveness, drastically affected the place of Japanese local economies in the production process. In particular, this was caused by the formation of a triangular trading zone encompassing the Asian NIEs, Japan and the United States. In order to compete strongly in this trading arrangement, Japan has had to accept that its role is no longer that of universal manufacturer and supplier. According to Tadao Kiyonari it now must "enter into relationships of … product item differentiation with the United States and the EC; of product grade (quality) differentiation with NIEs; and of product item differentiation and production stage differentiation with ASEAN countries and China." The challenge for local economies is to adapt to fit into this new structure.

There are two principal methods of adaptation: direct investment abroad using a "develop and import strategy", and exploiting local resources. In both cases, territory plays the determining role. If competition from lower production cost areas is irresistible and if the region is well placed, then a develop and import strategy can allow the region to enter a new niche in the production process, using its location to exploit a geographically sensitive economic trading area. In Japan, this is particularly true of coastal areas which use their location to act as entrepots for NIE and American goods entering the Japanese market. On the other hand, if significant R&D facilities or a highly-skilled labour force are already in place, then the option of building on local skills to produce high value added goods appears the most suitable. The local economy must then respond to the challenge of identifying local strengths and planning their augmentation (Kiyonari).

In both cases, the concepts of place and local organisation are centrally important, and globalisation, although it caused the initial upheaval, in the long term brings more opportunities than threats.

Despite the continuing detachment of most multinational corporations from geographical ties, the trend is unmistakably toward this type of area-based, local-level economic organisation. In the emerging
mosaic distribution, each "piece" is characterised by a strong internal production network, grounded upon exploitation of local capacities and linked vertically to national and international organisations, of which central government is but one. In this sense, it is not so much a national mosaic as a global one. Moreover, given the relative ease of transportation and communication, each individual region is competing against every other in terms of cost, product range and quality. Globalisation has thus exacerbated inter-firm and inter-region competition, putting innovation and quality at a premium. Raw materials are less and less important in the production process and intangible elements such as creativity, talent, ambition, organisational efficiency and control of information are the marginal advantages. Multinational corporations are also increasingly aware that they too can profit from exploiting these comparative advantages, and this is slowly redefining their relationship with the local economic area.

Globalisation and the local labour market

The replacement of the Fordist production system by a more flexible approach has had important implications for the geography of the labour market. The incorporation of automated production processes, the growth of sub-contracting and changes in business and working practices has promoted the growth of a more adaptable labour market in which these continuous changes can be met effectively.

With regard to the four regional types that have been identified in the new economic-activity structure, a parallel geography of labour markets can also be identified.

In urban, metropolitan areas, the labour market is extremely fluid: labour turnover is rapid, laid-off workers generally find alternative employment quickly, and quit rates are high. The labour force is well-informed and mobile from firm to firm. Balanced against this, employers have less trouble finding new employees because the labour market is large, well-educated and there are strong job-matching structures.

The new generation of post-Fordist industrial regions tend not to have this kind of traditional social and labour organisation. Its labour market is characterised by combinations of skilled employees, who are highly mobile and participate in national and even international labour markets, and unskilled workers who are flexible in the sense that they are often temporary or part-time employees but develop firm-specific skills.

In rural areas and industrial areas adversely affected by structural adjustment, the work force is "captive" and when laid-off will probably be available for rehire as necessary. This is particularly true in areas where the labour force is traditionally integrated and there are strong social barriers to mobility and flexibility.

The existing condition of the labour force and its ability to adapt concurrently with changes in the regional economy will be an important factor in determining the ultimate success of local development strategies.

The key to economic development is, therefore, improving the efficiency of the local production system, of which the labour force is an important component. The other major determinant of system efficiency is transaction costs, and here again local capacities can bring large comparative advantages.
The significance of location

The relocation and refashioning of economic activity is limited by the geographical sensitivity of commercial transactions and, more importantly, transaction costs. According to the frequency, complexity and codifiability of transactions, i.e., commercial relations, they all have an optimum space, be it local, regional, national or international (Scott). The classification of activities within spatial groups will, of course, change with technological advances and so on. And this will, in turn, reshape the optimum distribution pattern for business activities. Obviously, the growth of intercontinental information-transfer systems, greater labour mobility and reduction of capital controls means that the optimum space for some transactions is now infinite. Globalisation would seem to suggest a lessening of spatial constraints and a reduction in the importance of this category of geographically-sensitive transactions. In fact, the opposite appears to be true: globalisation has increased the value of non-transferable, geographically particular factors. The importance of the category of business interactions that take place most effectively at the local or regional level has increased dramatically. Benefits of proximity and direct information exchange can apparently outweigh gains from long-distance information-technological innovations (Scott).

A new "techno-industrial" structure is developing where knowledge and skills are the most valuable commodities, and firms are willing to locate where these elements are in abundance. Industrial corporations are streamlining their internal organisational structure but increasing dependence on outside service providers who can manipulate, at relatively low cost, the information technology the companies need. These small specialised component manufacturers and service industries draw their competitiveness not from globalised communications networks but from highly skilled employees, innovative business strategies, and intimate personal links with their customers and other small businesses in the local area. It is now accepted that the most dynamic characteristics of a successful production network stem from comparative advantages specific to that region (Quevit).

In making location choices, multinationals research three main factors: production cost estimates, potential market position advantages, and, to an increasing degree, local support services. For low value added products, production costs are usually the determining factor. In the case of high value added products, however, today's location decision is more complex than ever before, with companies evaluating the educational structure, availability of skilled workers, the concentration of small local component manufacturers, general sub-contractors, service providers and trainers, and a host of other related factors before finally making a choice. The greater the concentration of local support enterprises, the more likely a company will be to invest in the region. Obviously, the cycle is self-propagating, with concentration bringing further concentration, and so on. This suggests that industrial concentration in certain regions will intensify and implies that the disparities between regional economic performance will widen rather than narrow as some regions fail to create the infrastructural critical mass necessary (Quevit).

However, this conclusion rests on fatalistic assumptions that economic processes cannot be influenced and that success for one region inevitably comes at the expense of others. On the contrary, there is strong evidence that economic success is not pre-determined and can be developed and, on a national scale, development is not a zero-sum game. Local capacities in fields such as education and enterprise networking can be created or improved by concerted action, thereby increasing the region's ability to attract outside investment. In addition, the factors that encourage endogenous economic activity can be similarly stimulated. The aim of local development is to foster this process and construct an environment both attractive to investment from outside the region and conducive to economic growth from within. In turn, it is hoped, this will add to the prosperity of the national economy without having a detrimental effect on other regional economies.
Roads to competitiveness

The two core paradigms of development have been, for quite some time, polarised development or the core-periphery model and the diffusion of development from above, that is, centrally planned and implemented, national redistributive "development" programmes. The decline of the first of these and the relative failure of the second to combat regional economic distress, compels a reappraisal of local development policy approaches.

There are two general approaches that a region can take in order to preserve or attain competitiveness: the Low Road approach and the High Road approach (Sengenberger).

The Low Road approach advocates competitiveness through lowering production costs, especially wage rates. The expectation is that low costs will boost profits and enable OECD manufacturers to compete successfully with producers in, for example, Asian NIEs. Obviously, this would adversely affect working conditions and employee rights and come into conflict with social security requirements, safety standards and other regulations that control business practice within the OECD area. The attendant risks of "social dumping" and downward adjustment mitigate strongly against this approach. Furthermore, from a local development standpoint, it is completely anathema. Under this regime, business becomes delocalised and employment destabilised because enterprises are constantly searching for cheaper production alternatives and have no incentive to invest in the local region. There is little doubt, however, that it is a temptingly simple response to increasing competition, in particular in comparison to the complexity of the High Road approach. It is a temptation that many corporations have evidently found difficult to resist — as evidenced by the vast relocation of economic activity, particularly multinational corporations but also service industries to Southeast Asia. With no infrastructural advantages to offer and often remote from major markets, the only variable favouring relocation of these firms is the cost differential. Countries like Mexico and the Asian NIEs offer a supply of unskilled, but rapidly up-skilling, labour without the added expense of social provision, minimum wage requirements and so on — sufficient to offset all other drawbacks of locating in a developing country. Thus, bearing in mind the high-quality infrastructures already in place in OECD countries, if labour costs could be significantly reduced, a large comparative advantage could be created.

The High Road approach stresses the need to make more efficient use of resources and invest in processes, technological innovation and employee upskilling. The High Road approach, in contrast to that of the Low Road, views labour as an important commodity and skill-enhancement as a crucial targeted investment. This approach entails the mobilisation and upgrading of local resources and the exploitation of local strengths and advantages to produce sufficient economies to balance relatively higher wage rates. Concentration on small and medium-sized industries leads to a dynamic labour market with a wide range of skills and rapid job matching processes. In combination with an entrepreneurial culture this produces what can be called a "sticky economy", one where industries tend to locate and invest (Scott). Given the current large-scale industrial relocation, however, it is clear that such sticky economies need to be developed and maintained; OECD regions have obviously lost much of the stickiness they once had. Nevertheless, the High Road approach is the favoured policy instrument from the perspective of OECD countries; indeed, many would say the only option.

The full picture is, of course, more complicated than a choice between these two alternatives. While we may high-mindedly opt for maintenance of social standards and strive to achieve comparative advantage through technical excellence, the temptation to simply reduce wages will be strong. And, with increasing migration into industrial countries from the developing world, there is an increasing pool of labour willing to work for wages and accept conditions that the local population will not. The creation of an internal Low Road approach would inevitably undermine attempts on a regional basis to follow a High
Road policy. The only way to combat this threat is for member governments to commit themselves to monitoring labour standards and adopt appropriate measures to persuade companies to search for a competitive edge by means other than exploiting an immigrant labour force.

