



# CONTEMPORARY DRIVERS OF LOCAL DEVELOPMENT

Editor  
**Péter Futó**



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## **Contemporary Drivers of Local Development**

**Editor:**  
Péter Futó

**June, 2019**



# Contemporary Drivers of Local Development

PÉTER FUTÓ

**Abstract** This book was born from the joint effort of the professors and researchers of a university course on Comparative Local Development. It contains 25 articles on social, economic and institutional factors of Local Development, highlighting drivers of the development of settlements and regions in urban and rural spaces. The book has been organised according to the genre of the contributions as follows.

- Conceptual framework, theory and measurement. This chapter contains articles designing conceptual frameworks, identifying theories, setting up models, measuring statistical indicators and using these instruments for investigating spatial economic processes.
- Legal and institutional arrangement. The added value of the articles in this chapter lies predominantly in their contribution to understanding the legal and institutional arrangements of implementing local democracy, granting equal opportunities to minorities, and providing local services by public and private stakeholders.
- Sectoral and spatial analyses. The papers of this chapter are meso-economic empirical studies investigating the development trajectories of certain geographic areas and highlighting the development patterns of certain sectoral activities that generate urban and rural change.
- Innovative policy interventions, plans and initiatives. The papers in this chapter describe innovative combinations of policy areas and policy instruments that have been tested in real life situations of aid policy.

Evaluations of projects and programmes. The papers in this chapter formulate evaluation questions, apply evaluation criteria, form opinions about the evaluated development programmes, and identify the lessons learnt.

**Keywords:** • spatial economic analysis • legal and institutional • arrangement of local development • evaluation and innovation of local development • evidence based policy making

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## **Introduction and Lessons to be Learnt from this Book**



## On the Governance, Investigation and Education of Local Development

PÉTER FUTÓ

**Abstract** The article serves as the introductory editorial chapter of the book "Contemporary Drivers of Local Development". The book was born from the joint effort of the professors and researchers of a university course on Comparative Local Development, also called "Master CoDe". This Master Course and its predecessors have been offered for the last 15 years jointly by four European universities. The first part of the article elaborates on the paradigm of Local Development, which is a fruitful concept of development study integrating a wide range of research, education and policy making activities. In particular, research on Local Development facilitates evidence-based policy making on the local and regional level. Education of Local Development is based not only on lessons learnt from case studies of positive development, but also on the analysis of local stagnation and decay as well. The conceptual framework of Local Development differentiates clearly between (a) local changes attributed to policy measures on the one hand, and (b) local changes driven by spontaneous forces of markets, the society and of the environment. The collection of papers in the referred volume can be interpreted as a consultative, „bottom-up” definition of what the concept of Local Development means for the collective of those professors and researchers who have actively participated in this course of development education, that has been organised exactly around this very concept. The second part of the article describes the structure of the book and offers short summaries of every article published in it.

**Keywords:** • local development • local stagnation • local decay • development education • evidence based policy making

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## 1 Local development: a fruitful paradigm

This book was born from the joint efforts of the professors and researchers participating in a university course on comparative local development, also called “Master CoDe”.<sup>1</sup> This master’s course and its predecessors have been offered for the last 15 years through the collaborative efforts of four European universities. During the time of its existence, the course has involved the work of more than 50 professors and more than 300 students from at least 40 developing, emerging and developed countries. The former students of this course have found work at various levels of national, regional and local governments and in prestigious international organizations. Many of them have made their careers in NGOs, academic and research organizations, or are working as independent consultants and development practitioners.

International development has an inherently interdisciplinary nature, therefore any curriculum that covers this subject must find the delicate balance between covering a wide range of interdependent but relevant subjects on the one hand, and identifying some points of focus and accepting some limitations on its scope on the other.

The founders of the master’s course have chosen local development as an umbrella paradigm for integrating curricula, lectures, exercises and internships into a meaningful, coherent multi-country, multicultural activity. This paradigm<sup>2</sup> has proven to be very fruitful, as documented by the research papers that have been published and presented by the professors who teach on the master’s course, but also by the dissertations that have been prepared by the students of the course which cover an astonishing variety of relevant issues in their home countries.

While local development as a phenomenon has been eternally present throughout the course of human history, local development as an applied scientific discipline is relatively young. The founders of the CoDe Master’s Course have deliberately embraced a rather flexible interpretation of this term which has allowed for a wide margin of overlap with other associated, preexisting incumbent disciplines. In this special case, the lack of an exact definition arose from an active choice to incorporate contributions from several relevant and related scientific disciplines, and also from a wide range of policy areas in which the related findings can be applied. The framework of this research and education activity was defined using only a few principles, as follows.

- *Governance.* Local development as an area of applied policy research focuses on governance issues that aim at strengthening economic prosperity, social stability, and environmental sustainability at the local and regional level.
- *Investigation.* Local development as a discipline involving social, economic and institutional research aims at understanding, explaining, and highlighting the factors that lead to the development of settlements, regions, and urban and rural spaces. The aim of local development research is thus to facilitate evidence-based policy making on the local and regional level by creating the conceptual framework for the latter,



by identifying suitable theoretical explanations, and by collecting the necessary empirical evidence.

- *Education.* Local development as a field of higher education conveys the necessary knowledge to students who intend to become development practitioners at local and regional levels.

The above definitions can be further refined (a) by extending the scope of the term "local development," and (b) by differentiating between policy-induced and spontaneous mechanisms of development. Let us investigate two hypotheses which are conjectures closely related to the very concept of local development.

- The first hypothesis is that it would be more fruitful and more practical to extend the scope of the term by defining a somewhat wider paradigm which could be called "Local Change". This would incorporate not only local development, but local stagnation and decay as well. Case studies of local stagnation and decay abound, and are frequently more spectacular and deliver more lessons than local success stories of development. In such an extended conceptual framework, there would be a clearly defined, non-overlapping and complete set of so-called "drivers" that have been identified to facilitate local development, and it would be the lack of some of these very same drivers (or a poor combination of them) that exerts a negative effect on the attractiveness of a locality, and ultimately leads to local stagnation and decay. Thus, by using the umbrella term "Local Change," development (and its negation) could be investigated through a unified and coherent conceptual framework.
- The second hypothesis relates to the identity of the agent(s) that drive local development. Accordingly, it would be more logical and more productive to use a conceptualization of local development that clearly differentiates between (a) changes attributed to policy measures, and (b) changes due to spontaneous market forces societal pressures and environmental challenges.<sup>3</sup> Public policy interventions include certain instruments such as regulations, subsidies and services that are packaged into projects, while spontaneous changes can be conceived of as being driven by a combination of (a) autonomous market forces, such as supply and demand, (b) social pressures, such as aging and migration, and, (c) environmental processes such as erosion and climate change.

Worthy of further investigation is whether the application of the above conceptual framework could eventually lead to better governance, to a deeper understanding of development forces, and to more comprehensive university curricula.

The call for papers for this book was disseminated among the professors and researchers of the master's course in the summer of 2017. The contributions can be regarded as a representative sample of local-development-related research papers and the associated disciplines. This volume can thus be interpreted as a consultative, "bottom-up" definition of what the concept of local development means to a collective of professors and researchers who actively participated in a course of development education which was organized exactly around this very concept.

It would have been overly ambitious to create a predetermined structure for this volume based on substantive categories (e.g. sectors, policy areas, or countries). Such an approach may be more appropriate for a handbook or for an analogous, all-encompassing, encyclopaedic effort. However, it would not have been possible to classify articles into a completely exhaustive, non-overlapping system of categories of local development: the subject is just too colourful for that.

For the above reasons, the structure of this book has been organized according to the *genre* of the contributions. The categories of this classification are reflected in the chapter titles of this volume:

- Conceptual framework, theory and measurement;
- Analyses of legal and institutional arrangements;
- Sectoral and spatial analysis;
- Innovative policy interventions, plans and initiatives;
- Evaluation of projects and programs

Each of the *genres* identified in the above classification represents typical, widely used approaches to tackling local-development-related problems. All of these genres have been frequently used by researchers, consultants, educators and students of this subject. In what follows, we apply the above-defined structure to present an overview of the publications in this volume.

## 2 Conceptual framework, theory and measurement

As local development is an applied science, it relies heavily on the terms, models and empirical strategies of other disciplines, such as Economic Geography, Sociology, Political Science and Regional Science. The analysis of local development – as is also the case in other disciplines of social inquiry – starts with the selection of the proper terms, hypotheses, and theories. Following some efforts at measurement, the thus-collected empirical material is incorporated into a conceptual model which can be of a mathematical-statistical nature or, in the case of qualitative research, a qualitative model (for example, which compares case studies). Subsequently, the results of the above reasoning are used to test the validity of the selected hypotheses and the applicability of the theories within the scope of the particular area of research (King *et al.* 1994).

The following articles are good examples of the design of conceptual frameworks, identification of theories for structuring models, the measurement of statistical indicators, and the use of these instruments to investigate spatial economic processes. The added value of the articles in this chapter lies predominantly in their contribution to the theoretical underpinnings and methodological tools of local development.

- Joachim Möller's article, "*Theories in Regional Economics in the Light of Local Development*," is a short introduction to the principles of Regional Economics. It

demonstrates some basic concepts and models for investigating the spatial aspects of economic phenomena such as productive activities, co-operation, exchange, labour migration and per-capita income by highlighting the impact of population density and distance. The author offers an overview of contemporary literature about the advantages and disadvantages of agglomerations and the market potential of locations. The quantitative part of the article demonstrates the gravity model as applied in the regional context. This is a distance-sensitive regression analysis based on registered data about either transport streams or commuting data. The model is frequently used for measuring the economic importance of locations, both at the sending and the receiving end of these resources. The gravity model can be refined and extended by taking into consideration not only the sending and the receiving location, but also the attracting power of the so-called "intervening opportunities"; i.e. the market potential of locations along the route.

