From national to local economic development:
theoretical issues

Mario D. Tello

Based upon a brief and selective survey of the literature on local economic development (LED), this paper analyses four theoretical aspects that distinguish "local" economic development theories from their "national" counterparts. These are: location factors, local public goods, active participation by a variety of private agents, and the multidisciplinary approach of LED theories. This analysis could be used to design an academic discipline of LED, which seldom exists in developing countries, and shed light on the objectives and roles of agents involved in ongoing decentralization and LED processes in those countries.

Mario D. Tello

Associate Professor and

Research Fellow

CENTRUM Católica and

Economics Department,

Catholic University of Peru

✎ mtello@pucp.edu.pe

I

Introduction

Local economic development (LED) theory and national economic development (NED) theory are well established disciplines that are taught in most universities in industrialized countries (Blakely, 2003). Although developing countries, particularly in Latin America, have a long tradition of implementing regional policies, such as river-basin planning, tax incentives, regional development agencies, growth hubs and integrated rural development, which spawned an initial wave of graduate programmes on local economic development back in the early 1960s, Latin American universities rediscovered an interest in this field as recently as the early 2000s. The decentralization processes implemented in many developing countries over the last two decades (Montero and Samuels, 2004; Stren and others, 2002; Aghón, Alburquerque and Cortés, 2001; Oxhorn, Tulchin and Selee, 2004; and Rondinelli and Cheema, 1983) have contributed to this renewed interest. International development institutions are also paying attention to LED, and providing funding for it, as shown on their specific Internet pages.[1] Generally speaking, LED issues in geographic areas (regions, counties, provinces and/or departments) in developing countries are analysed through the NED framework without including distinctive local-development features. Moreover, government agencies operating at the local level, along with economic, social and political agents residing in specific areas, perceive that economic development

in those areas depends heavily on the interventions and economic policies implemented by central (or federal) government.[2] This article seeks to form a bridge between current LED and NED theories, by briefly surveying four additional theoretical aspects that distinguish local economic development theories from their national counterparts in the analysis of LED issues.

The first of these consists of the location factors associated with specific geographic areas in an economy; most *national* economic development theories implicitly assume an economy's territory to be homogenous. The second aspect is the nature of the goods and services provided by different levels of government, where NED theories implicitly assume that the influence of the public goods and services provided by government covers all geographic areas of the economy. The third aspect is the role and participation of specific agents living in the local areas. Traditional NED theories do not incorporate this explicitly. Over the last two decades, however, modern NED theories have given a more important role to the behavior of agents, although not necessarily linked to the local areas in which they live. The fourth aspect is the multidisciplinary approach to the analysis of LED issues. In NED theories, the focus is on economic fundamentals and the workings of markets, institutions and organizations, irrespective of the geographic areas in which they operate. A brief and selective survey of these four aspects is presented in sections III to VI of this article. As a starting point, however, section II discusses some of the definitions of LED found in the literature; and, lastly, section VII makes a number of concluding comments.

[1] For example, the World Bank (WB), Economic Commission of Latin America and the Caribbean (ECLAC), United Nations (UN), the Inter-American Development Bank (IDB), the Organisation for Economic Co-operation and Development (OECD), and others.

[2] See the study of two regions of Peru (Tello, 2008).

II

Definitions of local economic development (LED)

The World Bank website states that: *"Local economic development (LED) offers local government, the private and not-for-profit sectors, and local communities the opportunity to work together to improve the local economy. It focuses on enhancing competitiveness, increasing sustainable growth, employment generation and ensuring that growth is inclusive. LED encompasses a range of disciplines including physical planning, economics and marketing. It also incorporates many local government and private sector functions including environmental planning, business development, infrastructure provision, real estate development and finance."*

In various contributions from ECLAC (Aghón, Alburquerque and Cortés, 2001; Finot, 2001) and IDB (Albuquerque, Llorens and Del Castillo, 2002; Llisteri, 2000), LED is defined as: *"the structural and growth process which, by making full use of local resources, leads to a continuous increase of the welfare of the people living in a local area or region within a country. The process includes three dimensions: economic (encompassing the means of production that allow local firms to make efficient use of local resources, generate scale economies and increase their productivity and market competitiveness); sociocultural (characterized by the social and economic network, in which local values and institutions support the LED process); and the administrative and political dimension (involving local initiatives that create an appropriate local and business environment to foster local economic development)."*

In the economics literature and from the industrialized-economy standpoint (Blair, 1995; Bartik, 1995; Bingham and Mier, 1993; and Malizia, 1985) LED is traditionally defined as changes that affect a local economy's capacity to *"increase economic growth, generate employment and create new wealth for local residents."* A modern definition is given by Blakely (2003) and Blakely and Bradshaw (2002), who state that the LED field is a combination of disciplines and an amalgamation of policies and practices; and that today LED scholarship is a small and growing industry in its own right. The LED concept is based on four factors: (i) indigenous resources and local control; (ii) new wealth formation; (iii) new capacity building, and (iv) resource expansion.