Another challenge facing the High Road approach is that competition between regions will lead to attempts to undercut neighbouring regions irresponsibly; i.e., allowing wages to downscale as a matter of competitive regional policy or offering below-cost rents that distort the real estate market. Some observers stress the need for, perhaps voluntary, restrictions on relocations motivated solely by production cost savings. This, it is said, would stimulate companies to explore more progressive methods of reducing production costs, such as production process refinement, systems analysis, and so on. On the other hand, others contend that, at least in terms of competitive relocations in Europe, the conclusion that wage rates are the determining factor is too simplistic. The examples used to illustrate that such relocations do indeed take place between European regions, most notably the Hoover relocation to Scotland from Dijon (France), or that of Timex, Dundee (Scotland) to Besançon (France), demonstrate on closer examination, they argue, that the decision was based on many more factors than simply wage rates and social provision costs. Marginal cost differentials are important but not significant enough in Europe to warrant or explain such drastic production shifts. In addition, large companies sometimes relocate simply to gain market position; locating in certain countries or within a trading area can allow a foreign enterprise to circumvent quota and tariff restrictions. As such, a premature limitation on the ability of companies to move freely would be unjustified and dangerously infringe upon the ideals of free trade and open competition.

At least in theory, the problem of competitive relocation should arise less frequently if the new local approach to development is applied effectively. The new local approach has as one of its main goals the development of local external economies that make wage rates an even less significant factor and also tie the company to its locality. To enact restrictive legislation would be to admit defeat before giving the local approach a chance to succeed.

Attempts to construct a new paradigm of local development following the High Road development path — a territorial and knowledge-based paradigm — will have to overcome many countervailing forces. The most pressing question, therefore, in a situation where both High and Low Road policies exist concurrently, is to discover which policies promote one development route over the other. If economic destiny can be made and shaped, how is this best achieved without wasting time and resources?

The choice of the “High Road”

Broad outline proposals favouring the high road approach over other development strategies include:

As mentioned above, finding a way to ensure that wage rates and working conditions are upheld despite pressures to economise. Firms must be encouraged to try to find comparative advantage without having recourse to regressive wage policies.

Ensuring that local supply is as efficient as possible both within firms and in inter-firm relations. Enterprises should be assisted to incorporate innovative technology in the production process, though this ought to be ensured naturally by market forces. Inter-firm relations, on the other hand, are apparently not encouraged to any great extent by the market. They must therefore be imposed from outside. Executives need to be educated to the beneficial results of trust-based co-ordination, which offers savings on general
overheads, procurement, allows for the exchange of information and technology, and generally cuts the risk of isolation and insularity.

In effect, the efficiency of local supply in the new techno-industrial system depends on the creation of a knowledge-based economy. Suggested ways of promoting this "knowledge and technology paradigm" include:

− deregulation of markets to promote competition;
− building a regionally dispersed knowledge infrastructure with emphasis on education, training, research and business advice;
− programmes for supporting technology diffusion;
− the promotion of networks and new areas of collaboration;
− and fostering of flexibility in the labour market (Arbo and Bjornavold).

Strangely enough, given the role of overdependence in creating today's unemployment problem, the conclusion that region-specific advantages generate growth implies that firms will also benefit from clustering and regions from product specialisation, both of which will tend to reduce transaction costs and improve local networking. Traditional local development policy stressed diversification as the logical way to protect the local economy from external shocks and condemned clustering as a recipe for economic disaster — giving a region many legs to stand on. New local development strategies must react to the realities of the new situation and accept the potential of product specialisation as an effective way of attaining comparative advantage.

Growth opportunities appear markedly better if regions can identify a product range and then depend on external economies created by the closely linked production system — networking, skill-sharing, technology transfer, etc. — to give it a competitive advantage. The ability of many Italian regionally specialised industrial activities to survive recession despite serious crises was due partly to a reorganisation of production processes and technologies, but the foundation for survival was the strong external economies that had developed there over centuries of specialisation: labour skills and experience, specialist financial institutions, strong local networks of production and administrative experience.

The example of Ireland, where the economy is largely based on just five product areas, confirms that self-conscious concentration on a restricted range of industries can bring enormous benefits, both in encouraging the growth of existing enterprises and in attracting new industries from overseas. The specialisations can either be traditional, exploiting accumulated external economies, or new, high value-added industries where a community's educational and infrastructural advantages offer locational advantages. Either way, supply-side competitiveness can be artificially constructed. There is no reason for fatalism (Connellan).

Actively stimulating local demand. A significant proportion of a region's growth can come from within. Investment in social and environmental projects will help to create a vibrant local community and strong cultural life, which in turn boosts local absorption. This kind of policy inevitably raises the issue of large-scale public works programmes, which have been used to stimulate demand in several different OECD countries during periods of economic distress. A method of achieving the same end, without the political overtones or fiscal burden of local demand management/stimulation, is managed deregulation of the public sector. The trend toward privatisation is well underway across Europe and offers an opportunity
for governments to bring denationalised public corporations under local control. An uncoordinated privatisation will result in geographically insensitive private consortia, and the chance to give local regions the economic boost of control over the public sector will be lost.

On a smaller scale, enterprises should be aware that, despite so much discussion of global markets, a significant proportion of their output will be sold within the local area. Local businesses should, as a matter of prime importance, endeavour to exploit as fully as possible the local market and stimulate new demand before looking farther afield.

These points are of particular importance to backward, rural areas where there are few natural advantages and a restricted labour market. Although attempts to build local capacities should be encouraged, the prospects for strong internally generated growth are not promising and public support/demand management in the form of public works or government-supported service provision may always be necessary.

Perhaps most importantly for all regions, assuring the local character of the process, underscoring the region's commitment to its own development and upgrading links between local actors. Although the precise role of government in local development is a controversial subject, it is generally agreed that devolution of power (where appropriate) and increasing the stake of local actors in their own development will produce better results than those achieved through centrally planned policies.

**Advantages of local economies**

We must admit that, while it is true demand management from the centre as practised until the late 1980s often proved to be a failure, there is no certainty that decentralisation will be any more successful at producing durable development. There is, however, cause for optimism. The local economic area has recently acquired certain definable advantages over more dispersed production systems which will assist development efforts:

First, transaction-intensive small and medium-sized enterprises thrive best in a local environment where contacts and exchange can be made quickly and at low cost. Transaction costs rise with distance, even after taking into account the time-saving effects of the information revolution. The smaller the production area, the lower the transaction costs. As long as there is a strong local network of suppliers, sub-contractors, and service providers, the devolution of facets of the productive process to local specialists is the key to achieving transaction cost reductions. In addition, there are what Allen Scott calls "deep social divisions of labour" which provide small and medium-sized enterprises with, *in situ*, a wide range of skills. This heterogeneous local labour market also generates strong economies of scale with respect to reduced search and job-matching costs. It is external economies such as these that provide the glue for "sticky" economies (Scott).

Second, regions have or can create a region-specific culture of entrepreneurship, one of the crucial elements in achieving comparative advantage. Recent local pilot programmes in some OECD countries have succeeded in fostering a spirit of enterprise through incentive schemes. Such schemes on a national basis, aimed usually at enterprise development as a means of job creation, met only qualified success in the past. Locally based programmes, customised to suit the existing specialities and enterprise culture of a region, appear to have been more successful.

Third, technological change does not usually occur through large and costly multinational Research & Development initiatives. On the contrary, most takes place through more modest, incremental
adjustments to processes already well-established and understood. These minor innovations are made in the course of frequent contacts between supplier and customer at the local level. The process of continuous improvement is even more intensive when firms in the same sector are concentrated together. In this situation, technology transfer extremely quick and reduces the likelihood of production bottlenecks.

Fourth, a place-specific economic culture often develops around a local area. That is, social and cultural networks related to work in a particular industry grow up. A sense of local loyalty and pride in work tends to develop. Entrepreneurial activity and innovation in that sector are fostered and there is the incentive to invest time and money in training oneself.

The new local approach can be understood as a self-conscious attempt to develop these geographically sensitive factors. Its special significance is given by its stress on the generation of external economies from within, the importance of the territorial concept and the consistent use of local resources, not out of necessity but as an empirically proven method of improving productivity. The importance of co-operation relative to competition promises to reduce transaction costs and replace rivalry with collaboration as normal business practice. It also promises to achieve broader objectives such as raising local social solidarity by the promotion of local solutions to problems. This promising prognosis does not, however, allow local development agents to be entirely sanguine about the future. At present, local development is a fragile phenomenon, vulnerable to adverse changes in national policy priorities and shocks to the global economy such as currency fluctuations, commodity price changes, and so on. Even for the prosperous new industrial regions, there is an ever-present sensitivity to external factors. Nevertheless it is imperative to refute emphatically the classical economic conventional wisdom that free markets alone determine ultimate economic success or failure. The local approach hopes to prove that success can be made and sustained.

Similarly, it is imperative to limit the role of macroeconomic policy in national economic planning and underline the links between the local economy and government policy. First and most obviously, the aggregate of well-organised regional economies is a healthy national economy. Despite the growth of a borderless global mosaic structure, from a national policy point of view, the sum of well-functioning regions is a prosperous national economy (Scott, Garofoli). This translates into greater tax revenues and also fewer regions needing government support. At present wealthy regions pay to support the development of other regions. Although welfare payments are a very powerful redistributive and, indirectly, developmental tool, they create dependence rather than promoting self-sufficiency. The corollary is, of course, that the further growth of wealthy regions is inhibited by high taxation levels. At a time of sluggish economic growth, the argument for helping regions to help themselves is extremely persuasive.

Local initiatives allow a more sophisticated cross-sectoral approach to economic development, but on a manageable scale. They are also a useful way to offset the social dislocation and potential unrest generated by strong structural adjustment policies. The political fall-out of unpopular national restructuring policies can be reduced if the blow is softened by equalising regional policies. In sum, the benefits of strong local initiatives to both the local economy and in terms of national policy aims are being increasingly recognised.

In order to fully understand how the local economy can be stabilised and made prosperous, it is important to understand why local regions go into decline. The decline of traditional industrial regions which depended to a large extent on such heavy industries as shipbuilding, steelmaking and automobile production is relatively easy to explain. The intensification of global competition and the increasing ability of firms to invest overseas resulted in an almost complete loss of competitive edge in these areas and the wholesale closure of production facilities. But this has not been the case everywhere and where it
has taken place, the rate of economic decline varies greatly. Adjacent regions with similar sectoral profiles, possessing many of the same local advantages and deficiencies differ markedly in terms of economic performance, both over time and with respect to one another. This variation can be attributed to the prevalence of transactional failures in the local economic system: that is, failures to fully capitalise upon the potential benefits of co-operation, collaboration and co-ordination at the local level caused by a lack of trust, misdirected feelings of competition and lack of leadership. Another explanation is that regions have an observable tendency to become locked into often self-defeating development strategies and lose the flexibility of approach that is key to a successful development policy. Such strategic inflexibility is extremely wasteful and can tarnish the reputation of the local development approach as a permanent element of national economic planning (Scott).