- *Peter Haller and Joachim Möller's* article, "*Infrastructure and Local Economic Development*," discusses various ways of assessing the impact of investments in infrastructure on GDP and on future regional and local economic development. Infrastructure is generally defined by its constituents, such as water and power supply, communication networks, road and rail. The analysis investigates various ways of measuring the effects of proximity to main transport and communication axes on the economic growth of cities, suburbs and peripheral regions. The paper offers an overview of current findings in this field. A case study from Germany puts the literature into perspective: the impact of transport infrastructure on regional labour market development is investigated. For this purpose, the long-term effects of the autobahn (motorway) network on regional wages, local employment structure and efficiency are assessed by quantitatively analysing geo-spatial data.
- The paper by *Wolfgang Dauth*, "*Measuring regional economic dynamics*," explains some widely used statistical instruments for modelling the interrelationship between (a) national and, (b) regional growth of (1) regions, and (2) industries (sectors). The article explains the uses and limitations of the "shift-share" model as a predictive tool. Subsequently, a calculation exercise illustrates the use of this model. A database of employment data relating to the regions and industries of Germany is analysed at a very deep level of temporal, spatial and sectoral detail, whereby employment data extending to 20 years for the 402 administrative districts of Germany are disaggregated into 422 categories of economic activities. The paper ends with an interpretation of results, whereby the development trajectories of four case-study settlements are explained.
- The study of *Márta Kiss and Katalin Rácz* "*Factors and Policy Measures Influencing Local Economic Development: An Overview of the Conceptual Framework*" shows the considerations and dilemmas that arise when attempting to identify the driving forces that influence local economic development. The authors offer a wide overview of international professional publications devoted to

analogous tasks, and recommend a hierarchical classification of factors, the applicability of which is tested by analysing their own empirical observations in Hungary. Subsequently, the role of specific leading development factors are discussed, such as local endowments, social capital (interpreted as the cohesiveness of the local collective), institutional behaviour, market-based economic processes and the policy measures of the central government. The article also identifies major public, private and non-profit stakeholders.

### 3 Legal and institutional arrangements

According to the influential theory of new institutional economics, economic change is profoundly influenced by legal norms and rules, and by their enforcing organizations (North 2016). In central and local public administrations, regulations shape modes of governance, hierarchical structures, organizational arrangements and enforcement mechanisms associated with ownership, while the role of legal provisions in market transactions are crucial in determining the strength of commitments of exchange, in establishing contractual safeguards, and in shaping bargaining strength. History has shown that political and institutional choices contribute significantly to national and local changes and can be decisive in terms of whether an area will develop, stagnate or decay (Acemoglu and Robinson 2012). It has been recognized that the quality of regulations and the efficiency of the enforcing institutions have a direct effect on development. In international organizations, the assessment of the impacts of regulations on national, sectoral and local development has evolved into a routine activity (OECD 2009).

The following articles are good examples of the analysis of the regulatory environment of local development, with special respect to highlighting the impact mechanisms of various provisions. The added value of the articles in this chapter lies predominantly in their contribution to understanding (and reforming) the legal and institutional arrangements of implementing local democracy, granting equal opportunities to minorities, and the provision of local services by public and private stakeholders. Some of the publications apply a comparative method, which enables the authors to make generalizable conclusions.

- The paper by *Simona Kukovič and Miro Haček*, “*Comparative Local Governments In Europe*” starts with a thorough and logical overview of various typologies of local governments. The typologies taken into consideration are based on the representative features, democratic guarantees, structures and tasks of European local government arrangements, as well as their relations with regional and national levels of authority. The authors have elaborated their own typology, the “inclusive model,” which covers not only the types of local governments institutionalized in traditional European democracies, but also those of the new democracies of Central and Eastern Europe. This typology enables the reader to distinguish between three models of local government: the technocratic, the bureaucratic, and the

transformational model. The findings can readily be used in comparative research of local authorities in different national settings.

- The paper by *Simone Penasa*, “*The protection and promotion of linguistic minorities - The Italian Law of Diversity at the local level*,” first outlines a general conceptual and legal framework for the investigated policy area. The author describes and evaluates the legal tools and constitutional principles that have been elaborated and enforced by authorities at national and international levels. The subsequent case study focuses on the legal arrangement for protecting and promoting linguistic diversity in Italy. Special attention is paid to Italian Framework Law 482/99, which, as an application of the Constitution, recognizes twelve minority languages and provides for their protection in that country. Finally, the paper focuses on the role of local communities in effectively implementing the international and constitutional principles aimed at protecting and promoting linguistic minorities.
- The essay of *Matteo Ferrari*, “*The Role of Contracts, Standards and Certification in Protecting Fundamental Rights*,” deals with the role of privately elaborated rules in economic transactions. The paper focuses on rules agreed and implemented by private parties in order to guarantee and protect the fundamental rights of exporters, importers, suppliers, buyers, wholesale and retail traders and consumers participating in international supply chains. Recourse to standards and certification can be interpreted as a way of creating uniformity in protecting the fundamental rights of economic players, including consumers, whereby the specific requirements are agreed by professional bodies of private parties. The contract is an additional legal mechanism designed to make standards and certification binding for such actors. The author demonstrates the important role of these privately conceived legal instruments in rural development, human rights, safety at work, environment protection, and food safety by elaborating and comparing three case studies. The case studies explain various mechanisms of private self-regulation in the supply chain of the coffee industry: they describe standards and certification systems that help implement important norms and principles, thereby facilitating network-building among various stakeholders in the sector. Compliance with these norms is enforced by private contracts, thus facilitating co-operation between multinationals, their suppliers, the retailers of the final products and consumers.
- The two papers from *Don Elliott*, “*Environmental Protection and Sustainable Local Development in the USA*,” and “*Land Use Planning and Zoning as Key Tools in Sustainable Local Development in the USA*,” describe the division of labour and authority between various levels of government in governing the respective policy areas. The U.S. legal system includes very little federal regulation over land use – except for some general provisions on water, air, and endangered species and the application of Environmental Impact Assessment for projects that use federal government money. Most cities and counties are given substantial authority to

regulate the division, development, and redevelopment of land as they see fit – subject only to the requirement for constitutional protection of property rights and fair procedures. However, local governments must take into consideration global economic competition, the pressure for efficient public administration, and the desire of citizens for more effective participation. The article identifies some of the best practices of cities aimed at enhancing attractiveness and economic growth. The recommended measures are meant to develop public transit, housing, tourism-related facilities, to encourage local art and cultural activity, small business development, regional co-operation, the clean-up of polluted properties and the training of a workforce suited to the available job openings. Case studies of the metropolitan areas of Denver, Colorado and New York demonstrate the innovative and collaborative practices of local governments that result in environmentally and economically sustainable local development.

- *István Tózsza's* article “*A model of centralizing local government finances*” explains how the Hungarian Government after 2010 bailed out indebted local governments, and which other measures accompanied the financial reforms. In contrast to international trends of increasing local autonomy and shifting responsibility for expenditures and revenues to lower levels of government, the government of Hungary implemented a centralizing reform of the local government system of the country. The reform included the reduction of local autonomy in many respects by centralizing the governance, administration and public infrastructure of a wide range of public services, partly into the central government and partly into the seven administrative regions of Hungary. Significant steps toward centralization were made in the administration of public healthcare, education, environmental protection, unemployment policy, and local finances. Corresponding measures were also taken to reform local elections and local administration. The article describes the legal techniques involved in the above-described reform of responsibilities and finances. In particular, the formerly normative financing of the local governments was replaced by task-based financial support from the central government. This means that instead of using population size as the basis for financing local public service tasks, the financing regime now takes into consideration the amount of local tax and duty revenues.
- *Simona Kukovič, Colin Copus and David Sweeting's* paper, “*Local Democracy in Comparative Perspective*,” provides a comparative analysis of the local government systems and local democracy in three countries: England, Spain, and Slovenia. Emphasis is given to the rules concerning the election and accountability of mayors and local councils. Local government in the three case-study countries has evolved along fundamentally different historical trajectories, traditions and political cultures. The paper demonstrates the various conceptualizations, systemic differences, and choices of local politics and leadership. The institutional arrangements of the three countries are comparable, although wider national

developments have influenced and shaped local government in profoundly different ways.

#### 4 Sectoral and spatial analysis

Sectoral and spatial analyses are a form of meso-economic investigation. The scope of meso-level analyses is narrower than that of macro-level investigations, and in the case of local development studies is constrained either to sub-national geographic entities (e.g. a city or a group of districts) or to particular sectors of the economy (e.g. tourism or information technology). This limitation of scope enables researchers to pay more attention to the specific means, methods, impact mechanisms, organizational structures and geographic features under which the economic forces of supply and demand play out (Matkovskyy 2012).

The papers in this chapter are based on a rich body of empirical detail and are of significant analytical depth. This is achieved by consciously respecting related spatial and sectoral limits, and skillfully using geographic and sectoral specificities to reveal patterns of local development.

- The paper by *Italo Trevisan*, “*Local Development in Italian districts 'after the deluge'*,” describes the historical and economic significance and the adaptation strategies of Italian industrial districts. Italian industrial structure is characterized by the importance of SMEs and their weighty contribution in terms of employment, sales and exports. The international competitiveness of Italian SMEs has been enhanced by another peculiarity of Italian industrial structure: the sectoral concentration of production in small, specific areas. Industrial districts have been instrumental in the development of many areas of Italy. However, the last two decades have been rather disruptive for these Italian districts due to the increasing tension caused by globalization, and competition from low-cost countries. The author pays special attention to adaptation strategies such as enhanced outsourcing and increasing internationalization and delocalization. The study contains a historical and a statistical overview of Italian industrial districts. Subsequently, the adaptation strategies of industrial districts are demonstrated by two case studies containing rich empirical material: (a) one district specialized in the tannery industry and the manufacturing of leather products and, (b) another district specialized in the manufacturing of chairs.
- The paper by *Nicole Litzel and Christoph Rust*, “*History of Success: Regensburg – A local growth miracle*,” is an analysis of the development path of a city and of the impact of its university on employment and know-how transfer in Germany. Local development in the city of Regensburg was driven by a successful regional economic policy, by the evolution of a high-technology industrial cluster which extended networking to many sectors, and by the establishment of the University of Regensburg. The nationwide impact of the university is demonstrated by tracking

the professional and geographical path of its graduate students. The indicators for this impact assessment are calculated based on the student registries of the university, covering all 95,000 students who obtained a degree between 1995 and 2015. This database has been merged with the national social security database that spatially covers the territory of Germany. The results of the calculation show that while many students have found workplaces in the city of Regensburg, in Eastern Bavaria, in Munich, and in the capital Berlin, the impact of the university extends to the whole country. The spatial and sectoral components of the employment decisions of the university's students are analysed with the help of mathematical models, and the factors influencing students' employment decisions are identified and ranked by applying a logit model. It is found to be characteristic of the Regensburg region that very small (less than 50-employee) and very big (more than 1000-employee) local firms have exerted a relatively stronger attraction on graduate students than medium-sized local companies.