These definitions of LED share several aspects that tend not to be explicitly included in definitions of national economic development. The first is the geographic location of the LED process. Countries are usually divided, geographically, politically or administratively (see OECD, 2002) into different territorial levels or spatial units (such as states, regions, departments, provinces, districts, municipalities and so forth); and residents (economic, political and social agents) are identified with those territories. Greffe (2004) postulates at least three justifications for the local approach to the economic development process: one concerns the specific features of certain territories, which may affect the adequate functioning of spontaneous market mechanisms, or the policies formulated for an area without taking local features into account. Another involves the multidimensional nature of employment problems, which are usually presented as a mismatch between supply and demand. Thus, factors such as training, housing or mobility, health care, minimum-wage constraints and others can in fact only be identified and managed in a precise manner and close to the stakeholders involved, which means that initiatives must be planned, executed and coordinated at the local level. The last concerns the global-economy context of the countries, under which the local approach is justified, because it allows for greater synergy between the economic and social foundations of markets.

The second aspect of LED processes relates to the provision of public goods and services at the local level.[3] Governments use a variety of instruments to achieve the goals of efficient and equitable resource allocation in an economy, which entails providing public goods and services such as infrastructure (roads, bridges, etc.) and social services (education, health, etc.). Most of these "goods and services" are supplied locally, however, (Tiebout, 1956a) and mainly benefit the residents of the areas in which they are supplied. Thus, the difference between the public goods and services that affect residents in a country's territories

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[3] McGuire and others (1994), conceptualize local-development capacity in terms of three broad factors: citizen participation, community or local structure, and development instruments. The latter relate to local government policies and the supply of goods and services that support the LED process.

or spatial units and what the literature calls "local public goods and services" is another aspect that is not explicitly considered in definitions and theories of national economic development.

The third specific feature of LED (in contrast to NED) is its explicit consideration of the role and participation of local residents (economic, political and social agents and citizens) in the local development process. Firstly, local residents demand goods and services from government (at all levels), to support business activities and reduce income inequalities in local areas. Secondly, through the activities and participation of specific agents, together with alliances and partnerships among agents in local areas, they can also help increase the supply of public goods

and services, boost local economic growth and also influence economic policies at the local and national levels (OECD, 2007).

The fourth aspect that distinguishes LED from the NED is the former's multidisciplinary approach. To address the geographic-location or spatial dimension of the LED process, the key tools for analysing the LED process are drawn from the fields of regional, urban, rural and geographical economics. In contrast, the public-finance approach is used to analyse the provision of local public goods; and tools drawn from political economy, sociology and psychology are needed to understand the actions and interventions of agents in the LED process. The following sections deal with each of these four aspects in turn.

III

Location, geography and regional economic theories as inputs for LED theories

The starting point for understanding the relevance of economic theories of geographic and regional location for LED is regional economic-base theory borrowed from regional economics. Andrews (1953) defines the "economic base" as the set of activities in a "region" (defined as a local geographic area or a specific spatial unit) which "exports" goods and services to points outside its economic boundaries, or sells its goods and services to outsiders. Based on this definition, regional economic-base theory postulates that the "region's" economic growth is driven by growth in the "export activities" of the economic base (Sirkin, 1959, Tiebout, 1956b, and North, 1955).[4] In LED theories, the set of factors that determine location, activities and economic growth of the economic base of a region[5] come from the areas

of the economics of location and economic geography (both traditional and new). These factors include: external factors not localized in the "region", local resource endowments (human, natural and capital)

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[4] The economic base activities or *basic industries* of a "region" are the set of "export commodities or industries or staples". The non-base activities or *non-basic industries* of a "region" consist of "subsidiary industries" developed and/or derived from the economic-base activities, demand for which is determined locally by the residents of the "region" (North, 1955).

[5] Taking market demand, its geographic distribution, and local resource endowments as exogenous, location theories (Weber, 1957; Isard, 1956; von Thünen, 1826) and central place theories (Christaller, 1966) introduced transport costs and distance from markets as factors explaining the fixed and spatial distribution of the region's (base and non-base) activities. Marshall (1890) introduced

the concept of "external or spatial economies" associated with the proximity of economic actors within a given location. Such economies arise from three types of cost and market-location advantages: job creation and the capacity to absorb workers with specialized skills, who are attracted to local areas and form a supply pool of workers; creation of demand for (specialized and complementary) inputs which are profitable to produce, given the proximity of production markets; and the generation of technological spillovers via the exchange of information and production methods among firms located in the same spatial unit. Weber (1957) introduced the concept of "agglomeration economies" which arise from transaction cost savings stemming from the proximity of firms within a specific area; and "external economies of scale", also introduced by Marshall (1890), which are defined as the cost savings accruing to a firm because of the size or growth of output of the industry as a whole. Such economies contrast directly with internal scale economies, which are a source of increasing returns based on larger plant size. These external economies are essentially spatial externalities, which can generally be defined as economic side-effects of the proximity between economic actors. They can be negative or positive, static or dynamic, pecuniary or technological. The static variety is reversible, whereas dynamic externalities are associated with the technological progress, greater specialization, and division of labour that accompanies and/or drives growth and development (Young 1928). Pecuniary externalities are internalized thorough market mechanisms whereas technological ones are not, although they may be internalized through non-market mechanisms.