Both of these predicaments can be most effectively dealt with by the creation of institutions, which are suited to systems analysis and problem resolution. The broad tasks of such institutions with regard to reducing transactional failures can be summarised as follows:

- **Building trust, confidence and co-operation.** Institutions can offer a forum and framework for co-operative information exchange — not through formal regulation, but by an information flow that enables firms to evaluate one another. “Reputation effects” reduce the temptation to abuse trust relationships for personal gain. The reliability of inter-firm contacts are thus greatly improved. Industry associations can provide some self-regulation and similar arenas for discussion, but bridging institutions can expand the contacts between different but related industries.

- **Creating political coalitions.** Regional economic councils are needed that can publicise specific issues and generate a consensus, funding and impetus from a wide variety of actors. These councils should have a brief to look to long-term development and concentrate on educating and informing members about the reasons for new policies and suggesting ways that aims can be achieved for the benefit of all. One significant absentee from the local actors have been labour unions/trade union whose national administrative structure and occupational rather than geographical loyalty has made effective participation in local projects difficult. It would be useful if local/regional labour organisations could become more involved in the local development process, combining involvement at the local level with traditional national goals.

- **Inter-regional co-operation.** With the success of regional economic growth comes the problem of relations with other regions which are effectively competitors, whether they are compatriots or not. An attitude of region versus region can have destructive effects on national wealth and disastrous effects for both economies.

In addition, to combat strategic inflexibility, a fundamental adjustment must be made in our thinking about the local economy: from seeing it in a finite process of adaptation to seeing it as a dynamic system involved in a process of continual change. The local development strategy must therefore be flexible and suited to constant re-evaluation. Local development planners must set the local economy in its global context and predict where changes in the global economy will take the regional and local economies in the medium and long terms. This is obviously impossible or at least difficult for a small business or entrepreneur which adapts better to short term shifts. The task can, however, be taken on by regional or national organisations, either government itself, research bureaux or enterprise consortia.

In summary, the general aim is to combine the dynamism and ambition of local entrepreneurs with the collective organisational, analytical and financial capabilities of central and local government. There will always be, of course, regions that lag behind, but it should be possible to mitigate the worst effects of structural adjustment and globalisation by appropriate policies to isolate and amplify local
economic advantages. Implicit in this process is an accompanying change in the local labour market, whose flexibility can constitute a region's greatest advantages.

**The situation in Eastern Europe**

The foregoing discussion is based on examinations and analysis of the processes of globalisation and structural adjustment being experienced throughout the OECD area. The prescription that follow will also make certain assumptions about the level of economic development, government philosophy, entrepreneurial experience and so on. It is illustrative at this point to look at the situation in Eastern Europe to see how the severe structural changes taking place there affect the utility of the area-based approach being proposed for the OECD area.

The emerging geography of economic activity in Eastern Europe can be characterised in a similar way to that within the OECD. The four categories are:

1. Dynamic regions centred around metropolitan areas with international ties, increasing numbers of joint ventures, a skilled work force, and so on.

2. Old industrial areas with relatively high unemployment and characterised by over-exploitation of the natural environment. Good infrastructural development, industrial expertise, some foreign capital and R&D facilities mean, nevertheless, that they have strong future growth potential despite current difficulties.

3. Agricultural regions that have never developed any significant industry and are likely to remain backward and unattractive to foreign investment.

4. Smaller industrial areas (the majority of regions, in fact) currently hit by recession and lacking private entrepreneurial drive. They are dependent for growth on external factors — general national economic growth, government support — and are extremely vulnerable to external shocks.

It is clear that areas in category 1 and, to a lesser extent, category 2 will develop without specific development policies — though development can be enhanced by strategic co-ordination. The other regions, however, need significant assistance. There are, however, several obstacles that will hamper efforts to introduce an effective area-based approach in these regions:

First, regional development policies organised by the state necessarily have a strong welfare component. In areas that are not adapting to the harsh realities of the move to a market economy, before attempts to stimulate the local economy are made, the immediate needs of the population must be taken care of. Unemployment rates are very high and ensuring a minimum income level for the unemployed must be a first priority. Unfortunately, this means that further allocations for development projects are not available.

Second, economic rejuvenation will inevitably occur where there are tangible advantages and foreign capital can be attracted. In less fortunate regions, there is little incentive for private investment and money must come from the government. Funds for development purposes are scarce and thus the kind of large-scale stimuli required cannot be provided — at least not in addition to the welfare commitment to these regions. The prognosis is therefore that the disparity between adapting and lagging regions will grow wider. State regional policy therefore “can only ease the course of the process … especially its social consequences” (Sz lacta).
Finally, investment from abroad is concentrated largely around the main conurbations, leaving large parts of the country without direct investment. Of course, it is those regions most in need of foreign capital that are the least attractive investment sites. This is particularly disappointing given the limited ability of the central governments to invest in these regions itself.

The situation in Eastern Europe differs markedly from that in the OECD countries, but this is not to say that regional development approaches have no role to play. On the contrary, they should be even more useful. But it is clear that the enormous wrenching adjustments that these countries are undergoing makes it difficult for central governments to commit resources to local development schemes in preference to nationally oriented programs.
CHAPTER 2. THE CONTRIBUTION OF LOCAL APPROACHES TO BUSINESS, EMPLOYMENT AND ECONOMIC DEVELOPMENT

From local initiatives to tentative regional strategies

Locally based development approaches arose as a reaction to unemployment and economic dislocation caused by industrial decline and relocation. After the relative failure of centrally organised, nationally applied projects, the idea of a local initiative gained momentum. A trend towards broadening the scope of the initiatives grew up quickly as it became obvious that a more radical, integrated approach to the problem was required. But, initially at least, the focus was firmly on job creation through the stimulation of new business.

It is important to realise that the scale of the problem was greater than anything seen before. And it became obvious very quickly that the process could not be easily reversed and that many traditional heavy industries were in the later stages of terminal decline. Thus, the issue was not how to restimulate old industries or how to occupy and support the work force until the business cycle turned upward once more. Rather, the issue was how to consciously reorient the whole economy toward new industries and working practices.

The process had both short- and medium/long-term components. In the short term, the immediate needs of a community facing economic hardship had to be addressed — a relatively well-understood and easily implemented task. More difficult were medium and long-term initiatives to re-educate the labour force to the harsh realities of the new situation and persuade them that a transformation of the local economy was possible and that retraining was worthwhile. In this situation, rapid action was imperative both to arrest the growth of fatalism, demoralisation and passivity and also to generate quick, visible results to lend credibility to the chosen policy approach (Chereque).

As we move into the mid-1990s the next stage of evolution for area-based development policy is becoming clearer. It has two main strands: first, the adoption by regional development policy-makers of the local approach as the central foundation of policy in preference to the attraction of external industries and its incorporation into long-term regional development strategies. And, second, the conviction that the two elements — local initiatives and strategic regional planning — need to be more intimately married.

It is clear that the process of combining the two has already begun in some places. For example, in Austria, where local approaches developed early, local initiatives have made a significant contribution to the shaping of regional development policy. Firstly, negotiations with local actors involved in local projects have sharpened and defined the goals and methodology of regional policy, making it a more coherent vehicle for promoting the goals of regional development and ensuring its compatibility with existing local programmes. In addition, practice with local development programmes has improved the capacity of local actors to carry through regional initiatives. Regional policy-makers find local actors increasingly qualified and experienced partners. They are also practised in the art of working in partnership. Successful local programmes have increased the confidence of government agencies in the ability of local actors to produce the services and meet the targets that have been set in planning sessions. This experience has also led to the creation of high-quality, customer-orientated support, finance and
development services. The cumulative effect of this has been to create more focused regional strategies that value local input.

The new generation of regional policies that are emerging in Austria are informed by these local influences and focus more directly on strategic, long-term concerns, including sustainability, economic renewal and business development. The co-ordination between local actors and regional authorities will obviously continue and should serve to reinforce the gains made by more disaggregated, ad hoc policy approaches of the previous decades (Hummelbrunner).

After evaluating initial development efforts, the need for broadening scope, achieving scale and co-ordinating the approach also became apparent to development actors in the Netherlands. At the outset, partly because of a lack of resources and partly as a response to a perceived crisis, Dutch municipalities devoted much of their local development work on solving the unemployment problem, generally considered the most pressing and most political damaging problem. The approach had two themes: retraining the unemployed and promoting individual entrepreneurship. Of these two, enterprise development was the most popular. Despite some success in generating new firms, the impact of this growth on unemployment was small. In the Dutch case, "these first initiatives can be characterised as only partial solutions to the unemployment problem" (Wever). However, the process had not been a waste — the cost of the projects had been relatively small, often self-financed, and represented a useful learning experience for the participants. They also resulted in the growth of venture capital companies tailored to the needs of small business start ups. It was obvious, however, that these projects like those in the United States were not designed to cope with the problem as it existed. A new tactic was necessary that matched more closely the scale of the problem.

The focus of development shifted from simple job creation schemes to more ambitious regional visions. However, the local element was not eliminated. Rather, as had happened in Austria, its influence helped to mould and give relevance to the new regional policy.

General regional policy in the Netherlands has been undergoing a process of decentralisation for some time, with regions becoming more and more involved in attracting new industrial activity to the area and retraining the labour force to complement new industries. It was also becoming more active in lobbying national agencies for more budgetary and disbursement flexibility — in order to utilise available funds more comprehensively to suit the particular needs of the region, as distinct from those of other regions. Because differences between investing in one region as compared to another are small, that is, production cost and investment cost differentials are negligible, local initiatives can make the crucial difference in location choices. The centrality of a region's local development policy is an indication of its commitment to growth and is viewed as a positive locational feature. Every region or municipality that develops a local development strategy must create an explicit development plan, and in so doing articulate a specific vision for the future of the region. In turn, this attracts attention to, and hopefully support for the plan from the community at large and generates a cohesiveness in approach that other regions lack. Against a background of community-wide co-operation and commitment, government agents are more likely to commit funds or time to assist in implementing the plan. Furthermore, local businesses are likely to co-operate with one another more readily to solve "bottle-neck" problems, thus facilitating the smooth running of the economy.