- The paper by *Zsuzsanna E. Horváth*, "*Travel and Tourism: Impacts on Local Development*," investigates the advantages of developing tourism and travel in a locality or a region. Economies that rely on this sector have the advantage of diversification and resilience to negative external events and developments. The development of travel and tourism facilitates sectoral restructuring of rural, low-income regions that have previously relied heavily on agriculture and natural resource extraction. Moreover, travel and tourism development promote cultural heritage and traditions. Two regional case studies demonstrate how heritage tourism development may become a specific driver of local development.
- The article by *Zsuzsanna E. Horváth*, "*Smart and Intelligent Cities*," is devoted to the application of information and communication technologies to city management. Progressive city management increasingly relies on information and communication networks, sensors, actuators, and "big data" analysis while offering public services and involving citizens in decision making. The paper offers an overview of the findings of key international literature and describes the latest innovative developments in this domain. The author demonstrates the best practices of the application of IT in urban utilities, transportation, environment, environment protection and commerce. Case studies are presented from South Korea, Taiwan, Qatar, Norway, Netherlands, the UK and Spain.



## 5 Innovative policy interventions, plans and initiatives

During the last two decades, social and political experiments have become increasingly popular in sociology, political science and planning (Huitema *et al.* 2018). Experimenting is not only a research method widely used in medical research and in the evaluation of aid policy projects and programs (Gertler *et al.* 2011), but also a distinct approach to governing in terms of public policy and management. Experiments that involve innovative ideas about governance and management have the potential to become the starting points for policy reform, the re-structuring of certain markets, and for profound local change. Public and private stakeholders frequently try out specific innovative legal and organizational arrangements with a view to repeatedly and recursively improving upon them on the basis of experience. The lessons learnt from experiments in social systems and governance may contribute to a better understanding of the preferences, goals, and commitments of stakeholders and may also reveal the hidden impact mechanisms of policy measures.

The added value of the papers in this chapter lies predominantly in the fact that they describe innovative combinations of policy areas and policy instruments that have been tested in real-life situations of aid policy implementation. Their novelty lies neither in the underlying traditional policy aims (e.g. helping the poor), nor in the application of well-known policy instruments (e.g. offering microcredit to the enterprising poor people). Their innovation appears rather in the ingenious combination of the above-described policy aims and tools, which results in an efficient, interdisciplinary, inter-sectoral, inter-ministerial or inter-departmental approach. Subsequently, this approach can serve as the basis for promising policy experimentation.

- Šárka Waisová and Ladislav Cabada's paper, "*Environmental cooperation as a tool for local development and peacebuilding in conflict-affected areas*," reports on the application of various policy instruments that couple environment protection with security-related and peacebuilding activities. Since the end of the 1990s, environmental cooperation has emerged as a tool for local development, conflict transformation, and peacebuilding. International organizations have implemented various related projects in conflict areas or in post-conflict settings, aiming on the one hand at improving security, while on the other hand at meeting environmentally relevant objectives (such as establishing a natural peace park, preserving the rainforest, or developing water infrastructure). The article demonstrates the innovative policy instrument "Post-conflict Environmental Assessment" which was increasingly applied by international organizations in the Serbia–Kosovo conflict, and also in Lebanon, Iraq, Afghanistan, Sudan and Liberia. Subsequently, "Post-conflict Environmental Assessment" is placed in the context of other assessment methodologies that are applied by international organizations to address environmental challenges.

- The paper by Šárka Waisová and Ladislav Cabada, “*Local development projects and security strategy: security-development nexus in the post-9/11 period*,” offers a literature review of various interpretations of the interdependence between development and security. The security-development nexus is a policy framework that combines the need for security with striving for development. Since the 1990s, international stakeholders and thinktanks (e.g. the World Bank and OECD) and the governments of various developed countries (e.g. the USA and Canada) have been challenged by an increase in the number and volume of stabilization and reconstruction operations in post-conflict regions and in conflict regions. As a result, security as well as development experts have accumulated a wide range of experience and have accentuated the links between security and development. A new interpretation of development assistance was needed: accordingly, development assistance, particularly local development projects, are no longer seen only as tools for supporting local communities but are used as tools of counterinsurgency and counterterrorism. The article offers an overview of projects and programs which in conflict areas combine two sets of aims: on the one hand they establish security and build peace, and on the other contribute to local development. The article elaborates on the related institutional, organizational and managerial changes, and on the budgeting consequences of this combined approach.
- The paper by Dipak R. Pant, “*Re-thinking Development after Disaster - Notes on post-earthquake reconstruction planning in the Central Himalayas, Nepal*,” takes the form of a comprehensive multi-sector plan that describes necessary measures, technical and organizational interventions and associated administrative and financial requirements. The plan includes a description of methods for reducing various types of vulnerabilities of the local population and the environment. It recommends measures for confronting geo-physical and other environmental hazards, and for managing risks to human habitat and road traffic. The reconstruction efforts after the devastating Nepal Earthquake 2015 are regarded as an opportunity to foster collective resilience, to employ a local workforce in recovery projects, and to develop a sustainable economy by implementing well-targeted economic and fiscal policies and encouraging entrepreneurial activism. An integrated program is envisioned, which includes measures ranging from monitoring the geo-hydro configuration through training local people and administrators, and offering financial grants to families who have been hit by earthquakes or landslides. Further recommendations aim at making the settlement structure more resilient by creating new integrated, compact and safer settlements. Further proposals include measures for improving energy policy, minimizing waste, and granting a wide range of subsidies and discounts and concessions. The comprehensive plan foresees that its implementation will be financed not only by the government and international organizations, but also by donations from individuals and charities from both inside and outside Nepal. The essay is based on a field survey of the central Himalayan highlands in Nepal.

- The article by *Annamária Orbán*, “*Social and Cultural Innovations in Sustainable Urban Development*,” provides an overview of the ongoing scholarly debate about the notions of social and cultural innovation and their relation to sustainable urban development. Creative organizational ideas, original products and innovative services have the power to exert a profound impact on the development of locations by assigning new functions to selected places. Subsequently, the author focuses on Central Eastern Europe, where during the last quarter of a century – since the fall of communism – a wide range of grass-roots, bottom-up and spontaneous social and cultural innovations have emerged. The paper describes empirical evidence for the positive and negative impacts of these innovations on citizens’ quality of life. The article continues with two Hungarian case studies: (a) the social policy and child-protection initiative “Prevention by playing” and, (b) the success story of “Budapest Ruin Pub Culture,” which is a spontaneously evolving sector increasingly relevant to local development in relation to tourism, catering, entertainment and real estate. These innovations are put into the context of urban governance, which has the task of creating the necessary administrative and facilitational framework and reconciling emerging conflicts in the respective neighborhoods as well.
- The article by *Peter Futo*, “*Teaching Microfinance with the help of case studies*,” summarizes the educational lessons of an EU-financed project “Teaching Microcredit, 2014–2015”. Worldwide, the provision of microfinance for entrepreneurial poor people is a well-known instrument of development policy. The article presents those concepts of microfinance that are relevant for students of development courses. In particular, the following concepts are described: microfinance, microcredit, micro-deposit and micro-insurance, financial illiteracy and literacy, financial inclusion, the facilitation of micro-entrepreneurship among the poor, female entrepreneurship, creditworthiness, and the sustainability of microfinance schemes. Frequently, the provision of microcredit is used in an innovative way as the financial component of agricultural projects, of small business development programs, or some other delivery of aid. The article compares two case studies of microcredit schemes in a North African setting that serve hundreds of thousands of local beneficiaries: a government-sponsored social microcredit system, and a privately owned and managed commercial one.

## 6 Evaluation of projects and programs

During the last few decades, subsidized development programs have become the most widespread instruments and building blocks of aid policy. Similarly, most local development efforts are decomposed into programs and their constituents: projects (Swinburn *at al.* 2006). Evaluation concerns the assessment, as systematically and objectively as possible, of an ongoing or completed project, program or policy, its design, implementation and results. The aim is to determine the relevance of an intervention, the fulfillment of development objectives, and the efficiency, effectiveness, impact and sustainability of the measure. Evaluators of policy interventions in local development

must take into consideration complex economic, social and environmental constraints in order to assess the success and/or failure of the measures under analysis. Evaluation as a procedure has been institutionalized in all national and international development agencies, donor organizations and thinktanks such as the OECD, the World Bank, the European Union and some development banks. These organizations have defined their own institution-specific methods for standardising their evaluation efforts (OECD 2007; Gertler *et al.* 2011; EuropeAid 2006). Worldwide, public administrations and donors produce many thousands of evaluation reports on a yearly basis. Evaluation is thus a genre of two professions: research, and consultancy.

The added value of the evaluation papers in this chapter lies in their effort to understand and explain their respective projects, their formulation of clear questions for evaluation, and their consequent application of the selected evaluation criteria. The authors not only formulate their opinions about their respective programs, but also make considerable effort (a) to identify a suitable theoretical framework for social or economic change, and (b) to identify the lessons that may be learned.