and physical infrastructure, together with factors such as distance from markets (where the economic base's export demand comes from); transport costs (which affect production features of the goods and services produced in the economic base and the spatial distribution of the production of those goods and services); spatial (or external) agglomerations; and external economies of scale.

In a series of papers (Fujita and Krugman, 1995, Fujita and Mori, 1997; Fujit, Krugman and Mori, 1999; and Stahl, 1987), the new economic geography theories put forward by Krugman (1991) and Fujita (1988) have introduced all these concepts in a formal way (using rational optimizing decisions by agents, interactions among agents, skilled labour and capital mobility in a general equilibrium framework), allowing for the endogenous location of manufacturing and agriculture activities and explaining the agglomeration of activities around cities and the economic growth of the regions. The agglomeration of consumer and producer activities in a given spatial unit is formally shown as the outcome of two forces: centripetal or push forces, and centrifugal, dispersion or expulsion forces. The first of these stems from spatial, agglomeration, and external scale economies and the creation and development of backward and forward linkages, or market-size effects. The second group of forces is generated by the immobility of factors such as land and workers (factor rewards decrease as the distance from the agglomerated activities increases), fierce competition, and pure external diseconomies (Krugman, 1999 and Fujita and Thisse, 1996).

The LED literature has formulated various mechanisms through which the agglomeration of economic (base and non-base) activities generates economic growth and development for the local region or spatial unit as a whole. The first is the income/employment-multiplier mechanism (Sirkin, 1959), whereby higher income and employment in economic-base activities will increase the demand for goods and labour in non-base activities. A second mechanism, drawing on "staples and vent-for-surplus models" (Findlay and Lundahl, 1994), operates through the backward and forward inter-sectoral linkages generated by the economic-base activities when there are idle resources in the region. Multi-sector and multi-regional growth models have been based on these two mechanisms of economic base LED models (Loveridge, 2004; Nijkamp, Rietveld and Snickars, 1987).

The third mechanism involves "external and agglomeration economies", as sources of the

centripetal and centrifugal forces of the agglomerated activities in a region. Growth and development poles (Perroux, 1950, 1955, and 1988) and product-cycle development theories (Vernon, 1966) formulated the basic ideas, which were then formally modelled by the new economic geography approach (Fujita and Thisse, 2003; Walz, 1996; Baldwin and Forslid, 2000, Black and Henderson, 1999; Martin, Gianmarco and Ottaviano, 1999 and 2001).

According to Perroux (1950), an economic space, conceptualized as a field of forces, consists of centres (or poles) from which centrifugal forces expel and to which centripetal forces attract. As a reason for such agglomeration, Perroux argued that dominant (leading) firms are comparatively efficient, and they can make effective use of innovations and thus expand their output by more than other firms. This effect would be propagated and perceived throughout society through a multiplier process. Hence, a polarization process is needed for the population at large to benefit. Perroux (1955) also postulated that economic growth does not occur everywhere at once, but manifests itself in points or "poles" of growth of varying intensities; and it spreads through different channels with variable final effects on the economy as a whole. Consequently, a growth pole is an "aggregation of propulsive industries" connected to the surrounding (or peripheral) environment. It is a "set with capacity to induce growth [defined as a lasting increase of a dimensional indicator] in another set". Perroux (1988) adds that the development pole is a "set with capacity to generate economic and social structures, whose effect is to increase the complexity of the whole and expand its multidimensional performance". Based on the dynamic stages of products or "product cycles" (Levitt, 1965),[6] and evoking the leading role of specific and efficient firms in the creation of the

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[6] Levitt (1965) distinguish four stages: (i) the stage of market development, or creation of a product before there is a proven demand for it and often before it has been fully tested technically in all respects. Sales volumes are low and progress slowly; (ii) the market-growth stage, when a product has survived its introduction, demand starts to pick up, and the size of the total market expands rapidly; this is the peak stage for any product; (iii) the market-maturity stage, when sales growth has started to slow and is approaching the point where the inevitable decline will begin. In the two latter stages, products that are considered economic-base activities generate demand in subsidiary industries or non-base activities, and are "exported" to markets outside the spatial units in which they are produced; and (iv) the market-decline phase, in which the product starts to lose consumer appeal and a downward slide in sales sets in. Vernon (1966) called this the standardization phase, and it starts at the product-maturity stage.

growth poles, Vernon (1966) argues that regions which are capable of producing at the market-development and growth stages of the product cycle grow more rapidly. The region's capacity to produce in those two stages depends, among other things, on the degree of technological innovation among the firms located in the region, the region's endowment of innovative firms and the income generated in the region.