This process of developing local initiatives to create comparative advantage on what is, at least in national terms, a level economic playing field, i.e., with harmonised taxation policies, social provisions and production costs, implies fierce competition between municipalities within regions. This certainly occurred, but a realisation that co-operation can also bring positive results has been developing. And this collaboration has opened and sharpened discussion of how local and regional authorities should be
organised. Above all, as happened in Austria, the initial projects merely highlighted the need for a broader vision and more strategic approach (Wever).

A similar process has taken place in Spain, where local policy was similarly centred on the effort to cut unemployment by encouraging SME start ups. As with other OECD countries the results of these Spanish local programs are not easily quantified. It can be assumed, however, that the net effect on the national economy has been small and expectations at the outset were over-optimistic. On the other hand, at the local level, indications from individual projects in Spain have been sufficiently encouraging to boost calls for a more organised "next stage" with closer co-ordination of local initiatives into a general regional policy. (Regional government has become involved and, in some ways, is using local development co-ordination as a way to reimpose itself as an actor in the process.) This derives from a realisation that sustainable local initiatives cannot simply be imposed and create immediate employment, they depend on incremental upgrading of local capacities to respond to challenges, both individually and collectively.

This progression from haphazard to co-ordinated development is illustrated by such policies as the foundation of a network of development centres by a group of young graduates, the establishment of university courses in local development for directors of Écoles-Ateliers, and the creation of a central government Development and Employment Agency to lend local actors political and financial support (Baillo Ruiz).

The message seems to be that local initiatives cannot guarantee sustained growth without some form of organisation at a regional level. This is particularly true of the problem of creating viable new businesses.

In past development programmes, most entrepreneurial firms adopted a niche strategy; that is, they identified a gap in the market and introduced an innovative product to meet this perceived need. Although this technique offers extremely high initial growth potential, the growth curve is inevitably downward as rival products enter the market with new, more refined or cheaper products. Furthermore, many entrepreneurial businesses enter the market with just one product, and neglect to diversify until it is too late. The focus of development strategy was formerly to help entrepreneurs find a way into the niche. Now, it is to help them either stay in the niche or branch into other product lines.

The Training and Enterprise Councils in the United Kingdom offer a good example of how a well-directed policy can create an environment conducive to sustainable enterprise development along these lines and benefit both its target group (in this case the unemployed) and also the participants/providers (local business, educational institutions, and training providers). The principal aim of the TEC scheme was to find a way of involving the private sector in training and retraining of the labour force. It was hoped that this would make programmes more relevant and focused, and also pass some of the financial burden which up to this point had been carried by the government, to the private sector. The most striking feature of the scheme is its strong territorial emphasis — capitalising on the territory as "a strategic factor in development" (Garofoli). For example, the TEC regions are of widely different sizes in order to preserve established geographical units and foster a sense of popular identification with the TEC as a local institution. The size of each TEC was not standardised, nor was growth potential harmonised as this would inevitably have confused territorial integrity.

Stressing its co-ordinating role, the TECs attempt to devolve as much executive control as possible to the local level, creating partnerships involving the business community with many other local actors. The TECs are not concerned with direct delivery of services. They are strategic planning bodies, they offer funds and monitor and evaluate results. The TECs, in other words, act as facilitators or brokers. The contribution of the TEC derives from its power to advise, influence, create and lead partnerships,
bestow credibility and so on. Most importantly, the TECs make sure all partners are aware of the scheme's radical nature; i.e., actors should not be constrained by normal development practice. On the contrary, they should have "a broad charter and vision that extends beyond training and enterprise to influence education, employment and development" (Stratton).

The experience of these development schemes has illuminated several issues that will undoubtedly be encountered elsewhere when similar umbrella organisations are established.

First, the capacity of the smallest regions (single county or small urban centre) to achieve the same objectives as the larger ones has been questioned. Although they do valuable work, the mission of new area-based programmes is to create a new vision of the local community, rather than simply doing good works at the margins. However, these smaller territorial entities are often the ones with the strongest sense of identity and the greatest resistance to merger. It is important to keep in mind the critical mass of resources required to allow a regional body to achieve its broad aims. At the same time, the crucial sense of community spirit can be lost if the territory chosen is not historically or geographically unitary.

Second, one size does not necessarily fit all. For example, employment projects have been found to be effective even at the neighbourhood level, whereas education and training programs are best organised from a regional level. Inward investment and economic development strategy, on the other hand, must be made in the context of the region as a whole. In all cases, the same considerations as in the preceding point remain valid.

Third, the experience of the TECs raises the question of whether performance tables and goal-setting are adequate replacements for rigorous free-market competition in ensuring efficiency and preventing abuses. Particularly when the majority of funding comes from government finances, there is always the possibility of a relaxation of the standards that would be demanded in the private sector. This problem may be solved, however, by the inevitable existence of inter-regional competition. In the Netherlands, for example, where the marginal cost of investment in geographical terms is almost nil and production costs from one location to another will be almost identical, there is competition between regions to attract new industry and ensure the competitiveness of existing local firms. Given that municipalities have only limited financial resources, there is an imperative need to make the best possible use of the funds available. Even without strict "goals" and "targets," an implicit competition is acting. This should ensure that regions obey rules of open competition in the choice of service providers — though the question of the regional body as a monopolistic entity remains.

A fourth potential problem for the local development policy is that the growing power of non-governmental development agencies comes at the expense of politically accountable elected local government. The involvement of business executives, trade unionists, chairmen of not-for profit organisations and so on, gives the appointed boards a great deal of professional expertise, but not necessarily local accountability. There is concern that the growing influence of regional unelected bodies will eventually result in questions about their fundamental legitimacy in such a vital role, shaping the economic future of the region. Obviously, complaints are particularly likely if the benefits of the local approach do not materialise and evidence of mismanagement, waste or corruption begin to surface.

A final question is whether these regional, co-ordinated policies can ever be compatible with national government policy. The government's need to take note of macroeconomic indicators and take actions that often have drastic consequences for microeconomies. An obvious example is the commitment of the Twelve to meet the convergence criteria outlined in the section of the Maastricht Treaty that deals with European Monetary Union. How will attempts to reduce fiscal deficits and cut government outlays affect the local development process. The problem remains that local development policies are still in a
probationary period and vulnerable to budget cuts. This situation will only change if national policies and local policies can be shown to be compatible and complementary, rather than one vital, the other, good publicity but ultimately expendable. A key element in this process will be the development of effective outcomes evaluation by which contribution to national goals and compatibility with national policies can be assessed (Stratton).

**The assessment of process versus measurable outcomes**

It is clear that there is no quick way to develop rural regions and no sure way to counteract the decline of heavy industrial regions. The process will inevitably be long and results will come slowly. And because results are often intangible, a degree of fortitude will be required to persevere with policies that seem to be bearing little fruit. Particularly in a time of fiscal contraction and deficit reduction, pressure to cut corners on local development strategies is likely to be great unless the positive contribution of local development projects can be unequivocally proven.

Assessing the contribution made by local development programmes is, therefore, vitally important in terms of attracting and consolidating outside financing and political support. It is also a valuable way of refining development policies. Unfortunately, the nature of local development projects means that the most valuable outcomes of a project are often barely discernible and usually unquantifiable. In the past, this has been a source of conflict between local development projects and central government funders, who demand tangible, statistically significant results, and has impeded progress toward more flexible, imaginative programmes.

The contradictory philosophies of actors at the national and local levels have led to calls from the local level for development assessment to be based more on process than outcomes; on levels of participation, breadth of community involvement, and so on. The assumption is that when the process is correct and achieves certain targets of inclusion and participation, positive results will inevitably follow. The effectiveness of the process is, however, hard to gauge and the results, when they appear, may be just as difficult to measure as the process was. Such things as regional self-confidence, a sense of community identity, heightened personal ambitions and entrepreneurial spirit are all positive attributes in any society, but are extremely difficult to enter on a balance sheet or convert into graphical form.

The difficulty of assessing the true contribution of the local approach has also resulted in moves toward the other extreme. The state of Oregon, for example, in its development programme has adopted a system of benchmarking or goal-orientation where local projects (and the state as a whole) are evaluated on their ability to reach precise targets set by state planners. The targets are result — rather than effort-based; i.e., such things as school expenditures and pupil-teacher ratios are considered as inputs and are therefore not indications of satisfactory performance. A report card for each programme grades success or failure in terms of these pre-set goals. This approach stresses that if there is real development it should be measurable, and the only way real development can be forcefully encouraged is by incentive-driven goal-setting and outcomes testing. The counter-argument contends that this approach merely results in manipulation of inherently weak data to reach questionable conclusions, solely to satisfy arbitrary targets. Furthermore, the role of the state in positioning benchmarks suggests both a top-down approach and the potential for political goal-setting. If the local role is merely as an executor of centrally planned policies, is there any real local content? Nonetheless, Oregon state administrators claim that the system has revitalised the state economy and helped to engender a general atmosphere of motivation and drive (Wyse).
In a similar fashion, the Training and Enterprise Councils in the United Kingdom also stress performance and results rather than efforts or process. Each regional body is given freedom to design its own projects, but within a national framework, working towards specific national objectives (Stratton).

Clearly central government will be reluctant to accept that the local approach necessarily produces uncountable "results" and will continue to expect some kind of outcome evaluation. An immediate priority for local development planners should be to address this issue. In a sense, the problem may be transitory and important only because the local development model is so new. The experience of the Community Futures scheme in Canada suggests that once a certain level of credibility is reached by local development projects, the attitude of government agencies toward insisting on specific results will become more flexible. Planners at both the local and regional levels should, therefore, carefully consider ways to enhance the credibility of their programmes. Unfortunately, it is difficult to create credibility without results, and results without credibility (Bryant).