- The article by Ildikó Husz and Éva Perpék, “*Equal opportunities and investing in children: theory, policies and projects,*” investigates the theoretical embeddedness of the policy area of preventative childcare in the context of human, cultural and social capital theory and social inclusion and exclusion theory. Investing in children is a priority of national and international policies and of development programs. A preventative and child-centred social investment strategy is more productive than one which compensates already existing disadvantages or levels unfair differences. Early child development contributes to better health and educational attainment, favourable job market position, and a lower deviance rate. The authors offer an overview of the related international conventions, recommendations and policies. Recent Hungarian national strategies and their local implementations that aimed at reducing child poverty are investigated with special respect to Roma families affected by extreme poverty, poor housing conditions, a low level of education, and weak labour market participation. Two Hungarian local development programs that aim to improve the life chances of children at risk of poverty and social exclusion are presented and evaluated. The article compares the two programs, according to the services they offer and their impacts. The paper is based on site visits, stakeholder interviews, needs assessment studies, and evaluation documents.
- The article by Marta Kiss and Katalin Rácz, “*The Role of Local Governments in the Development of the Local Economy: international findings in the light of Hungarian case studies,*” evaluates the economic development activities of several Hungarian local governments by taking into consideration analogous measures implemented worldwide. The authors show that the role of local governments in economic development has become strategic over the last few decades, as the former have been able to mobilize resources and coordinate stakeholders. The authors

evaluate the economic development strategy and performance of three Hungarian settlements. For description, comparison, assessment and justification purposes a set of well-defined indicators of local economic development are applied. These factors have been identified by carefully analysing the international practices used in analogous evaluations. A remarkable typology of local economic development strategies is developed by using a conceptual scale that ranges from (a) demand-oriented strategies, which focus on the satisfaction of the needs of the population, to (b) supply-oriented strategies, which focus on business support and the promotion of local investment.

- The paper by Péter Futó, *“Teaching Business Climate Development with the help of case studies,”* presents a practical conceptual framework for Business Climate Development as an area of development policy, and introduces the terms used for evaluating Business Climate Development projects and programs. The structure of such programs and the method of their evaluation is demonstrated with the help of an illustrative case study in which a Business Climate Development program was evaluated in a post-soviet republic. The evaluated program covered the following policy areas: (a) registering businesses, (b) issuing various permits for businesses, (c) dispatching inspectors to oversee various business activities, and (c) managing taxation. Additionally, the evaluators classified the services offered by the program into so-called “aid delivery mechanisms” whereby the categories were as follows: (a) research into the small- and medium-sized business sector, (b) promotion of legal changes, (c) capacity building, institutional development of government agencies and NGOs and (d) awareness raising. The evaluation used the following four criteria, (a) relevance, (b) effectiveness, (c) sustainability, and, (d) impact. The case study has since been applied for educational purposes in the Master’s Course on Comparative Local Development.
- The article by Sinisa Zaric, *“Social capital and local development: citizens’ participation in decision making processes,”* analyses the practice of crowdsourcing and its application to citizen consultation purposes in public policy, which is called citizen sourcing. Crowdsourcing is an internet-based method of obtaining information, ideas or votes by enlisting the participation of a large number of people. Citizen sourcing can be used as an instrument of local democracy, facilitating the links between local leaders, administration and citizens. The article explains how and why the phenomenon of citizen sourcing can be embedded into the context of social capital theory and local development. Social capital as a term has been used widely to operationalize interpersonal trust among citizens, trust in local and other institutions, trustworthiness, as well as citizens’ networking in various associations, clubs, organizations at local and other levels. A typology and evaluation criteria of local citizen sourcing projects are presented. The subsequent case study demonstrates and evaluates the process and the results of a participative budgeting project in a Serbian town. This is an innovative citizen sourcing initiative led by the

local government, whereby each year a well-defined sum from the budget is spent according to the votes of citizens.

- The paper by *Bárbara Gabriel and others*, “*Assessing Entrepreneurship and Innovation in Higher Education Institutions: The ‘HEInnovate’ Initiative at the Universidade de Aveiro, Portugal*,” is a micro-level evaluation of a wider policy initiative. The analysis focuses on the process and results of a self-assessment exercise at the level of a university. The method of self-assessment is a standard investigation, which enables a comparison and aggregation of findings across many higher education institutions. The name of this questionnaire-based self-assessment instrument is “HEInnovate” (HE is an abbreviation for Higher Education). This tool has been used to evaluate the entrepreneurial and innovative activities of many universities and other higher education institutions. The self-assessment is based on the feedback of university personnel and students. The method has been elaborated and disseminated by the OECD and the EU. This paper demonstrates its application at the Department of Mechanical Engineering (DME) of the University of Aveiro (UA), Portugal. It also provides insight into how the results of the “HEInnovate” exercise are utilized in a university setting for designing and implementing innovative, entrepreneurial activities, for exchanging technical know-how, and for connecting the university with wider society.

The authors of this volume are engaged in promoting local development worldwide through their research, education, and consultancy efforts.

#### Notes:

<sup>1</sup> The Joint European Master in Comparative Local Development (Master CoDe), offered by the University of Ljubljana, is a two-year Erasmus+ Master Program organized by a consortium that includes Corvinus University of Budapest (Hungary), the University of Ljubljana (Slovenia), the University of Regensburg (Germany), and the University of Trento (Italy). The master’s course was supported by the European Union. The Master developed into a full, two-year, 120-ECTS-second-Bologna-tier course following the 2011–2012 academic year (previously, it was a 95 ECTS program).

<sup>2</sup> For a fuller and more formal definition of Local Development as a discipline, see the conclusions chapter of this volume by Bruno Dallago: “An integrated systemic view of Local development”.

<sup>3</sup> The English language is not very explicit in this respect because it uses the same form of the verb “develop” in both of the following sentences: “The city developed quickly,” and “The local council developed the city”. However, other languages more clearly specify the reflexive form of this verb, e.g. in French “*se développer*” is the reflexive form of the verb “*développer*”, and analogously in German “*sich entwickeln*” - “*entwickeln*”, while in Russian “*развиваться*” - “*развивать*” have different forms. The Hungarian language is unique in that not only is the reflexive verb “*fejlődni*” formally different from the corresponding transitive verb “*fejlesztani*,” but the respective two nouns have different forms: “*fejlődés*” meaning *development as a process which evolves* can easily be distinguished from “*fejlesztés*” meaning *development as an activity implemented by specific actors*.

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## **Conceptual Framework, Theory and Measurement**



## Theories in Regional Economics in the Light of Local Development

JOACHIM MÖLLER

**Abstract** The spatial dimensions of economics are discussed in the sub-field of Regional Economics. The theories formalize a wide range of issues on a local level. Typical research topics, for instance, are the location choice of firms or workers, economic divergence and convergence of regions, agglomeration advantages and disadvantages, specialization of cities and regions or the importance of knowledge spillovers. This chapter jointly reviews the most important theories on regional economics along with empirical evidence. It aims at identifying factors that important for understanding mechanism of local development along with interregional exchange. As a specific case, the chapter addresses the importance of agglomeration (dis)advantages in developing countries. In general, a deeper understanding of the spatial dimension of economic development can be fruitful for policy guidance on escaping the poverty trap.

**Keywords:** • regional economics • agglomeration • market potential approach • gravity model • Germany

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## 1 Two principles of regional economics

Regional economics is a sub-discipline of economics that introduces spatial aspects into economic analysis. It starts with the observation that productive activities and per-capita income are not evenly distributed across space. In this context, two interrelated principles in regional economics come into play: (i) population density matters for economic outcomes, and (ii) distance hinders exchange.

The concentration of population in space matters for economic outcomes because of a number of factors. If people live close together, there are more intensive transactions between them. These transactions could involve the exchange of knowledge through direct communication; i.e., face-to-face contact. Alternatively, it could mean close supplier-customer relationships either for business-to-business activity or producers to consumers. These locational networks allow for better logistics or for more direct feedback from customers to producers that improves the quality of products and services, for example. Moreover, high population density in an agglomeration fosters the development of patterns of specialization, which increases efficiency and therefore reduces cost. If specialization moves along the value chain then typical cluster phenomena arise that strengthen the economic performance of a region (Marshall 1890; Porter 1990; 1998; 2008). Last but not least, the concentration of people in space generates a big domestic market so that producers in that location are faced with high demand and can profit from economies of scale. A further consideration is that agglomeration fosters diversity (Jacobs 1970). The accessible pool of knowledge and competences in a highly populated location is simply much bigger than that of a sparsely populated area in the periphery.

The second principle, “distance matters,” is closely related to the first. Distance can be seen as a hurdle to economic and knowledge exchange. The latter is important in the innovation process. Economic innovation typically occurs in the form of the combination of ideas that are already known about by experts from different specializations. For instance, constructing robots for nursing care assistance requires combining mechanical engineering and medical knowledge. A higher spatial concentration of (highly) skilled people in areas increases the probability that such forms of co-operation will occur.

Overcoming distance typically involves transport costs in one direction or the other. This immediately becomes clear to any supplier who delivers an intermediate product to another firm – for instance, a producer of car seats delivering to an automotive plant. Greater distance simply means higher transport costs. However, there is another cost component that typically declines with growing distance: reliability of delivery. Today’s high-performance logistics require delivery of intermediate products not only “just in time” but also “just in sequence”; i.e., a seat of the right color, material, shape, etc. within the right time window, as required by the production process for an individual car. Such high-performance logistics are almost impossible over long distances because transport

streams over such distances are more likely to be disturbed by unforeseen events such as traffic jams, etc.

Imagine for a moment that through a technical revolution all transport costs were reduced to zero. In this case, population density would also become economically irrelevant. For instance, the location of a supplier would be of no significance. If communication takes place regardless of distance, then knowledge spillovers<sup>1</sup> are not attached to a specific place. Some scholars are indeed arguing that advances in communication technology and the internet in particular are leading to a situation in which distance becomes increasingly irrelevant to exchange between humans. The “death of distance” (Cairncross 1997) would imply the “end of geography” (O’Brien 1992). This type of argument is also used by Thomas Friedman (2005) in his bestseller *“The world is flat”*. Friedman argues that obstacles to economic exchange and communication have been reduced significantly since the invention of the internet and the end of political block confrontation in the early 1990s.

There is, however, overwhelming empirical evidence that the “death of distance” hypothesis is wrong. Although pieces of information can easily be exchanged worldwide through the internet, there also exists “sticky knowledge”; i.e. knowledge that is attached to specific locations. The importance of informal face-to-face-contact, oral communication, etc. in the innovation process has been widely documented. Here, we refer to “creative milieus,” “something in the air,” “the place to be for a specific business,” etc. All this points to the fact that the choice of location is in many circumstances not arbitrary, and therefore distance plays an important role. With respect to knowledge, this is well expressed in a well-known sentence by Glaeser *et al.* (1992, 1127): “After all, intellectual breakthroughs must cross hallways and streets more easily than oceans and continents”.