These ideas have been formalized by the new economic geography (NEG) approach, in which the sources of agglomeration, the rate of technological innovation (associated with investment in R&D activities) and technological spillovers are modelled as the key mechanisms driving local economic growth. Furthermore, and as a result of the local growth models of NEG, regions are divided in two groups: central regions, which are the more developed; and peripheral regions which are less developed. Central regions produce goods included in the first three stages of a product cycle, while the peripheral regions produce at the standardized stage. These concepts of "centre and periphery" first appeared in the seminal work of Prebisch (1959).

A fourth and related mechanism shared by NEG models is the "circular and cumulative causation" mechanism generated by the "lock-in" effects of agglomeration (Fujita and Thisse, 1996; Arthur, 1989). Under this mechanism, the set of (usually differentiated final and/or intermediate) goods at the first two stages of the product cycle will be produced by innovative firms in locations where there is a relatively large and attractive market (measured the number of workers or consumers). But the market

will be relative large and attractive if a relatively large number of producers locate their production there. Thus, the concentration of the leading sector (usually manufacturing) in a given location is generated and reinforced through this circular and cumulative causation mechanism.[7] The initial activity (usually with increasing-returns technology) and its location, which generate this mechanism, stem from lock-in effects caused by accidental or historical conditions (or events).[8]

While local economic development depends on location factors that fuel development in the economic base and region through mechanisms of transmission between the economic base and non-base activities, local public goods and services and economic policies are also key ingredients in local development capacity.

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[7] A relatively large market is attractive for firms because of the potential demand that may exist for their goods (a relatively large number of consumers) and the availability of (particularly skilled) labour (many consumers also means many workers). Thus, firms will demand inputs and labour through backward linkages. Moreover, large market size results in lower prices and higher real wages, which may induce workers to migrate to locations where the leading sector is concentrated. Thus, firms will increase the supply and number of (differentiated) goods through forward linkages, and they will lower their prices in the locations where their goods are produced. According to Fujita and Thisse (1996), the backward and forward linkages of the circular cumulative causation mechanism turn increasing returns to scale at the firm level into increasing returns to scale for the region as a whole.

[8] Increasing-returns technology may lead to multiple equilibriums; with economic conditions and random events determining which equilibrium actually occurs.

IV

Local public goods, local government and LED policies

Several issues arise when local public goods and services (LPGs) are introduced into the analysis of the local economic development process, three of which are analysed here.[9] The first is the efficiency with which the central (federal) government provides LPGs. The second is the level of local government that can supply LPGs most efficiently. The third is the economic and social role of local government in the LED process.

On the first of these topics, the pioneering studies by Oates (1972) and Olson (1969) provided a starting point for the analysis of decentralization theory or fiscal federalism. Recent surveys of this strand of literature are contained in Oates (1999, 2005) and Bardhan (2002) among others. According to the Oates (1972) decentralization theorem, in the absence of heterogeneous consumer preferences, and if LPGs overflow the local jurisdictions in which they are supplied, the most efficient arrangement is for central government to provide a common level of public goods and services to all localities. In contrast, when preferences are heterogeneous and there are no spillovers across jurisdictions, local governments are more efficient in providing LPGs to their respective localities. In the first-generation theory of fiscal federalism, Oates (2005) envisioned a setting in which governments at different levels provide public goods, whose spatial patterns of benefits are encompassed by the geographical scope of their jurisdictions. This allocation of LPGs is called a "perfect mapping" or "fiscal equivalence" to use Mancur Olson's (1969) terminology.

Based upon (i) public-choice and political-economy studies focusing on political processes and the behavior of political agents, and (ii) the extensive literature on information problems, the modern theory of fiscal federalism (or second-generation fiscal theory) summarized by Oates (1999, 2005) analyses the workings of different political and fiscal institutions in an imperfect-information and control setting, focusing basically on the incentives that those institutions embody and the behaviour they induce from utility-maximizing participants. In this context, the first issue of whether to centralize or decentralize public activities is analysed from this new perspective; and the trade-offs between the inefficiencies under centralized provision of public services stemming from more uniform outputs that fail to reflect divergences in local tastes and conditions, versus the inefficiencies of local supply resulting from the failure to internalize inter-jurisdictional externalities, are analysed from a somewhat (but not altogether) different perspective.