The problem of programme assessment is as acute for an Austrian village community as for the states of Mississippi or Oregon. On whatever scale, development is "a process not an event" and must remain a flexible approach to constantly changing challenges. Evaluation of its impact will therefore remain a complicated and contentious issue, and the need for strong data to confirm the efficacy of local development strategies will increase (Mabus).

In summary, local development initiatives have brought a new direction to economic development policy. They have, however, had only limited impact so far and remain marginal to national policy planning.

There are signs that this is changing in the sense that independent area-based programs have demonstrated that comprehensive success can only be guaranteed through regional co-ordination. This has led, in some countries, to the creation of innovative regional bodies that have a broad mandate and act in a consulting and co-ordinating capacity without infringing upon the essentially local character of individual projects.

Further growth of this phenomenon will continue to be hampered by the difficulty of outcomes-assessment. Unless results can be quantitatively evaluated, national funders will be disinclined to commit greater funds. This problem can be partly overcome by making programmes explicitly performance- and results-oriented, as with the Oregon and TEC approaches, but this constricts the larger aspiration of local development to affect unmeasurable aspects of economic and social relations, attitudes, lifestyles and so on.
CHAPTER 3. BUILDING LOCAL CAPACITIES

It is clear that the new local development approach exists and, moreover, it is legitimate. "The question is not what to do, it is how to do it!"

The new approach is called the "Third Wave" of local development policies by Robert Friedman. Third Wave strategies are characterised by a desire to transform, to structurally adjust the local economic environment in a way that will increase quality of life and ensure sustainable development. There are several common features in this type of strategy. First, they empower local people to act on their own behalf and make their own decisions with help and advice from the policy-making body. Second, they aim for community-wide, cross-sectoral involvement. Third, organisations are financially responsible but freed from tight budgetary supervision and strict operating procedures. Fourth, financing strategies are investment rather than spending oriented. And, fifth, programmes are designed for scale; that is, they attempt to meet a large-scale challenge with appropriately sized policies.

On the economic level these general aims translate into local policies to boost local economic activity such as:

1. Activities to encourage region-specific innovation, including direct investment in technology centres relevant to local specialisations.
2. Large-scale intervention to co-ordinate education and labour training services with the changing needs of the labour market.
3. Assistance to small businesses, including marketing services, export organisation, design services, help with business contacts and accounting.
4. Encouragement of collaborative management efforts — joint ventures, just-in-time networks and technology sharing.
5. Continuation of regional government concentration on infrastructural development and incorporation of new roles to co-ordinate the activities noted above.

In addition, although centred around economic development, the new local approach tries to go beyond the economic sphere and address issues of economic disadvantage as they impinge upon other aspects of society. As Robert Friedman puts it, "For too long we have looked at poverty as purely a matter of income.” These local policies should try to affect local development through ameliorating social conditions and improving human resources. In short, by helping ordinary people to help themselves. This is, without doubt, an enormous challenge and cannot be achieved without a great deal of co-ordination and co-operation, among the local community in general, business leaders, education and training providers, central government and by introducing strategic planning and efficient networks and partnerships. This process is called "local capacity building".
The role of local capacity-building

The local content of a development policy, as has been stated, is one of its most obvious and potentially far-reaching elements. Yet to be effective vehicles for development, local actors must be able to respond to the new responsibilities of the local approach. The global market means that efficiency and competitiveness are the pre-eminent factors determining economic success and stable employment. In order to create and sustain growth, a local actors must be able to maximise as nearly as possible the region's capacity to produce efficiently and competitively. Particularly if "high road" development is the chosen development path. A region's assets can be broken down into two broad categories; Hardware or physical resources and Software or skills and training. Capacity building involves making the best possible use of these two types of asset and making them interact and complement one another (Martinos). The question for local development actors and/or government planners is to decide which skills training is appropriate, what type of investment will be the most fruitful, and so on, to attain this goal. However, it is apparent that a general approach to local capacity-building is emerging.

The basic elements of a successful development strategy are, generally speaking, the ability to network and spread the message; co-ordinating the objectives of diverse groups and individuals; entering into partnerships with a common and coherent goal; and designing and implementing the development strategies on a local level. These general principles have become more defined as a series of "second stage" problems have arisen that are conducive to local responses, but which require direct and forceful action. These problems include:

- tackling unemployment in general, but particularly in special groups such as minorities, disabled people and the long-term unemployed;
- promoting links between industry and education to build local skill capacities;
- using innovative techniques in job creation, such as incubator units, small business counselling, seed and venture capital, and so on;
- sectoral development, including tourism, environmental protection and cultural activities;
- innovative enterprise development; for example, encouraging entrepreneurship among skilled employed people not only the unemployed.

Obviously, internal resources alone cannot guarantee success, particularly in dealing with issues as complex and wide-ranging as these, despite recent refinements and increased capacity. External actors are essential to the process, but they must be brought into the process in such a way that the dynamic local flavour of the process is not sacrificed. At the same time untapped local potential must be given the highest possible priority.

There are five main areas where capacity can be built: the community as a concept; business involvement; financing; education and training; and networking/partnership development.

The community in the new local development process

After the large scale relocation of multinational corporations and the emergence of structural unemployment, the importance of creating a cohesive community has become prominent among local development planners. Business is only likely to feel committed to the community if the community
appears to be committed to itself. For this reason, the geographical communities must learn to act more collectively; speaking with a single voice in negotiations with central government, in applications to supranational bodies, in cultural matters, etc. There are major advantages for both the communities themselves and for governmental agents in having strong local participation.

First, it is much easier to target programmes to a clearly defined audience in a specific geographical entity, one recognisable both to government and to the inhabitants of the area. The stronger the sense of community, the more a programme can be made region- or municipality-specific. As has already been noted, the local content of the policy is its main feature, so the more a policy can be made particular the more it will generate external economies, through mobilising community-wide partnership and co-operative networks. The sense of community is also important in eliciting outside support for the local development process.

Second, the local development model is untested and has produced few unqualified success stories thus far. In consequence, it is a relatively low priority for public funds and remains of marginal though increasing interest. The credibility deficit that local projects experience in dealings with government is exacerbated if programs are uncoordinated and individualised, thus seeming even more trivial and irrelevant (Bryant). A solid recognisable community makes a far more influential lobbyist. Public and private funders inevitably have a tendency to reward superficial factors such as professional presentation style and solid image. A community application therefore stands more chance of success than individual approaches because greater resources can be invested in impressive presentations and more work done on creating or appropriating an image, a slogan and a motif for the region.

And finally, the presentation of a credible image to the outside world is only half the story; the image also provides a rallying point for the community itself, enhancing civic pride and civic participation. A strong indication of the value of civic participation and communal self-reliance is offered in the negative case of Southern Italy. There is a growing feeling that sustainable development can only come from endogenous factors, one of which is "civiciens". This concept — a mixture of political activism, local organisation and self-sufficiency — is, it is argued, difficult to create and explains, to some extent, the difference in economic performance between, for example, Emilia Romagna and Calabria. In regions lacking a strong community spirit, there has been a tendency to accept local development initiatives as short-term handouts without really capitalising on the opportunities for generating participatory local development institutions. This is important because the community approach is by its nature selective, in the sense that only the most politicised communities will generally receive funds and be able to respond constructively to their problems. Without such community drive, the ability to attract funds and co-ordinate policy is severely restricted. The example of Community Futures suggests that the Canadian government has recognised that communities are capable of solving their own problems with a certain degree of guidance and financial assistance. But as active participants in local development rather than merely recipients of aid should ensure that the breadth of stakeholders is increased and a greater number of people in the community feel like contributors and participants in the development process. In the past, "local" development schemes have often been hijacked by elite groups — business leaders and politicians — and have lost the local element, but the potential for this should be reduced in a strongly politicised and informed community. The significance of the community input has now been widely recognised and planners give it increasing prominence and consider it as a tangible local asset (Fuller).

The role of business

Large businesses have a somewhat tarnished reputation in the field of local development. In the Fordist era, when large multinationals were seen as the engines of economic growth and main providers of
large-scale, stable employment, they held a privileged place in the local economy. In this period of structural adjustment, however, due in part to the relocation or rescaling of many of these large corporations, their ties to a particular community have been shown to be fragile. And the consequences for the local community of overdependence on large mass-production plants are now all-too-evident. A central tenet of local development policy, concentration on small and medium-sized, locally based firms, is thus, in part, a reaction against businesses directed from headquarters outside the area, with few ties to the local community and little interest in improving the local physical and social infrastructure.

Nonetheless, large businesses represent a huge reservoir of managerial, technological and financial skills and experience. The aim should be, therefore, to increase contacts between business leaders and local development actors with the ultimate aim of increasing the scope of business involvement in community projects and making it "a normal part of business practice" (Grayson).

An example of this is the tutoring system instituted under Law 44 in Italy whereby businessmen or consultants are assigned as tutors to a new enterprise and offer "on-line" technical assistance and training. The assumption is that entrepreneurial ability cannot be taught and is better acquired through practical experience. The tutors are assigned with care, to ensure that they have skills and experience appropriate to the pupil enterprise. The organisers also hope that the tutors themselves learn from the experience of helping new businesses and will be willing to take an even more participatory role in the program based on their experiences (Roncaglia).

Even in the absence of incentive schemes, some companies have a tradition of participation in local community activities, and this should be actively encouraged. Particularly during a recession, firms will try to cut spending on peripheral projects like community action projects. It is imperative that local people persuade firms currently involved in the local community it is not a peripheral issue and has concrete benefits for the company. Similar arguments must be invoked in an effort to bring in new firms. Unlike other regional development programmes, the focus is on enterprise creation not job creation, which is an important by-product.

From the other angle, local development groups need to learn how to make the best use of this highly-trained consultancy service. The contact with business leaders should also promote an imitation of the professional standards required in business, raising the quality of presentations, proposals, applications and lobbying by local development agents.

The involvement of senior business leaders is, however, worrying for many people involved in local development work. Their participation is seen as another distraction from the real original feature of the local approach — its local content. Business leaders are experienced in talking with government and there is the suspicion that the two may conspire to crowd out the local element is the most exciting and progressive aspect of the new local approach. Also the input of business leaders will, some think, make the process top-down in structure and too economically focused, leaving little room for social regeneration.