The title of an article by Philip McCann (2008) expresses the conviction of the vast majority of regional economists: “Globalization and economic geography: the world is curved, not flat”. Numerous authors have discussed the seeming contradiction that in times of globalization local factors have gained in importance. In this context, Michael Enright has coined the notion “glocalisation” as an artificial composite of globalization and localization (Enright 2003). Enright argues that although competition and economic activities are becoming more globalized, the decisive competitive factors are locational.

## 2 Agglomerations: advantages and disadvantages

A spatial concentration of population with the corresponding economic resources is called an agglomeration. Agglomerations are typically characterized by high population density, and provide specific functions for the surrounding space, known as the periphery. Agglomerations include important cultural and administrative institutions such as universities, research institutes, opera houses and supreme courts. Moreover, central

transport infrastructure such as big airports and railway hubs are typically located in agglomerations.

Why do agglomerations exist? There must be economic advantages of the concentration of populations and economic activities. Traditionally, a distinction is made between two advantages of agglomeration: urbanization, and locational advantages. Urbanization advantages arise due to the general concentration of population and production activities in an agglomeration. Knowledge spillovers, cooperation between different actors, common innovation activity, diversity, close customer-supplier relationships, the shared use of general infrastructure or sheer market size are factors that can be alluded to in this context. By contrast, locational advantages refer to advantages created by firms from the same industry becoming concentrated in specific locations. Important reasons for this phenomenon are the shared use of specific infrastructure and the emergence of a specialized workforce or specialized suppliers for that industry. Localization advantages lead to cost savings and higher levels of competitiveness for firms in specific industries.

Urbanization and locational advantages can explain the occurrence of agglomerations in general. However, agglomerations are not like black holes that draw in all economic activity. The reason for this is that counter-forces in the form of disadvantages to agglomeration also exist. In comparison to the periphery, agglomerations are expensive locations where rent and housing costs are significantly higher. Moreover, agglomerations suffer from traffic jams and other forms of congestion. Typically, social problems like criminality are also concentrated in agglomerations. Hence, there are centrifugal and centripetal forces that at least partly compensate each other.

In Paul Krugman's famous centre/periphery model, factors that foster agglomeration can be identified (e.g. Krugman 1993). In this model lower transport costs and the higher fixed costs of setting up production sites favor agglomeration. The same is true of a higher share of mobile workers.

In the following we introduce two workhorse models in regional economics that show how the elements of distance and density can be combined. The first approach, market potential, can be used to compare different locations with respect to the access to the purchasing power of customers. The second approach, the gravity model, aims to explain the transport streams of persons and goods between different locations.

### **3 The concept of market potential**

The concept of market potential dates back to work by Harris (1954). It represents an example of the combination of the two principles that are discussed in the section above. Market potential is a way of describing a location with respect to accessible purchasing power. The question is how much purchasing power is available at which distance from the location. Purchasing power depends on population density and, of course, on disposable income. However, it should be clear that purchasing power within 20 or 30

kilometers' distance is less relevant to a location than the same amount of purchasing power nearby. Hence, distance matters.

The market potential of a location can be defined as the sum of distance-weighted total accessible purchasing power of that location. Hence, it measures the relevant purchasing power at a location and in the neighborhood of that location. The concept implies that distance is a barrier to economic transactions. Consider, for instance, a customer who seeks to acquire a specific piece of furniture. Of course, it is much more convenient for them if a store is close by. The likelihood that this consumer will choose to visit a furniture store 20 or 30 kilometers away is much lower.

The probability that purchases will decline with distance can be described by a so-called distance-deterrence function. A distance-deterrence function simply generates declining weights for purchasing power located further away. One application of the concept of market potential concerns the choice of a location for a department store, for instance. Other things being equal, the location with the highest market potential should be selected.

Formally, the market potential of a location  $i$  in a region  $J$  can be defined as

$$M_{i,J} = \sum_{j \in J} PP_j f(d_{ij}) \quad (0.1)$$

Here,  $PP_j$  is the total purchasing power in location  $j$ , while  $d_{ij}$  is the (economic) distance between locations  $i$  and  $j$ , for example, measured in travel time. The purchasing power of a location can be calculated as per capita income multiplied by population. The function  $f(d_{ij})$  with  $f' < 0$  is the distance deterrence function (DTF). DTF awards the purchasing power of a nearby location a higher weight, and a more distant locations a lower weight.

Several propositions have been made regarding the concrete specification of the DTF. The most prominent ones are:

$$f(d_{ij}) = d_{ij}^{-\gamma} \quad (0.2)$$

and,

$$f(d_{ij}) = \exp(-\gamma d_{ij}) = e^{-\gamma d_{ij}} \quad (0.3)$$

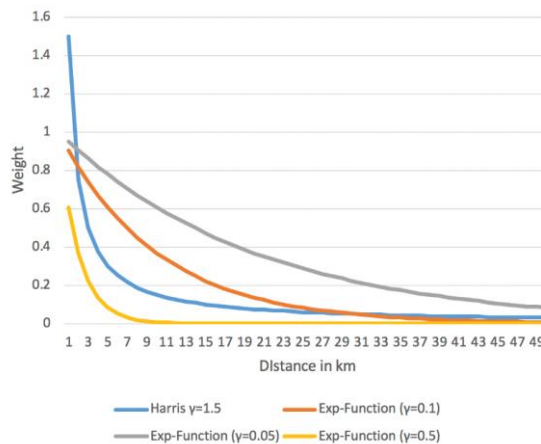
In these equations,  $\gamma$  is the so-called distance deterrent parameter (equation (0.2) originates in original work by Harris (1954)). One specific drawback of this formulation is that the function goes to infinity as distance goes to zero. By contrast, the formulation

in equation (0.3) implies that the value of the function goes to unity if the distance becomes very low. Although the latter supposition seems to be more plausible, many applications in the literature use Harris' original specification.

Figure 1 shows the weight given to purchasing power as a function of distance for alternative specifications of the distance deterrence function. The original DTF of Harris awards high weights to areas in direct proximity to the chosen location and then declines steeply. The exponential function with similar weights for low distance taper off more smoothly. For instance, within a distance of two kilometers the Harris DTF with  $\gamma=0.5$  gives a weight of 0.75, whereas the exponential function gives a weight of 0.82 ( $\gamma=0.1$ ) or 0.90 ( $\gamma=0.05$ ). For distances within ten kilometers the weights for the Harris DTF shrink to 0.15 and to 0.37 and 0.58 for the exponential functions. Of course, for a relatively high parameter in the exponential function ( $\gamma=0.5$ ), the weights also taper off very quickly.

Consider the example in Table 1 where we calculate the market potential of fictitious "City A" for two alternative exponential distance deterrence functions with a relatively high distance deterrence parameter  $\gamma=0.1$  (Model 1) and a relatively low parameter  $\gamma=0.05$  (Model 2), respectively. One can observe in the table that in Model 1, City A exhibits lower market potential than in Model 2. The bulk of the market potential with a high deterrence parameter lies in close proximity to the location that is the subject of observation. In Model 2, the lion's share of market potential is not in City A, but in its neighborhood, especially in the large settlement at 50 kilometers' distance. In general, the contribution of neighboring cities to the market potential of a given location depends on the size, richness and distance of the settlements in the neighborhood. Of course, the smaller the distance deterrence, the greater the weight of more distant neighbors.

**Figure 1:** Weight given to purchasing power for specific distances for alternative distance deterrence functions





**Table 1:** Calculation of the market potential of City A for two alternative exponential distance deterrence functions (fictitious example)

City					Model 1 ( $\gamma=0.1$ )		Model 2 ( $\gamma=0.05$ )	
	Popula- tion in 1000	Disp. income per capita in 1000€	Purch. power in million €	Distance to City A	Exp. weight	Weighted purch. power	Exp. weight	Weighted purch. power
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
A	75	25	1875	0	1	1875	1	1875
B	50	20	1000	10	0.368	367.9	0.607	606.5
C	10	40	400	25	0.082	32.8	0.287	114.5
D	60	35	2100	30	0.050	104.6	0.223	468.6
E	1000	22	22000	50	0.007	148.2	0.082	1805.9
	Market potential of city A:				2528.5		4870.6	

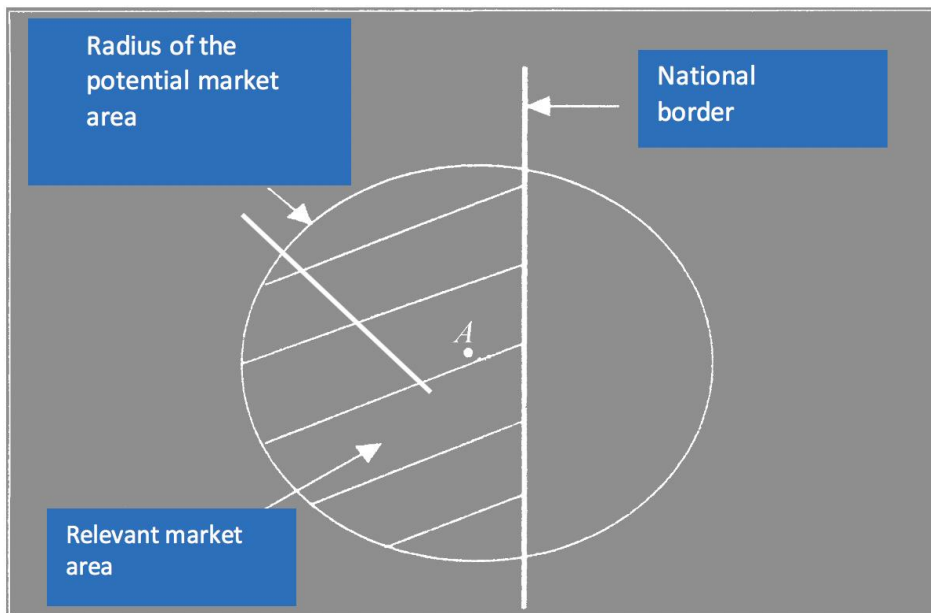
\* Notes: Exp. weight calculated as  $\exp(-\gamma d_{iA})$ , where  $d_{iA}$  is the distance between City i and City A.