The pioneering work of Tiebout (1956b) is the starting point for the second topic, which is closely related to the first one. Tiebout argues that government levels are directly related to the set of LPGs that governments supply within their jurisdictions. He showed that, under conditions of high household mobility, households can optimally (and efficiently) choose the jurisdiction of residence that offers the LPG package that best suits their preferences. In contrast to this non-spatial allocation theory of LPGs, the Hochman, Pines and Thysse (1995) geographic or locational approach to the provision of LPGs postulates that their consumption entails transport costs. These costs increase with the distance between residential locations and the public facilities where the goods and services in question are available. Consequently, decentralization does not have to be based on the types of LPGs supplied by local governments, but could be based on territories instead. It has been shown that optimal provision of LPGs can be decentralized only through metropolitan governments supplying the whole range of LPGs over one or more appropriate territory.[10]

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[9] A fourth issue, which emerged in the 1990s and is partially discussed in this paper, is local governance, for which recent surveys can be found in Liou (2007) and Shah and Shah (2006). This issue concerns the various types of institutional framework that best enable governments to fulfil their economic role. It deals primarily with the failings of government institutions when intervening in markets. A fifth and related issue, not discussed here, is decentralization (in other words the transfer of specific functions from central government to local governments). Surveys on this topic are presented by Rondinelli and Cheema (1983), Litvack, Ahmad and Bird(1999), and Bardhan (2002) among others.

[10] The geographic jurisdiction of the metropolitan local government is a territory where the user charge collected from its residents, plus the corresponding aggregate land rent, is just equal to the

The third issue is what most LED practitioners have concentrated on. The starting point is the theory of the economic role of the government as formulated by Musgrave (1959) and Samuelson (1954). According these authors, efficiency, equity and (macroeconomic) stability are the three basic market principles on which the economic role of the government needs to be based. Consequently, market failures or distortions, such as the existence of public and merit goods, externalities and natural monopolies, have traditionally been viewed as market inefficiencies to be corrected by government. Income-distribution inequalities arising from the market allocation of resources is another area that requires government intervention in the economy. Consequently, market distortions and inequalities arising from the jurisdictional distribution of resources may be territorial features of the market; and central (or federal) and local governments share the role of intervening in the economy at the national and local level; while the goal of macroeconomic stability is left as an exclusive preserve of central government.[11]

Recently, Shah and Shah (2006) have summarized the evolving economic role and responsibilities of local governments since the Musgrave and Samuelson contributions. Using the traditional fiscal federalism approach, which is based on the market-failure and LPG- provision approach to the role of government, they classify the different expenditures, public goods and service provision and taxation responsibilities of government and assign them to three levels: central (or federal), regional (states or provinces) and local (municipalities and metropolitan areas).

Under the same market-failure and LPG-provision basis for the role of government, the new public management approach focuses on what local governments should do and how they should do it better. From this standpoint, (central and local) government is viewed as the "agent", and the population represents the "principal"; so its responsibility is to serve the public interest and create public value (defined by Moore (1996) and measured as improvements in social outcomes or quality of life). This approach also suggests a change in the way local government should fulfill its responsibility: from the top-down approach of fiscal federalism to a bottom-up approach in which

local governments behave as managers serving the people living in their local jurisdictions (Shah, 2005 and Caulfield 2003).

In contrast to these two perspectives, public choice theory and the new institutional economics focus on government failings rather than market failures. These approaches propose different ways of organizing governance to avoid the inefficiencies caused by government failures. The public-choice literature endorses the self-interest doctrine of government and argues that the various stakeholders involved in policy formulation and implementation can be expected to use opportunities and resources to advance their self-interest. Consequently, for local governments to serve the people's interests, they need full local taxing and spending autonomy, and they must be subject to competition within and beyond government. In the absence of these prerequisites, local governments are likely to be inefficient and unresponsive to citizen preferences (Boyne 1998). In contrast, the new institutional economics postulates various orders of government (as agents) to serve the interests of citizens (as principals). The jurisdictional design should ensure that these agents serve the public interest while minimizing transaction costs for the principals (Williamson, 1985; Horn, 1997 and Shah, 2005).

Similar to the previous two approaches, the network form of governance is also concerned with the institutional arrangements of government, while focusing on both market and government failures. It provides specific guidance in dealing with government failures in a hierarchical form of public governance, and local government involvement in a partnership with multiple organizations. Under this perspective, a network mechanism of governance has been advanced for local governments, based on trust, loyalty and reciprocity between partners with no formal institutional safeguards. Networks formed on the basis of shared interests (interest-based networks) can provide a stable form of governance provided their membership is limited to partners that can make significant resource contributions and there is a balance of powers between members. Local government may thus have an opportunity to serve as a catalyst in facilitating the roles of both interest-based and hope-based networks to improve social outcomes for local residents (Dollery and Wallis 2001).

A more proactive approach to the role of the local government is formulated in the LED literature summarized by Liou (2007), Bartik (1995 and 2003),

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cost of supplying all the LPGs provided by the metropolitan government.