On the other hand, few would argue that business should be excluded from the process. Rather, the involvement of business should be as one of many partners. Its role should exploit the skills of businessmen both to assist local entrepreneurs and also bring new interdisciplinary approaches to non-economic problems and issues.

The question of domination of the process by business interests can be avoided if the role of business is enabiling, that is, attempts to increase the capacity and efficiency of local actors. The problem of unequal partnerships with business, as with central government, remains unresolved.
The role of finance

Although the role of larger corporations and business groups in steering the local development process is controversial, the need for finance to stimulate the local economy will remain central to the success of local development initiatives.

Traditional economic development policies stressed the overarching importance of large corporations in creating jobs and fostering economic prosperity. Development strategies were therefore designed to attract investment from these firms, by subsidies, low rents sites, and other financial incentives. Today, however, the situation is much changed and there is evidence that multinationals are now creating no net new jobs and all job creation is taking place in small- and medium-sized enterprises. Local development strategy must concentrate on encouraging the appearance of such enterprises and, obviously, financial factors must play a major role in their emergence and prosperity.

The rate at which firms are generated and mature depends in large part on the ease of access to sources of capital. Where funds are available at an acceptably low cost, entrepreneurship develops and one aim of local development planning must be to make such pools of capital available to the budding entrepreneur.

Contrary to general perception, most entrepreneurial ventures have only moderate growth potential. The new businesses founded by established and successful managers and those harnessing cutting edge technology are easy to finance and the myriad of venture capital firms have no qualms about investing in them. Such high growth companies constitute the minority of job-creating enterprises. The majority have more “pedestrian” potential, yet, by their sheer number, they have a significant role in a well-functioning economy. Despite this, they have difficulty finding sources of finance and there prospects for survival and thus, indirectly, that of the regional economy itself, are greatly reduced.

There are two main reasons why banks are unwilling to finance these low-return SMEs: first, the risk involved in investing in a business with, presumably, no collateral and no track record is too high; and, second, loans to large businesses are proportionally far more profitable than low-principal loans to SMEs.

This significant market failure was identified in the 1980s and led to the creation of publicly guaranteed or funded product development companies and venture capital funds specifically aimed at the small business sector. However, although well-aimed, these schemes proved to be inadequate to deal with the scale of the funding shortfall. As Paul Pryde put it, they were "million dollar answers to billion dollar questions.” The approach has been refine since the mid-1980s with the aim of making development finance more appealing to the private sector and reduce the perceived risk involved in development finance.

Three examples help illustrate the new formulas for fostering investment in small- and medium-sized enterprises:
1. **Asset Securitisation.** This is the bundling of assets to create collateral on the basis of which securities are then sold. These collateralised mortgage obligations (CMOs) enable banks to earn often good rates of return without having the risk and possible regulatory scrutiny that would be invited by bank or pension fund investment in individual small enterprises.

2. **Portfolio insurance.** This attempts to reduce the risk inherent in loans to small- and medium-sized new businesses. This can be done by calculating the default rate on loans to small businesses and then offering portfolio insurance to protect banks against bad debt losses at a significantly higher rate. Sufficiently broad coverage will allow banks to extend credit to entrepreneurs with little or no experience. The insurance cost is covered jointly by the participating bank and central government and as such offers a way for the state to encourage investment in small business without taking full financial liability itself. In addition, arithmetically, banks are rewarded for making more loans, which increases their earnings without greatly increasing risk. As is the case with most government-sponsored schemes the tendency for the application process to become too bureaucratised should be avoided.

3. **Investment tax deduction.** Because of the difficulty of finding regular sources of funding, most initial capital in a new business comes from personal savings, or from relatives and friends, rather than from banks. An effective way to promote investment to new businesses, therefore, is to offer significant tax relief for those who contribute to the start-up capital. This, in effect, redirects money that taxpayers money into small business support without it having to work its way through various government agencies before being distributed to local development initiatives. It also, very importantly, puts investment decision-making in the hands of those who are closest to the project. The fact that their own money is involved rather than some government grant implies that the idea is sound and suggests that the participants will put all their efforts into making the business a going concern.

The foregoing examples illuminate the three guiding principles of development finance policy in the 1990s. First, policies must "achieve scale". They must be designed to alter the investment behaviour of commercial lenders and change the flow of business capital so that the large needs of small businesses are adequately met. Second, the public cost must be low, both for reasons of fiscal stringency and because public financing induces complacency on the part of both enterprise and lender. And, third, programmes must be incentive based. That is, they must tangibly reward investors for the risk that they take.

Paul Pryde nevertheless speculates that the next phase of development would be "characterised by fierce competition among commercial lenders to give money to people they currently ignore."

**The role of education and training**

In order to build the software capacity of the region, it is vital that education and training providers adapt to meet more fully the needs of the business community and effectively prepare the labour force for employment in today's rapidly evolving economic environment. Educational systems need to take greater account of major changes in their economic environment and take appropriate action. In addition, of course, educational institutions must continue to fulfil their traditional role and provide a solid general, humanistic education and stimulate personal growth.

The question of education and training is primarily one for late secondary and tertiary-level students and adults. However, attempts have been made to inculcate an entrepreneurial spirit at an even earlier age. In Norway, the "Pupil Enterprise" scheme utilises the natural creativity and imagination of
the students to develop genuine market-oriented products or services. The student-entrepreneurs learn how to construct and follow through a business plan, conduct market research, prepare a budget and keep accounts. This practical experience is valuable not only for the students themselves, but also for the community in general — teachers, friends, relatives, local businesses are all inevitably drawn into the process and this helps to foster a sense of entrepreneurship beyond the confines of the school itself. The organisers hope that by integrating the programmes into the curriculum of the school, it will be possible to avoid claims that general educational standards will suffer from this distracting influence. A tertiary level course on "the world of work and entrepreneurship" serves to contextualise the practical projects (Kjelsen).

Some concerns have been expressed, nevertheless, about the effect the strengthening of ties between education and local business will have on the fundamental role of education. There are fears that the school could become too vocational in structure and too intellectual limiting. For example, entrepreneurship training in schools, which is being undertaken in several places within the OECD area, should integrated into the curriculum in a broader context. The integrity of learning as the acquisition of knowledge rather than as a means to make money must be maintained. Without it, the educational system will be seriously undermined. This objection is obviously less applicable to adult education.

The concentration of the university system on conducting major research projects for industry is also being questioned. It is argued that the university should move away from this multinational or large corporation-centred approach and take a greater role in training people to innovate individually as entrepreneurs. Instead of using them as a part of a large research team and conditioning them to expect or desire a research job in, for example, a large pharmaceutical company on graduation, they should be made aware of the opportunities for opening a small business.

The most pressing issue for educational institutions is, however, adult education and retraining rather than primary and secondary level initiatives. Clearly, one of the important elements of local capacity-building involves up-skilling the labour force to meet the needs of “high road” development policy. To this end, most OECD countries have made retraining efforts a matter of priority. The problem now is fundamentally one of organisation. In Norway, for example, the educational system is fragmented between several different government departments and at many different levels. The first objective should thus be to co-ordinate activities to ensure that the government is not funding duplicate courses at different school and colleges. Not only should course offerings be analysed to make best use of available funds, but in order to contribute to the development of the local region, education planners need to evaluate the training needs of industry. This will require a major effort on the part of education planners to consult to with industry not only about present needs but also future, anticipated requirements. It cannot be taken for granted, of course, that industry knows what type of school leaver will suit its future skill needs, and a high degree of strategic planning will be required from the two sectors.

One way to arrange closer ties between the two is to use local employment services as a broker between the two. Local employment agencies have close links with local industry and also have influence through interdepartmental links with local education authorities and training institutions. Possible responsibilities for the local employment centres would include:

− mapping the training needs of industry;
− passing on findings to educational organisations;
− initiate and guide the development of certain courses;
− motivate companies to utilise courses and programs;
– establish and operate arenas for consultation (Arbo and Bjornavold).

Despite the specificity of these duties, the basic task of the local employment agency is simply as a facilitator to promote and maintain relationships between education and industry. Once integrated the three bodies should be able to work effectively together to improve the quality and suitability of the local labour supply.

A further goal for the education-local employment office-industry partnership should be the redistribution of “matière grise”/“grey matter” into rural and semi-rural areas. This redistributive function is indispensable if these areas are to develop the other attributes — new production technologies and innovations, and so on — that are needed to achieve competitiveness on a regional basis (Monory). As with other projects in rural areas, the initiative will probably not evolve naturally from the market and needs to be promoted by an external organisation.

As a cheap and easily implemented method of improving educational service provision, the importance of networking and integration cannot be overstated. An integrated network of colleges and trainers reduces course duplication, facilitates information exchange, ensures that market gaps can be closed efficiently and allows for the sharing of equipment. As well as improving service delivery from the supply side, it also improves the service from the customers’ point-of-view, giving the appearance of a perfectly comprehensive range of services. A supervisory body could help initiate communication between different educational bodies and ensure that quality of service is maintained while wasteful competition is minimised.

**The importance of networking**

It is true that markets are becoming more competitive and more global. Yet when markets enlarge there is no inherent drop in production costs. The potential to relocate in South Korea or China gives some scope for cutting production costs, certainly in the more labour intensive industries. However, that the key element in the new economy is not a drastic drop in production costs, it is a reduction in transaction costs (Lahti). The layered structure of control and hierarchical management that developed and contributed most to transaction costs are now redundant because of the simplicity and speed of information exchange. Without vertical depth, companies are more obliged to rebuild their operation networks horizontally, depending on other actors for services they traditionally took care of themselves. There are several examples of successful horizontal networking ranging from manufacturers like Benetton and Toyota to the Italian province of Emilia Romagna.

There are different kinds of networking that bring tangible benefits. Some are merely an extension of normal social practice. For example, in the case of Italy where family and social networking is strong, the task is to push these networks beyond their natural geographic limits.