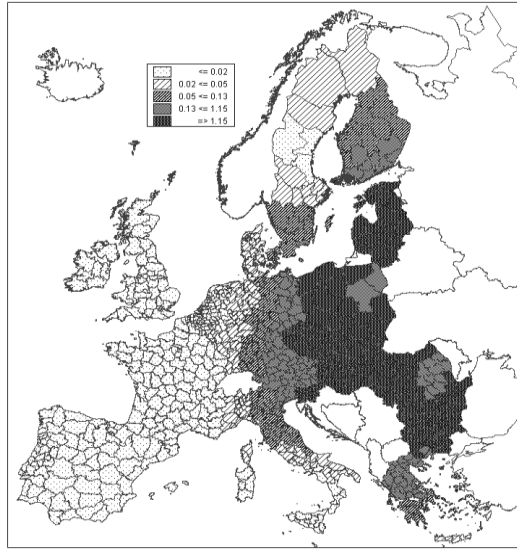
The example shows that the market potential of a location is very sensitive to the distance deterrence parameter. This parameter depends on the nature of the good or service under consideration. To buy an everyday product like a pizza, you would not drive 20 or 50 kilometers under normal circumstances. For a very special cultural event like a concert by your favorite superstar, you certainly would.

The market potential approach has direct applications with respect to border regions. A border is typically a significant obstacle to economic exchange or customer relationships. To investigate the economic effect of a border, imagine the situation of an evenly populated featureless plain and neglect any differences in the transport infrastructure. Then, in an idealized way, the potential market area of location A would be a circle around A with radius  $r$ . The radius is determined by the distance within which the corresponding weight remains under a certain level, so that the weighted purchasing power of such a location – and of all more distant locations – can be neglected. Of course, the smaller the radius  $r$ , the greater the distance deterrence parameter is. Now, consider the situation of a region close to a border through which no transactions are possible. It is immediately clear that the potential market area of a border region is smaller than that of a non-border region. As the weighted purchasing power of the area beyond the border has to be subtracted, the market potential of a border region is typically smaller than that of a non-border region. This effect is frequently used as an argument in regional economic policy for subsidizing border regions to equalize economic conditions.

Of course, opening up of borders produces the opposite effect. An interesting application of the market potential approach concerns EU enlargement. In the analysis of this situation, the fact that western regions typically were much wealthier than eastern regions at the time of EU enlargement played a role. This led to an asymmetric effect of this huge quasi-natural experiment on market potential, as Niebuhr (2005) demonstrated in a study depicts the situation. One can see that the bulk of the effect occurred in central Europe, and was more pronounced in former East Germany, the Czech Republic, Slovakia, Hungary and the Baltic states. Because of distance decay, France, Great Britain, Spain and Portugal were not very much affected.

**Figure 2:** Potential and relevant market area in the case of a border region



**Figure 3:** The effect of EU enlargement on the market potential of European regions

Source: Niebuhr (2005).

## 4 Gravity models

### 4.1 Basic ideas

The gravity model is a workhorse model in regional economics. The basic idea is taken from astrophysics, as developed by Isaac Newton in the seventeenth century, while adaption to the context here is attributed to Tinbergen (1962). Newton's theory of gravity describes the force of interaction between two objects in space (e.g. between the earth and the moon). The use of the concept of gravity for capturing spatial interaction phenomena in regional economics has turned out to be extremely useful (for a comprehensive overview see Head and Mayer (2014)). Of course, the application of the concept in a completely different context requires some modification.

Formally, Newton postulates that the gravity force  $a_{ij}$  between object  $i$  and  $j$  in space is proportionate to the product of the masses of the two objects,  $m_i$  and  $m_j$ , and inversely proportionate to the square of their distance,  $d_{ij}$ . Hence, the law of gravity can be written as:

$$a_{ij} = \gamma m_i m_j d_{ij}^{-2}, \quad (0.4)$$

where  $\gamma$  is a natural constant.

The corresponding model for regional interactions, in direct analogy to the gravity model, would be:

$$t_{ij} = \kappa u_i \tilde{x}_j d_{ij}^{-\gamma}, \quad (0.5)$$

where  $t_{ij}$  stands for a stream of goods, persons or other items originating in  $i$  and ending in  $j$ . The variables  $u_i$  and  $\tilde{x}_j$  are indicators of importance with respect to the region of origin and destination, respectively. As in the original law of gravity, a constant parameter  $\kappa$  is included. Of course, there are several ways of measuring the “importance” of the region of origin and region of destination. A natural choice is to use for  $u_i$  the total volume of all streams originating in  $i$  to *all* relevant destinations  $j \in J$ , where  $J$  includes all relevant destinations for region  $i$ . By the same token, the importance of the region of destination  $\tilde{x}_j$  could be measured as the total volume of all incoming streams to location  $j$  from all relevant regions of origin.

As an example, consider the commuter streams within a certain area. A commuter is defined as a person who lives in place  $i$  and works in place  $j$ . A natural choice for  $u_i$  in this case would be the sum of all outgoing commuters from place  $i$ , whereas for  $\tilde{x}_j$  one could use the sum of all incoming commuters in place  $j$ .

Of course, there are other ways of specifying the importance of the sending and receiving locations. Using the example of commuters, one could use the potential workforce for the place of origin, and the total number of potentially available jobs in the destination area. The potential workforce comprises all persons of working age (e.g. from 15–69 years old) who could be active on the labor market (i.e. the basic population that may commute). The total number of available jobs at the destination site can be measured as total employment plus vacancies. This is the maximum of workplaces that in principle are available to commuters – even if positions cannot be regarded as immediately available.

#### 4.2 Adaption of the physical model of gravity to the regional context

Let us return to the possibility of measuring the importance of sending and receiving locations by the sum of outgoing and incoming streams. These transactions ( $t_{ij}$ ) between

$n$  regions of origin  $i$  and the same number of regions of destination  $j$  are collected in the origin/destination matrix  $\mathbf{T}$  of dimension  $n \times n$  with the typical element  $[\mathbf{T}]_{ij} := t_{ij}$ .

Table 2 shows this matrix together with the sum of transactions over the rows and columns of matrix  $\mathbf{T}$ . Note that  $u_i$ , the sum of row  $i$ , collects all outgoing streams of that location, whereas  $z_j$ , the sum of column  $j$ , collects all the incoming streams of the corresponding location.

The next step is to consider the information about distances between locations or regions. According to the law of gravity in physics, “distance” refers to Euclidean distance (i.e. the minimum length between [the centers of] locations  $i$  and  $j$ ). In our context, “distance” means *economic distance*. Economic distance typically differs from Euclidean distance and includes the cost of bridging the distance between locations  $i$  and  $j$ . For instance, travelling 50 kilometers between two locations means something completely different if there is an express highway connection or only a sand track. Therefore, it might be more appropriate to consider travel time instead of total distance. Note that economic distance is not necessarily symmetrical. Think of the traffic jams in a greater agglomeration. If there are a lot of workplaces at the centre, incoming roads will be typically congested during morning hours, and outgoing roads in the evening.

Assume that an adequate indicator for economic distance between the locations under consideration is available. This information can be collected, analogously to the transaction matrix, in a distance matrix  $\mathbf{D}$  with typical element  $[\mathbf{D}]_{ij} := d_{ij}$  (see Table 3).

**Table 2:** Transactions between the place of origin and the destination area

origin	destination				$\Sigma$
	$R_1$	$R_2$	..	$R_n$	
$R_1$	$t_{11}$	$t_{12}$	..	$t_{1n}$	$u_1$
$R_2$	$t_{21}$	$t_{22}$	..	$t_{2n}$	$u_2$
$\vdots$	$\vdots$	$\vdots$		$\vdots$	$\vdots$
$R_n$	$t_{n1}$	$t_{n2}$	..	$t_{nn}$	$u_n$
$\Sigma$	$z_1$	$z_2$	..	$z_n$	

**Table 3:** The distance matrix

origin	destination			
	R <sub>1</sub>	R <sub>2</sub>	..	R <sub>n</sub>
R <sub>1</sub>	$d_1$	$d_1$	..	$d_{1n}$
R <sub>2</sub>	$d_2$	$d_2$	..	$d_{2n}$
⋮	⋮	⋮		⋮
R <sub>n</sub>	$d_n$	$d_n$	..	$d_{nn}$

Note that the entries on the main diagonal of the matrix  $(d_{11}, d_{22}, \dots)$  stand for the average travel time (or travel cost) within the corresponding region.

Direct application of Newton's law to modelling regional interdependencies does not seem to be reasonable. At least two adjustments are required:

1. The gravity model in physics implies that doubling the mass of two interacting objects in space quadruples the force of gravity between these objects. This implication is questionable. Doubling of the importance of the region of origin and the destination region leading to four times more transactions is not plausible.
2. Distance dependence is very specific. Why should the volume of transactions between  $i$  and  $j$  decline exactly in accordance with the squared distance between the locations? This calls for a modified formulation of distance deterrence.

Considering objections (i) and (ii) leads to a more general formulation of the model of gravity in the context of regional economics. This can be written as follows:

$$t_{ij} = \kappa u_i^\alpha z_j^\beta f(d_{ij}). \quad (0.6)$$

Here, the two new parameters  $\alpha$  and  $\beta$  are introduced to measure the impact of changes in the importance of origin and destination in a less restrictive way than in Newton's law. For instance,  $\alpha = \beta = 0.5$  would imply that the volume of transactions between  $i$  and  $k$  doubles if importance doubles. The general function  $f(d_{ij})$  with

$f' < 0$  stands for the *distance deterrence function*. In the present context it measures how a higher (economic) distance between locations  $i$  and  $k$  influences the volume of transactions. Several proposals have been made for the concrete specification of the distance deterrence function. The most prominent ones are:

$$f(d_{ij}) = d_{ij}^{-\gamma}, \quad (0.7)$$

and,

$$f(d_{ij}) = \exp(-\gamma d_{ij}) = e^{-\gamma d_{ij}}. \quad (0.8)$$

A specific drawback of the formulation in equation (0.7) is that the function approaches infinity as distance approaches zero. By contrast, the formulation in equation (0.8) implies that the value of the function goes to infinity if the distance becomes very low. The latter assumption seems to be more plausible.