[11] Watt (2006) and King (1984), among others, argue that stabilization and redistribution (usually through transfers) are the main roles of central government, whereas the local-government role is to allocate local public goods efficiently.

Bachtler and Yuill (2001), Blair (1999) and Blackely and Bradshaw (2002), among others. In addition to the traditional and modern theories of the economic role and responsibilities of local government summarized in Shah and Shah (2006), LED practitioners (from the United States and Europe) propose another role for local government, namely to implement policies that foster local economic development. The rational for this role is based on specific aspects of theoretical models of LED, which may be related to, or are claimed to be consistent with, the efficiency and equity roles of the traditional and modern theories of local government.

According to Bartik (2003), local-government economic-development policy is defined as the special activities undertaken by local government to promote economic development. Activities referred to as "economic development programmes" fall into two categories: (i) providing incentives and customized assistance for individual businesses from which greater economic development benefits are expected; and (ii) strategic initiatives to alter more general tax, spending, and government regulatory policies to promote local economic development.

Blackely and Bradshaw (1999), Blair (1999) and Bachtler and Yuill (2001) distinguish up to three "waves" of LED programmes and policies implemented by LED practitioners in developed countries: the first wave, before the 1980s and based on location theories of LED, dominated by (incentive and subsidy) programmes designed specifically to attract footloose firms from old industrial areas into growing regions; the second wave, during the 1980s, based upon traditional and neoclassical regional development theories, dominated by local growth programmes (such as creating new businesses, increasing investment capital, developing incubators, and providing technical assistance); and the third wave, from the 1990s onwards, based on LED competitiveness and cluster theories, dominated by policies aimed at providing an appropriate regional business environment, emphasizing public-private partnership, collaboration and coordination.

From the institutional standpoint of local governance models, however, local governments are not the "principals" of the LED process; instead, the citizens' residents in local areas, in their diversity of composition and roles, are the "principals", and their active participation is also a distinctive feature of LED theories. The next section considers the role and participation of the citizen or private agent in the local economic development process.

V

The role and participation of local private agents in the LED process

Various groups of citizens or private agents (entrepreneurs, women, groups representing social capital, etc.) play multiple roles in the LED literature,[12] and they affect the local development process through a variety of mechanisms. Entrepreneurship (Bates, 1993 and Malecki, 1994), "intrapreneurship"(Pinchot III, 1985) or entrepreneurship capital (Audretsch and Keilbach, 2004a) are the terms normally used in the LED literature to identify one of the oldest mechanisms used by entrepreneurs and managers to generate

knowledge creation and innovation (Schumpeter, 1934) leading to regional/local economic growth (Audretsch and Keilbach, 2007, 2005, 2004b; and Lawton, Glasson and Chadwick, 2005). Innovation, however, is not the only business activity that affects the LED process. An OECD (2003) report summarizes activities and interactions among entrepreneurs in local areas that affect the area's economic development and growth process. Entrepreneurs are sources of investment, savings, job creation, networks and agent-coordination, which may enhance the development capacity of the local areas in question.

A second way a group of citizens can affect the LED process is through social capital (Trigilia, 2001; Putnam, 1993). Although social capital (defined as

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[12] For example: (i) governors (such as owner-authorizers, voters, taxpayers, community members); (ii) activist-producers (such as providers of services, co-producers, self-helpers obliging others to act); and (iii) consumers (clients and beneficiaries) (Moore 1996).

the level of interpersonal trust, civic engagement and organizational capability prevailing in a community or among group of citizens) is a feature of specific local geographic areas, the concept was originally conceived as having economic-development consequences at the national level (Woolcock and Narayan, 2000; and Zabojnik and Francois, 2005).

Moreover, as pointed out by Durlauf (2002), social capital also has an impact on issues relating to political participation (DiPasquale and Glaeser, 1999), development traps (Woolcock, 1998), human-capital formation (Coleman, 1988) and the efficiency of the judicial system (La Porta and others, 1997). In the first case, citizens' investment in social capital might include membership of a social organization leading to better coordination and political actions within a community. In the second case, a lack of trust among citizens (or social capital) in a community could contribute to the persistence of development traps. In the third case, the trust and coordination dimensions of social capital may improve information channels, communications skills, and knowledge creation, transfer and flows, leading to human capital formation. In the last case, the efficiency of the judicial system may affect the level of trust among people and thereby encourage or discourage the formation of social capital.

Women are another group of citizens whose participation has recently been discussed in the LED literature (Blumenberg, 1998). Beyond the gender-inequality and social-exclusion issues in the development process (Weinberger and Jütting, 2001; Blumenberg, 1998; and Elson, 1998), gender issues and women's role in the family also have been linked to other aspects of social development (as defined in Mokate, 2004), such as: poverty; fertility rates; human-capital formation; household nutrition; infant, child and maternal mortality rates (Elson, 1998). In terms of women's role in economic development and growth at the local level, the LED literature emphasizes three roles: as entrepreneurs, as innovators (particularly in retail and service industries), and in forming social capital (Forsyth, 2000; and Molyneux, 2002).