Indeed, constructing networks of entrepreneurs might be more valuable than such innovations as incubator units and technology parks. The implication is, in keeping with a tenet of the local approach, that existing local strengths should be built upon rather than insisting on experimental test tube projects. In areas such as northern Italy, the ancient entrepreneurial culture represents a powerful springboard for economic growth. As such it is an obvious starting point for local development strategies (Garofoli).

On the other hand, the Carpi example demonstrates the value of a mix between network building and new techniques in education, training and enterprise creation. In Carpi, partnerships between firms and trade associations are common and traditional. The main problem is not so much the creation of
networks as the transformation of informal ties into formal durable networks. Participants are well aware of the advantages of partnership and co-operation, but they also have a strong tradition of informal networking, independence and autonomy. Nevertheless, the widespread participation of local enterprises in working relations is a great advantage for a local economy.

The Business Service Centre, CITER is able to concentrate its efforts on building the competitive capacity of member enterprises, without worrying about the networking issue. In fact, in this case, it is CITER that must strive to develop connections and create networks — with central government, the European Union, trade associations and distributors in other countries and so on. Finding institutional partners for CITER is thus an important aspect of the networking process in the area (Ligabue).

In many cases, however, the concept of networking as a matter of policy is unknown or the element of trust between businesses is underdeveloped. In this case, a concerted effort must be made to overcome these habituudinal prejudices, by no means an easy task.

The most obvious type of networking is social networking. The basic point is that the various actors in a production chain should know each other, appreciate one another's contribution and come to rely on each other. If envy and personal antipathy colour relationships then it is inevitable that social barriers to networking will exist and transaction costs will remain high. There are many ways to promote friendly relations among businessmen and community group leaders, from seminars to dinners, and so on. (Lahti)

Political networking means forming business relationships, perhaps fostered by social contacts between representatives of the two firms but also possibly the result of a conscious active search for potential collaborators. The first phase of political networking involves entering into contractual relations and progressing from this stage to alliances and joint ventures then finally to common ownership. This is dynamic networking, along delicate process of building socio-economic trust. However this is only one side of the story. Networking cannot produce results unless the company already has a viable market position which networking can exploit. Thus networking and partnership creation are not substitutes for efficiency and competitiveness; they can merely enhance existing potential. However, there is evidence that the boost to an enterprise of active networking and involvement in the community can be enormous and well-worth the time and effort (Lahti).

The important point to remember is that networking is not necessarily something that will happen naturally. It must be pursued as an active policy by companies. And in order to facilitate the process, national, regional or local bodies must be established to bring entrepreneurs together and imaginatively find elements of common interests between firms in different sectors to cut transaction costs.

In conclusion, the key points are: first, the Community should be an identifiable geographical territory able to mobilise local inhabitants. Second, it must establish itself as a partnership by removing traditional sectoral demarcations and working toward commonly defined goals. And finally, the partnership must engage a wide range of actors from all sectors of the Community — its educational institutions, business groups, financial institutions and the residents themselves — acting in co-operation with one another.
CHAPTER 4. A NEW ROLE FOR GOVERNMENT?

The two major trends in central government policy as it touches upon local development are decentralisation and cross-sectoral co-ordination. Both will have a great impact on the direction of local development policy in the next few years. Indeed, decentralisation has already been recognised in France and elsewhere as an excellent method of furthering area-based development initiatives (Monory). But, both are problematic and raise complex issues of power redistribution and politically delicate questions of power-sharing.

Decentralisation has been a rallying point for local development initiatives in recent years with the assumption being that central government is too distant and preoccupied to play an effective role as the director of local development initiatives. Yet, however desirable, decentralisation is a process that can be undertaken in two ways by central government; either responsibly or irresponsibly. The irresponsible route is for government to devolve power and then walk away, leaving local authorities or non-governmental agencies with wide-ranging powers but little experience in organising or delegating them.

The preferable route is for government to decentralise gradually and supportively. It is important that the government knows why it is handing over which powers and realises that decentralisation is an active policy not a passive abrogation of responsibility. It requires a strong awareness of where the powers are going and a realistic evaluation of the capacity of the receiving body to take on this new role.

Government is thus vitally important and intimately involved in the process which suggests that the process will proceed as it wants rather than with respect to the wishes of local development agents. The reply is that it does not represent top-down, governmental planning. Rather, as government decentralising itself, it is a necessary way to find a new framework within which the central authority's role is more limited but not removed.

The new role for government is as a partner in local development. But it will remain a vitally important element in any program; if only because central funding is so crucial to the success of many local development initiatives. In addition, certain functions appear to be necessarily a public domain. For example, long-range planning of telecom systems, environmental protection programs, pollution control, and so on need to be tackled from a broader perspective than the local. On the other hand, some commentators argue that these same services offer a way for even the least developed regions to develop a certain amount of economic vitality. By running strategically important local services or new high-profile industries autonomously, each region would control a large budget and could try to use these public service provisions as a lever to economic growth, for example, by preferential procurement policies toward local suppliers and using local sub-contractors.

The issue of privatisation raises similar issues — whether privatisation means more or less control over local service delivery than under a nationalised system. If the public corporation is broken down into regional private businesses then this suggests a greater level of control and perhaps opportunities for local small businesses and service providers. If, however, large national private corporations take over and operate from national headquarters, the region is left very much unaffected. A
national corporation may use economies of scale in its buying policies and, without links to the local community, may not bring any significant economic advantages to the local economy.

In fact there are several areas where central government monopolies are not favourable to regional development. The major example of a geographically sensitive industry affected by moves away from central economic management is electricity provision, widely regarded as one of the vanguard industries in any economy. A reappraisal is needed of the situation of this and other major industries where the entry of local actors is impeded by political barriers, arbitrary regulations or powerful economic vested interests. The benefits to small business and to the local economy as a whole could be quite considerable.

Yet the ability, as well as the willingness of government to carry out these redefinitions of its role and the way it organises economic activity is in question. In the same way that local actors are being rated on their suitability as partners in the local development process, the capacity of central government must also be assessed. Blessed with high-quality staff and strong financial and informational resources, central government should, in theory, be a most desirable partner. But the move toward decentralisation is, in addition to being motivated by a search for greater efficiency in local decision-making, is also being demanded by local actors who feel a sense of mistrust, dissatisfaction and sometimes outright hostility to the central government. Local development policies in the 1980s were often hampered by conflicts with local and regional organisations who resented the imposition of government programmes. Because of this anti-central government mood, it is imperative that central government prove itself to be a capable local development partner. In what can be called a multi-stakeholder system, the government is an important partner and could play a crucial role in overseeing the whole process of local development. In order to do this, however, it must comprehend and sympathise with the process and its anticipated outcomes.

It is clear that working on a local-level development project is a far cry from planning the national policies of a Ministry. What then do central government agents know about the enabling skills of local development: conflict resolution, negotiation, confidence-building, and so on. Can central government adapt its operating procedures to cope with involvement in local development projects where results are incremental and certainly cannot be timed to coincide with electoral cycles. Similarly, can the accountancy and audit-driven procedures for which government is castigated be revised to cope with the non-monetary outcomes and elongated timeframe of local development initiatives? There is also the difficulty of evaluating programs where the results are intangible and can be seen only in, for example, growing self-confidence, regional cohesion, increased collaboration. In periods of budgetary constraint, the security of such programs will be repeatedly undermined unless some way can be found to integrate this type of program into the national fiscal accounting structure.

As one suggested method of alleviating this problem, it seems logical that government should undergo a period of retraining like many of its citizens. There are several ways that this situation could be improved:

- Civil servants should be trained in aspects of local development work and their business management skills should also be enhancement.
- Exchange tours could help bring together senior administrators and local development workers. Once administrators have seen projects at first hand, they may have a better understanding of how such projects contribute to the local economy and be more sympathetic to the broader aims of local development.
Perhaps most radically, civil servants could be seconded to work for an extended period of time on development projects alongside local development workers. This would immeasurably broaden their perspective on the value of the local approach.

Evidently what is required, from the point of view of local development activists, is a re-evaluation of the aims and attitude of central government; from pure growth to sustainability; from control to flexibility; from universality to targeting; and from a concentration on economic goals to inclusion of social objectives. In all cases accompanied by decentralisation and devolution of power. In short, central government must rebuild trust in it and its agencies in the community. Capacity-building at the central level.

Yet such a change in attitude will not come about unless local development groups build a greater degree of trust and respect between themselves and central government. From the government perspective, it would be failing in its public duty as guardian of taxpayers money if it were to disburse money without first having a clearly defined project proposal. There is a feeling among local development workers that government has an audit mentality that frustrates creative attempts to encourage local growth. Local development agents would prefer that, while expecting appropriate managerial standards, government should not be restrictive in how the funds are used. But the question of accountability means that government will probably continue to demand a comprehensive statement of why the funds were needed and how they are to be spent.

In addition to acting as custodian of public finances, the government is also committed to protect the interests of all its citizens, including minority groups and geographically remote areas. Local development proposals must be balanced to reflect diversity in the community. Furthermore, as guardian of national values and morality, the government should ensure that its role includes the ability to uphold national interests and values as they are affected by local initiatives.

From another angle, will central government be willing to accept the shifting power relations between it and the variety of new regional and local bodies? It is tempting for central government to see local organisations, particularly not-for-profit groups as amateurs and therefore be disinclined to grant scarce funds for a project administered by them. Moreover, as has been foreseen in the case of the TECs, the government has a responsibility to account for its use of power, and will be naturally cautious to grant excessive power to an unelected body over which it has limited control. The question of the legitimacy of regional bodies arises from the perspective of central government as well as from local actors.

Nevertheless, the ability of central government to act effectively alone in the local environment is seriously compromised. However well-intentioned they may be, government agents run up against information deficits and partner deficits. Without suitable local collaborators, lack of deep knowledge and understanding of the local geography, business scene and labour markets represent insurmountable obstacles to an effective locally implemented national policy. Depending on the tradition of relations between central government and its regions, finding suitable partners with whom to interact can be a frustrating experience, exacerbated by baggage brought from a tradition of centralised policy-making and the accumulated conviction that local actors are not trustworthy or reliable stakeholders. Organisations such as Chambers of Commerce may prove to be a useful liaisons between government agents and the local community. They have an intimate knowledge and contacts within the local business community and knowledge of local geography and customs. Perhaps most importantly they have long experience of working with government bureaucracies.