### 4.3 Transformation of the model into a regression approach

Assume we have data for all  $t_{ij}$  so that matrix  $\mathbf{T}$  is known. From the row and column sums we can then calculate  $u_i$  and  $z_j$ . How should we then obtain the unknown parameters  $\alpha, \beta, \gamma$  and  $\mathbf{K}$ ? The answer is by regression analysis. However, the model considered so far is a non-linear model. The ordinary least squares (OLS) method requires linearity. By taking logs we can transform the gravity model into a linear version:

$$\ln t_{ij} = \ln \kappa + \alpha \ln u_i + \beta \ln z_j - \gamma \ln d_{ij}, \quad (0.9)$$

for a distance deterrence function as in equation (0.7), or,

$$\ln t_{ij} = \ln \kappa + \alpha \ln u_i + \beta \ln z_j - \gamma d_{ij} \quad (0.10)$$

for the alternative specification (0.8). In the following, we use the latter equation.

Reparametrisation of the model and inclusion of a disturbance term yields:

$$\ln t_{ij} = \beta_1 + \beta_2 \ln u_i + \beta_3 \ln z_j + \beta_4 d_{ij} + \varepsilon_{ij}, \quad (0.11)$$

where  $\beta_1 := \ln \kappa, \beta_2 := \alpha, \beta_3 := \beta, \beta_4 := -\gamma$ . The parameters in equation (0.11) are collected in a vector  $\boldsymbol{\beta} := (\beta_1, \beta_2, \beta_3, \beta_4)'$ . Let  $\mathbf{Y}$  be the vector of variables to be explained,  $\mathbf{X}$  be the matrix of explanatory or independent variables, and  $\boldsymbol{\varepsilon}$  a vector of stochastic disturbances that describes non-systematic random influences on the relationship under consideration. Then the regression approach can be written in a more compact matrix/ vector form, as follows:

$$\mathbf{y} = \mathbf{X}\boldsymbol{\beta} + \boldsymbol{\varepsilon}, \quad (0.12)$$

Vector  $\mathbf{y}$  can be formed through a simple transformation and re-organization of the elements of the origin/destination matrix  $\mathbf{T}$ . All the elements of the matrix are taken in logarithmic terms and the matrix is “vectorized” (the columns of the matrix are stacked above each other). Formally, this can be written as:

$$y = \text{vec } \ln \mathbf{T} := (\ln \mathbf{t}_1', \ln \mathbf{t}_2', \dots, \ln \mathbf{t}_n')', \quad (0.13)$$

where  $\mathbf{t}_i$  is the  $i$ th column of matrix  $\mathbf{T}$ .

The matrix of explanatory variables,  $\mathbf{X}$ , consists of four columns. Let us consider as an example rail travellers per month between three cities such as Munich (1), Nuremberg, (2) and Frankfurt (3). If we have data for one month only, the origin/ destination matrix and the distance matrix are given as:

$$\mathbf{T} := \begin{pmatrix} t_{11} & t_{12} & t_{13} \\ t_{21} & t_{22} & t_{23} \\ t_{31} & t_{32} & t_{33} \end{pmatrix}; \quad \mathbf{D} = \begin{pmatrix} d_{11} & d_{12} & d_{13} \\ d_{21} & d_{22} & d_{23} \\ d_{31} & d_{32} & d_{33} \end{pmatrix}. \quad (0.14)$$

Here  $t_{11}$  stands for the number of rail travellers within Munich,  $t_{12}$  for the travellers between Munich and Nuremberg, and  $t_{21}$  for travellers between Nuremberg and Munich, for instance. The variable  $d_{11}$  stands for average travelling time in minutes for rides within Munich, whereas  $d_{21}$  denotes travelling time from Nuremberg to Munich, and so on. Then the regression equation can be written as follows:

$$\mathbf{y} = \mathbf{X}\boldsymbol{\beta} + \boldsymbol{\varepsilon},$$

or more explicitly:

$$\begin{pmatrix} t_{11} \\ t_{21} \\ t_{31} \\ t_{12} \\ t_{22} \\ t_{32} \\ t_{13} \\ t_{23} \\ t_{33} \end{pmatrix} = \begin{pmatrix} 1 & \ln n_1 & \ln \zeta_1 & d_{11} \\ 1 & \ln n_2 & \ln \zeta_1 & d_{21} \\ 1 & \ln n_3 & \ln \zeta_1 & d_{31} \\ 1 & \ln n_1 & \ln \zeta_2 & d_{12} \\ 1 & \ln n_2 & \ln \zeta_2 & d_{22} \\ 1 & \ln n_3 & \ln \zeta_2 & d_{32} \\ 1 & \ln n_1 & \ln \zeta_3 & d_{13} \\ 1 & \ln n_2 & \ln \zeta_3 & d_{23} \\ 1 & \ln n_3 & \ln \zeta_3 & d_{33} \end{pmatrix} \begin{pmatrix} \beta_1 \\ \beta_2 \\ \beta_3 \\ \beta_4 \end{pmatrix} + \begin{pmatrix} \varepsilon_{11} \\ \varepsilon_{21} \\ \varepsilon_{31} \\ \varepsilon_{12} \\ \varepsilon_{22} \\ \varepsilon_{32} \\ \varepsilon_{13} \\ \varepsilon_{23} \\ \varepsilon_{33} \end{pmatrix}. \quad (0.15)$$

If observations for several periods are available, then a more general model would include a repeating structure of  $\mathbf{y}$ ,  $\mathbf{X}$  and  $\boldsymbol{\varepsilon}$  for each time period (1,2, ...T):



$$\mathbf{y} := \begin{pmatrix} y_1 \\ y_2 \\ \vdots \\ y_T \end{pmatrix}; \quad \mathbf{X} := \begin{pmatrix} \mathbf{X}_1 \\ \mathbf{X}_2 \\ \vdots \\ \mathbf{X}_T \end{pmatrix}; \quad \boldsymbol{\varepsilon} := \begin{pmatrix} \varepsilon_1 \\ \varepsilon_1 \\ \vdots \\ \varepsilon_T \end{pmatrix}. \quad (0.16)$$

The Ordinary Least Squares (OLS) method yields an estimate  $\hat{\boldsymbol{\beta}}$  for the coefficient vector  $\boldsymbol{\beta}$ . With the help of this estimate it is straightforward to calculate the fitted values of the dependent variable  $\hat{\mathbf{y}} = \mathbf{X}\hat{\boldsymbol{\beta}}$ .<sup>2</sup> Moreover, it will then be possible to determine the expected values of transport streams if there are changes in the explanatory variables.

As an example, consider that the travelling time between Munich and Nuremberg is reduced by a significant amount because of the opening of a rapid new railway connection. In this case, the model allows us to make predictions about the corresponding transport streams  $t_{ij}$  that would be highly valuable in public planning procedures, among other uses.

#### 4.4 Intervening opportunities

The application of the gravitation model considered so far suffers from specific drawbacks. It relies on an unrealistic “as if” assumption: the analysis implicitly assumes that between the cities under consideration there are no competing places that might distract transport streams. As with Newton’s model, the analysis of gravitation forces on the earth might be heavily biased if only the force of gravity between the sun and earth were considered and other spatial objects like the moon were neglected. If transport streams are generated by economic opportunities, then locations between City A and City B could be influenced by places between A and B that also represent economic opportunities. This situation becomes immediately clear in the situation that the transport streams are mainly associated with commuting or shopping trips.

Let the intervening opportunities of A be defined as opportunities that are more easily accessible from A than the opportunities in B. The recognition that the intervening opportunities might play an important role in the analysis of spatial economic interaction dates back to the work of Stouffer (1940),<sup>3</sup> who formulated a kind of law in relation to this context. In the present case, Stouffer’s law might be formulated as follows:

*The number of trips between a zone of origin and a zone of destination are proportionate to the number of opportunities in the zone of destination, and inversely proportionate to the number of intervening opportunities.*

As an example, consider customers who are interested in buying furniture. The number of shopping trips of this group of customers from origin A to destination B might be proportionate to the total sales area in square meters of furnishing shops in B, and inversely proportionate to the total sales area of furnishing shops that are situated between A and B, because these intervening opportunities diminish the chance of customers choosing a shop to visit in B.

Stouffer's approach was first applied in the famous *Chicago Area Transportation Study* (1960). There can be no doubt that his basic argument is valid. However, the concrete formulation of his law is quite unlikely to be relevant in reality. The problem concerns the postulated proportional relationship. Moreover, the original Stouffer approach assumes a one-dimensional economic space and should be generalized. Intervening opportunities should be understood not as opportunities directly situated between A and B, but all opportunities that are more easily accessible than opportunities in B. To extend our example, assume that B is situated north of A and the travelling time is 30 minutes. A furniture shop to the East, South or West that could be reached within 20 minutes clearly belongs to the set of intervening opportunities. Hence intervening opportunities in this example are defined as all furniture shops that are reachable in less than 30 minutes from location A.

In empirical studies, the consideration of intervening opportunities requires an augmented gravity model. If the importance of intervening opportunities between origin  $i$  and destination  $j$  can be measured by  $V_{ij}$ , then the model that should be estimated can be written as:

$$\ln t_{ij} = \beta_1 + \beta_2 \ln u_i + \beta_3 \ln z_j + \beta_4 v_{ij} + \beta_5 d_{ij} + \varepsilon_{ij}$$

Its transformation into a regression model is analogous to that undertaken for the classical gravity model.

## 5 Summary

Regional economics has developed several workhorse models. Starting with the fact that distance and the spatial distribution of population matters for economic outcomes, we introduced the concept of market potential and demonstrated some applications of this. We then described the classical gravity model and transformed it into a simple regression model. This model is capable of describing spatial interactions such as commuter streams and trade flows, etc. The classical gravity model is extended by the intervening opportunities approach. A labour market model that captures the basic idea is used to show that the "law" of indirect proportionality postulated by Stouffer is typically not appropriate in an economic context. However, in a generalized form the intervening opportunity approach is helpful for avoiding the biased estimates of the classical gravity model.

**Notes:**

<sup>1</sup> Knowledge spillover refers to the voluntary exchange or the involuntary leakage of information that is useful in the production process or to businesses providing services.

<sup>2</sup> The goodness of fit can be checked using various statistical measures such as the coefficient of determination, the standard error of the estimation, or the average root mean squared error.

<sup>3</sup> Stouffer, S. A. 1940. Intervening Opportunities: A Theory Relating Mobility and Distance. *American Sociological Review* 5 (6): 845–867.