Another way citizen participation can influence the LED process is through local "partnerships" (or cooperation, collaboration, coordination or association) between two or more group of agents (including institutions, community or private organizations, and government entities) sharing common development objectives that are location-based and operate within spatially defined social, cultural, economic and political relationships. Local partnerships are territorial entities by definition (OECD, 2007). Aside from issues relating to the definitions and forms of partnerships (such as vertical supplier or purchaser associations, horizontal and lateral governmental partnerships, and private and public partnerships, as listed in Camarero, Hernández and San Martín (2008), it is through their social-capital and local-governance features that partnerships can influence local economic development process (OECD, 2007).

The "trust" element in social capital may improve knowledge flows among the members of local partnerships (Jones, Kashlak and Jones, 2004) and overcome the market failures arising from market activities based on the partnerships' development objectives and programmes (for the supply of public infrastructure); and the local-governance feature may make it possible to overcome government failures arising from the process of achieving development objectives (by providing stability in a turbulent environment caused by economic, social and political changes; and by improving market efficiency through adequate control and allocation of resources and responsibilities among partnership participants, as suggested in Walsh and Meldon (2004) and OECD (2001)).

Active participation by these and many other groups of agents and entities —such as the economic or interest groups analysed by Gray and Lowery (1988); and the local developers analysed by Laukkanen and Niittykangas (2003)— is considered by LED practitioners as a part of any planning strategy to foster local economic development (Walsh and Meldon, 2004).

VI

The multi-disciplinary approach
of modern LED theories

The fourth distinctive feature of LED theories is their multidisciplinary approach to the LED process. As shown in previous sections, LED theories draw on a variety of disciplines (such as spatial and location theories, public finance theory and the theory of governance, among others). Nonetheless, these are considered separately to emphasize different aspects of the local development dynamic. Until the 1980s there was a consensus among LED practitioners in terms of the various factors taken into account in the LED process (Thompson, 1968). In the early 1990s, however, a set of LED theories emerged with a multi-disciplinary, multi-dimensional or multi-factorial approach to the LED process within a unified framework. Those theories have been associated with the third wave of LED policies and local government programmes, and they highlight simultaneous interactions between various factors to achieve local development goals. Two of the most widely studied "modern" theories in the LED literature are the regional/local competitiveness or "cluster" approach developed by Porter (1990) (surveyed, by Budd and Hirmis, 2004 among others), and the cluster-development approach (Rainess, 2003; Rocha, 2004; Enright, 1996).

Leaving aside the problems involved in defining the concept of competitiveness (Lall, 2001) and clusters (Martin and Sunley, 2003), Porter's approach to LED is based on his competitiveness diamond which contains four sources of the competitive or productivity advantages of national or regional economies. These are: demand conditions; factor (or input) conditions; firm strategy, structure and rivalry; and related and supporting industries, According to Porter (2000), "demand conditions at home have much to do with whether firms can and will move from imitative, low-quality products and services to competing on differentiation. In low-productivity economies, the focus is heavily on foreign markets. Advancement requires the development of more demanding local markets. The presence or emergence of sophisticated and demanding home customers presses firms to improve and provides insights into existing and future needs that are hard to gain in foreign markets. Local demand also can reveal segments of the market where firms can differentiate themselves. In a global economy, the quality of local demand matters far more than does its size."

"Factor inputs", argues Porter (2000), "range from tangible assets such as physical infrastructure, to information, the legal system, and university research institutes that all firms draw on in competition. To increase productivity, factor inputs must improve in efficiency, quality, and (ultimately) specialization to particular cluster areas. Specialized factors, especially those integral to innovation and upgrading (a specialized university research institute), not only are necessary to attain high levels of productivity but also tend to be less tradable or available from elsewhere."

On the other hand, the context for firm strategy and rivalry concerns the rules, incentives, and norms governing the type and intensity of local rivalry. Low-productivity economies with are characterized by little local rivalry. Most competition, if present at all, comes from imports; local rivalry, if any, involves imitation. Price is the sole competition variable, and firms hold down wages to compete in local and foreign markets. Competition entails minimal investment.

Moving to an advanced economy requires the development of vigorous local rivalry. Rivalry must shift from low wages to low total cost, and this requires upgrading the efficiency of manufacturing and service delivery. Ultimately, rivalry must also evolve from cost alone to include differentiation. Competition must shift from imitation to innovation and from low investment to high investment —not only in physical assets but also in intangibles (skills and technology, for example). Clusters play a key role in these transitions.