Despite the problematic history of relations between state and local actors, there is general agreement that an active government policy in some form or other is necessary or desirable for a
successful local approach. A division of roles according to competence will ensure that powers are efficiently distributed. It is a matter not of transferring responsibility from one place to another. Rather it is process of convincing central government of the value and contribution of local programmes to the national economy. Government, once convinced of the competence of local actors, will act as a more committed partner.

Nevertheless, if central government fails to react with sufficient speed or enthusiasm to meet local demands, then, at least in Europe, the role of international bodies will inevitably increase. Already, the impetus for a new formulation of national-local relations has been inspired by the European Community. The Structural Funds are seen by some observers as a model for organising relations between a central, financing body and competing regional applicants for financial aid. The regulations governing Structural Funds require applicant regions to submit a detailed project description along with a budget and method of outcomes-testing. This requirement for solid and comprehensive proposals means that the grant-awarding authority, in this case the EU., has a ready means of tracking the use of funds without having to act as a "Big Brother" scrutinising and demanding justification for each expense. This system is also beneficial to the local actors who must create persuasive outlines and, in the process, think through and refine their proposals in what are essentially competitive conditions. Across Europe regions are developing marketing departments to lobby the Commission for funds. Obviously, only the most cogent and well-considered projects will receive funding and the mere application process is a great learning experience for local development organisations.

In some ways, this process of by-passing national government and organising at an international level demonstrates the innovative and original nature of local development strategies in the 1990s. Rather than waiting for information to filter down through international organisations like the OECD to national governments and eventually to the local level, communities are exploring supranational funding options. The trend towards trading blocs with international or supranational high authorities may increase the number and importance of bodies to whom regions can turn for project finance. As the value of alternative sources of finance increases, the role of government will inevitably decline. Certainly, the process conforms closely to the principle of subsidiarity and as such will be strongly supported by the EU, at least until national government express their objections.

However, there is hope that the addition of a new tier of government above the national level will in fact spur national governments to reinvolve themselves. With both locally sponsored and EC-funded projects to learn from, central government may make strides to imitate the success of other programmes and adapt its programmes to meet more closely market demand. By implication, government in its local development activities becomes a service industry, an entrepreneurial business, competing to provide services to customers. In this way, the state may be able to overcome its institutional inertia, not to mention the misgivings of many potential customers, and create a niche for itself within local development work.

In summary, the old problem of "them and us" persists in relations between the state and local actors. An attitude of partnership needs to be created by means of closer and more imaginative meetings between the two groups. Local development should endeavour to overcome the doubts of government agencies by presenting authoritative development plans. At the same time, in addition to broadening its co-ordinating role, government must ensure that local actors are received sympathetically and greater flexibility in approach is accorded to local development issues. The key, then, is decentralisation without disengagement.
CHAPTER 5. CONCLUSION

As mentioned earlier, the question among local development actors is no longer "What to do?" but "How to do it?", or, rather, “How to do it better”. The foregoing discussion outlined the present condition of area-based economic development approaches and suggested some conclusions about how to take the process a stage further.

The idea of "geography in policy-making", that is, the conscious attempt to incorporate spatial considerations into economic policy planning, depends, essentially, on the successful identification of the ways in which national goals and local policies interact. Five important links between the two can be summarised as follows:

1. Local and regional development activities do seem to actually work as a means of creating jobs and promoting economic growth, both in regional and in national terms. An aggregation of well-organised regional economies results in a healthy national economy.

2. Strong (equalising) regional policies are a precondition to strong structural adjustment policies. Drastic national measures to meet macroeconomic challenges can only be implemented if concurrent regional policies soften the blow on a social level and reduce the political fallout of unpopular economic policies.

3. Unhappy past experience of precipitous decline caused by over-specialisation means that in order to wholeheartedly embrace an industrial policy of regional re-specialisation, regions need to be convinced that central government and/or international organisations will be willing to step in should their comparative advantage erode. This requires strong co-ordination between central government and local regions to design a patchwork of complementary, rather than competing, regions.

4. The nature of the state budget means that wealthy regions pay to support the development of other regions. Assisting regions to help themselves and reducing dependence on the budget as a method of regional economic equalisation will reduce poor regions' vulnerability to grant cuts and lower the tax burden on richer areas, in turn promoting further growth.

5. Deregulation and privatisation will tend to remove regional representation in large sectors of the economy as regionally-administered public enterprises are sold off into the private sector. A special effort should be made to achieve the regional profile that was once assured by the regionalization of nationalised industries. The ultimate objective is to harness the power of the public sector for specific regions.

In order to ensure that these links are identified, examined and conceived of as opportunities for remaking the relationship between the centre and regions, there are some specific proposals that should be adopted.

− OECD member countries should make a conscious effort to act upon the links mentioned above and work to create an efficient balance between national and regional policymaking.

− The "add-sum" hypothesis, which asserts that economic gain for one region adds to national wealth without necessarily coming at the expense of other regions, needs to be analytically proven.
- A similar study should be commissioned to find empirical evidence to support regional specialisation in preference to diversification. The study should also address ways in which central government can co-ordinate the various specialisations of its regions and investigate the feasibility of insurance pacts between the state and its regions to protect against economic adversity.

- The inter-regional economic transfers produced by the state budget should be mapped and their characteristics and influence ascertained.

- The political and administrative units on which geographically sensitive policies are currently based should be re-evaluated in terms of size and optimal profile — perhaps taking a cue from innovative metropolitan planning and decision-making efforts.

- Finally, the pedagogical problem needs to be overcome. Preaching to the converted is no longer enough, converts must drawn in. The task of spreading the word about area-based development is not an easy task but it must be undertaken effectively if further progress is to be made.
BIBLIOGRAPHY

ARBO, Peter and Jens BJORNARVOLD, "New Roles and Challenges for Educational Institutions in Economic Development Innovations in Norway".

BAILLO RUZ, Valeriano, "Des initiatives locales au developpement territorial: L'expériece Espagnole".


FULLER, Tony, “Community Futures: An Approach”.

GAROFOLI, Gioacchino, “Economic Development, Organization of Production and Territory”.

JOHANSSON, Marten, "A Scandinavian Business Grouping".

KIYONARI, Tadao, "The Global and the Local: A Japanese Viewpoint”.

KJELSEN, Oddny, “Innovations in Norway”.

LAHTI, Arto, "The Tree-Finland Program as a Case Example of How to Develop an Industry-Specific Regional Network Economy".

LIGABUE, Loredana, "L'industrie de la bonneterie dans le district de Carpi at l'expérience du CITER".

MARTINOS, Haris, “Building Capacities at the Local Level: A Review of Recent Experiences in EC Countries”.

MAGALHAES, José M., "De nouveaux roles et responsibilités pour les gouvernements: L'adminstration centrale et les initiatives locales (un temoignage).


QUEVIT, Michel, “Impacts des changements structurels sur les dynamiques territoriales du développement local”.


SZCLACTA, Jacek, "Mega Adjustments and their Regional and Local Impact in Central and Eastern Europe (case study: Poland)".

WEVER, Egbert, "Local Initiatives: From Exception to the Rule".
Mr Valeriano BAILLO RUIZ
Deputy Director of the National Employment Institute (Madrid)
Spain

Mr Jordi BORJA
Responsible for International Relations
Office of the Mayor (Barcelona)
Spain

Prof. Christopher BRYANT
Department of Geography
University of Montreal
Canada

Mr Carlo CARMINUCCI
CENSIS (Rome)
Italy

Mr Jacques CHEREQUE
Former Minister for Regional Development and Industrial Restructuring
France

Mr Liam CONNELLAN
Former Director-General of the Confederation of Irish Industry
Ireland

Mr Jean-Paul DE GAUDEMAR
Chairman of the OECD Working Party on Regional Development Policies
France

Mr Jobst FIEDLER
Chief Executive Officer
City of Hanover
Germany

Mrs Eithne FITZGERALD
Minister of State
Office of the Deputy Prime Minister
Ireland

Mr Robert FRIEDMAN
The Corporation for Enterprise Development
USA

Prof. Tony FULLER
School of Rural Development
University of Guelph
Canada

Prof. Giaocchino GAROFOLI
University of Pavia
Italy

Mr David GRAYSON
Business in the Community
United Kingdom

Dr Richard HUMMELBRUNNER
Director, Regional Development Agency ÖAR
Austria

Prof. Tadao KIYONARI
Hosei University (Tokyo)
Japan

Mrs. Oddny KJELSEN
Director General
Ministry of Agriculture
Norway
Mr. Hartmut KREBS
Secretary of State
Ministry of Economy, SMEs and Technology
for North Rhenanie
Westphalie
Germany

Prof. Arto LAHTI
Helsinki School of Economics
and Business Administration
Finland

Mrs Loredana LIGABUE
Director, CITER (Carpi)
Italy

Mr Ray MABUS
Former Governor of Mississippi
USA

Mr Joao MAGALHAES
Ministry of Labour and Social Security
Portugal

Mr Haris MARTINOS
Director
Local and Regional Development Planning
(Brussels)
Belgium

Mr René MONORY
Former Minister
President of the French Senate
France

Mr Gösta OSCARSSON
Swedish National Board for Industrial and
Technical Development
Sweden

Mr Paul PRYDE
Development Finance Consultant
USA

Prof. Michel QUEVIT
Catholic University of Louvain
Belgium

Mrs. RONCAGLIA
Agency for Youth Entrepreneurship
Italy

Mr Richard SCOTHORNE
Director, Partners in Economic Development
Ltd.
United Kingdom

Prof. Allen SCOTT
University of California Los Angeles (UCLA)
USA

Mr Werner SENGENBERGER
Director
International Institute for Labour Studies
(Geneva)
Switzerland

Mrs Kay STRATTON
Adviser to the Secretary of State for
Employment
United Kingdom

Dr. Jacek SZLACHTA
Deputy-Director for the Regional Policy
Planning Office
Poland

Prof. Egbert WEVER
University of Utrechtt
The Netherlands

Mr Duncan WYSE
Executive Director
Oregon Progress Board
USA