While the nature of rivalry in a given location is heavily influenced by many aspects of the business environment (factor availability, local demand conditions), the investment climate and competition policies set the context. Issues such as macroeconomic and political stability, the tax system, labour-market policies affecting the incentives for workforce development, and intellectual property rules and their enforcement, affect the willingness of companies to invest in upgrading capital equipment, skills and

technology. Antitrust policy; government ownership and licensing rules; and policies toward trade, foreign investment, and corruption play a vital role in defining the intensity of local rivalry.

Lastly, related and supporting industries refer to the local presence or absence of suppliers of materials, components and machinery and equipment, together with related industries that support enterprise productivity and competitiveness (Porter, 1998). The level and rate of growth of productivity in a particular location, according to Porter (1998), depend less on what industries and firms compete on and more on how they compete. The sources of competition define the factors that influence how firms compete, thus affecting productivity and the LED process in local areas.

A structural variant of Porter's approach is the systemic competitiveness approach outlined in Meyer-Stamer, Altenburg and Hillebrand (1998) and Meyer-Stamer (2005), in which the concept of systemic competitiveness seeks to capture the political and economic determinants of successful industrial development. It refers to a pattern in which State and social actors deliberately create the conditions for successful industrial development. The concept distinguishes four levels: the "micro-level" of the firm and inter-firm networks; the "meso-level" of specific policies and institutions; the "macro-level" of generic economic conditions; and the "meta-level" of "qualitative" variables such as sociocultural structures, the basic economic order and orientation, and the capacity of social actors to formulate strategies.

At the local level, the vehicle through which specific geographic areas may become more competitive and achieve systemic competitiveness for successful economic and industrial development is a "geographic cluster" (Porter, 1996 and 1998). This is defined as a "geographically proximate group of interconnected companies and associated institutions in a particular field, linked by commonalities and complementarities. The geographic scope of clusters ranges from a region, a state, or even a single city, to span nearby or neighbouring countries" (Porter, 2000).

In contrast to the competitiveness approach to LED, the cluster approach focuses on the way specific features of clusters affect the LED process, which are intrinsically associated with the "economies" and properties generated in a geographic location. Under the former approach, Porter (1990) and Meyer-Stammer, Altenburg and Hillebrand (1998) claim that competitiveness (and its cluster vehicle)

can be also applied at the national level, and is not necessarily linked to the development properties of specific geographic areas.[13] In addition to the factors that determine competitiveness locally, the cluster approach focuses on the following LED features of clusters localized in specific geographic areas: linkages and interdependency among firms and activities within a given space (Feser, 1998b); externalities (including technological spillovers) and agglomeration economies arising from location (Feser, 1998a); the formation of non-market social networks among agents within the geographic cluster (Jones, Hesterly and Borgatti, 1997; Powell, 1990); the innovation environment (Audretsch, 1998; Audretsch and Feldman, 1996); and path-dependency and lock-in effects (Kenney and von Burg, 1999; and Antonelli, 2000).

Location-factor and cluster-development features have been also associated with the emerging literature on (national and regional) innovation systems, learning and knowledge-based economies (Lundvall and Johnson, 1994; Morosini, 2004; Maskell, 2001 and Cooke, 2001). In a knowledge-based economy —defined by OECD (1995) as an economy which is directly based on the production, distribution and use of knowledge and information— location and cluster features can serve as vehicles for knowledge creation and economic growth in local areas. In this regard, Cappellin (2003) postulates that the knowledge-creation process is interactive and combinatorial; and that closer geographical proximity and greater cognitive proximity makes it easier to combine complementary pieces of knowledge and facilitates interaction between various complementary actors. Maskell (2001) adds that the cluster is considered the territorial configuration most likely to enhance learning processes. Lastly, Leydesdorff (2006) states that the "dynamic of a knowledge-based economy has important consequences for the function of regions. The locales may serve as the incubators where production, innovation, and diffusion processes are closely coupled. The density of the local interactions increases the chances for "lock-in" and therefore the (co-)shaping of trajectories within the system. The density of the interactions within clusters and regions determines this capacity. Therefore, one can expect metropolitan regions to hold an advantageous position in the knowledge-based economy."

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[13] Enright (1998), Raines (2001) and Camagni (2002) summarize the geographic or territorial aspect of the competitiveness concept.

VII

Conclusions

The decentralization process pursued by developing countries over the last three decades has generated a demand for conceptual frameworks to define the appropriate objectives and roles of private and public agents in LED processes. Unlike the situation in the industrialized world, LED is practically non-existent as an academic discipline in most developing countries. This discipline provides four theoretical approaches to the analysis of the LED process in developing economies, going far beyond the economic fundamentals, institutions and the market-failure approach of national economic development theories. Thus, location factors, local public goods, active participation by diverse private agents, and the multidisciplinary framework of the LED theories can help elucidate the necessary objectives and roles of agents in decentralization and LED processes in developing countries.

(Original: English)

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