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## Infrastructure and Local Economic Development

PETER HALLER & JOACHIM MÖLLER

**Abstract** Investments in infrastructure have always been an issue in political discussions about future (local) economic development. Besides the overall effects of infrastructure on a country's GDP, the regional and local consequences of the latter are of special interest to policymakers. Infrastructure is generally defined by its different constituents – for example, the water and power supply, communication network, or transport infrastructure (such as road or rail) – of a region. Questions about the role of infrastructure mainly concern spatial aspects: for instance, the importance of proximity to main transport axes, or how information and communication networks can reduce physical distance are issues often addressed. In developed countries, infrastructure mainly drives the spatial economic interaction between cities, suburbs and peripheral regions. In contrast, a lack of infrastructure is one reason for the rapid urbanization of developing countries. This chapter reviews the current findings in this field. To put the literature into perspective, we utilize the case of transport infrastructure on the regional labor market development. For this, we examine the long-term effects of the German Autobahn network on regional wages and local employment structure, and look at current road investment in Germany.

**Keywords:** • investment in infrastructure • German Autobahn • urbanization  
• wages • employment structure • Germany

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## 1 Introduction

A nationwide, robust and reliable infrastructure constitutes the base for sustainable economic development or the transition from a locally fragmented agricultural economy to an integrated nation dominated by a tertiary sector. Around 40% of investment goes on assets such as buildings and public structures (e.g., roads, bridges, dams, excluding dwellings) (OECD 2019). In Europe, investments into roads have accounted for the dominant part of expenditure on transport infrastructure since 1995 (European Environment Agency 2017).

However, basic infrastructure such as roads, rail, communication technologies and electrical power, as well as water and sanitation, remains scarce or defective in many developing countries. The OECD stresses the importance of transport infrastructure which provides “economic and social benefits to both advanced and emerging economies by: improving market accessibility and productivity, ensuring balanced regional economic development, creating employment, promoting labour mobility and connecting communities” (OECD 2019). In other words, inadequate infrastructure leads to a lack of access to national or international good markets and employment opportunities, and hinders information transfer and education – which all hamper economic development. For this reason, the United Nations defines investing into infrastructure as one of the 17 sustainable development goals for transforming developing countries. By 2030, the aspiration is to “build resilient infrastructure, promote inclusive and sustainable industrialization and foster innovation” (OECD 2019). Admittedly, these are ideal goals whose realization is very complex. For the more accurate evaluation of such investment, more empirical justification by researchers and consultants (e.g., from the field of local development), is hence necessary.

Accordingly, the purpose of this chapter is to offer guidance about how to identify and evaluate the aforementioned theoretical advantages of investments into infrastructure.

- First, we give an overview of the recent economic literature about the economic importance of infrastructure.
- Second, we define the basis on which the wider spatial effects of infrastructure investment can be captured.
- In the following, we focus our discussion on the case of investment in the German motorway road network known as the *Autobahn*. For two different (economic) stages of the current and early construction of the major road network, we discuss the market access and local economic development that followed such road investment.

Although the focus in this chapter is road infrastructure, we do not wish to diminish the importance of other types of infrastructural development – especially in developing countries (e.g., Dinkelman (2011) for electrification in South Africa).

## 2 Empirical evidence about urbanization and transport infrastructure

A striking element of economic development worldwide is the growth in the urban population (see Desmet and Henderson (2015) for an introduction). Rapid urbanization in the developing world has attracted recent attention in regional and urban economics (Glaeser and Henderson 2017) by stressing the importance of distance in this process. Patterns of urbanization are partly determined by so-called “first nature” fundamentals; i.e., factors such as access to waterways, whether such processes involve the regional capital, and path dependency (related to the country's history). However, the existence of booming and declining cities can also be attributed to forces of agglomeration and dispersion (“second nature” factors), which also play a role in shaping spatial structure (see Combes and Gobillon (2015) for a review). The advantages of agglomerations can be summarized as the sharing of inputs and common infrastructure, better matching of jobs and workers, as well as knowledge spillovers and learning effects between workers and firms (Duranton and Puga 2004). In developing countries, close proximity to labor supply and demand are the main drivers, despite the lack of sufficient infrastructure. The dispersion and agglomeration forces of spatial economic activity significantly depend on the transportation of people and goods (see Redding and Turner 2015), of which the transportation of people is much more expensive. One reason for patterns of urbanization may be a lack of infrastructure and the resultant failure to bring economic growth to distant regions.

Transport infrastructure is the binding thread in local development and in place-based policies (see Duranton and Venables 2018). Related investments can have direct effects (e.g., on construction) and wider indirect economic effects. The latter are economically more important but very diverse. For instance, improvements in transport infrastructure can stimulate regional economic development in rural areas, along with population growth and changes in industry structure or commuter flows. In the past ten years there has been a vibrant discussion about these impacts in regional and urban economic research, often with special emphasis on developing countries (Redding and Turner 2015).

Any meaningful evaluation of the effects of infrastructural investment is aggravated by the complex system of centrifugal and centripetal forces. For instance, the reduction in transport-related costs following the opening of a road may significantly depend on the specific history and the spatial economic system of associated cities. Due to this complexity, the ideal starting point for any discussion is a sound review of empirical evidence from different countries at different stages of economic development. Better transport infrastructure per se can stimulate growth due to improvements in the accessibility of a region; however, it can also hinder growth, or harm the local economy. This is the so-called “two-way roads problem” (see Cheshire *et al.* 2014) that was described by late-nineteenth century German engineer and spatial economist Wilhelm Launhardt in the statement that the best protection of an underdeveloped region is a bad road (Möller and Zierer 2018). For instance, a new road can help establish new trade links

with other regions, which will not necessarily be advantageous for all locals (see also Baum-Snow *et al.* 2018).

In any discussion about the advantages of infrastructure investment it is very important to discuss causal relationships. In order to estimate the so-called “treatment effect,” the effective direction of causation needs to be carefully considered. In a nutshell, the availability of infrastructure – or its construction – may be either the cause or effect of economic developments. Baum-Snow and Ferreira (2015) have established a framework which summarizes identification strategies for causal inference in local development. Furthermore, Duranton and Venables (2018) have designed place-based policy framework to empirically evaluate such investments. A large part of the literature focuses on current and past road infrastructure (e.g., Michaels 2008; Baum-Snow 2007; Duranton and Turner 2012; Duranton *et al.* 2014) or railroads (Donaldson and Hornbeck 2016) in the USA. Another part of the literature discusses the effects of infrastructure in newly developed economies (Donaldson 2018; Ghani *et al.* 2016; Baum-Snow *et al.* 2017) and developing countries (Storeygard 2016; Jedwab and Moradi 2016). For Germany, Heuermann and Schmieder (2018) investigate the effects of the rail network on workers' mobility, while Möller and Zierer (2018) examine the impact of the autobahn network on regional employment levels and wages.

A common method is the parallel analysis of historic plans and the actually developed transport networks which are still in use today. The original plans may have promoted different objectives than those of current investments. Another method is the so-called “straight-line-approach” which is favored for identifying the causal effects of infrastructure in regions situated in between two major cities.

Investment into roads and rails has been a dominant factor in the budgets of developing countries and international aid organizations. In order to provide a more thorough introduction to local development analysis, we discuss several cases from different countries more in detail.

- Agrawal *et al.* (2017) examined how roads can facilitate local knowledge flows, hence innovation activity. The stock of planned highways and rails tracks in the USA spur regional growth due to the inflow of new workers. Policy makers may conclude that transport infrastructure can also serve to facilitate innovation spatially.
- Ghani *et al.* (2016) investigated the effects of large-scale highway infrastructure on the growth of the manufacturing sector (e.g., productivity increases and entry costs) along newly established roads in India. The authors also included a cost-benefit calculation in their conclusion.
- Also focused on highways, Banerjee *et al.* (2012) assessed the impact of access to transportation networks on regional GDP growth in China. They also incorporated a highway system that connects major historic cities.



- Focusing on Sub-Saharan Africa, Storeygard (2016) used exogenous variation in transport costs (i.e. oil prices) to shed light on the short-term development of more or less accessible regions in the hinterland in different African cities.
- With respect to railways, Jedwab *et al.* (2017) discussed the effects of railways constructed by European settlers or Asian traders in Kenya. The city structure established by the investments into transport infrastructure did not vanish after independence. Hence, infrastructure is considered crucial for the spatial economy and has long-lasting effects.
- In another publication about Ghana, Jedwab and Moradi (2016) confirmed that the original colonial railroad network created a spatial structure, which persists after the development of road transportation.

When analysing local development with regard to transport infrastructure, a review of causes and outcomes is a necessity, and should always mark the starting point.

### 3 The concept of market potential

Every region is embedded in a spatial structure with several neighboring regions or cities. Dispersion and agglomeration forces relate to two fundamental principles of regional economics: population density, and distance. In chapter “Theories in Regional Economics in the light of Local Development” the concept of market potential is introduced. Market potential can also be described through the decrease in spatial economic interaction across space, usually referred to as “distance deterrence”. Empirical examples of spatial economic interaction are commuting between cities or regions, as well as trade in intermediate goods in manufacturing (both sharply and spatially decline with distance). For instance, research has shown that for one additional minute of driving time, the number of commuters declines by 1.8% (Ahlfeldt *et al.* 2018). Around 95% of commuters’ workplaces are located within 60 minutes of their residence.

However, distance in our context means economic distance, which, in contrast to physical distance, can be influenced by infrastructure and transport technology.<sup>1</sup> The concept of market potential is an excellent starting point from which to obtain a feeling about how regional and potential economic mass can differ, and how changes in transport infrastructure impact distance deterrence, hence mass. An alternative representation of market potential can be defined as follows (see Harris 1954):

$$\text{Market Potential}_{rt} = \sum_{\substack{j=1 \\ r \in J}}^J L_{jt} f(d_{rj}) = L_{rt} + \sum_{\substack{j=1 \\ j \neq r}}^J L_{jt} f(d_{rj})$$

where  $L$  can be any economic variable (e.g., population or GDP), in any region  $j$ . The spatial decay function  $f(d_{rj})$  depends negatively on the distance between region  $r$  and  $j$ . Here, transport infrastructure is implicitly recognized since it affects the physical distance between two regions. We can separate the equation into “Local Market” ( $L_{rt}$ ) and

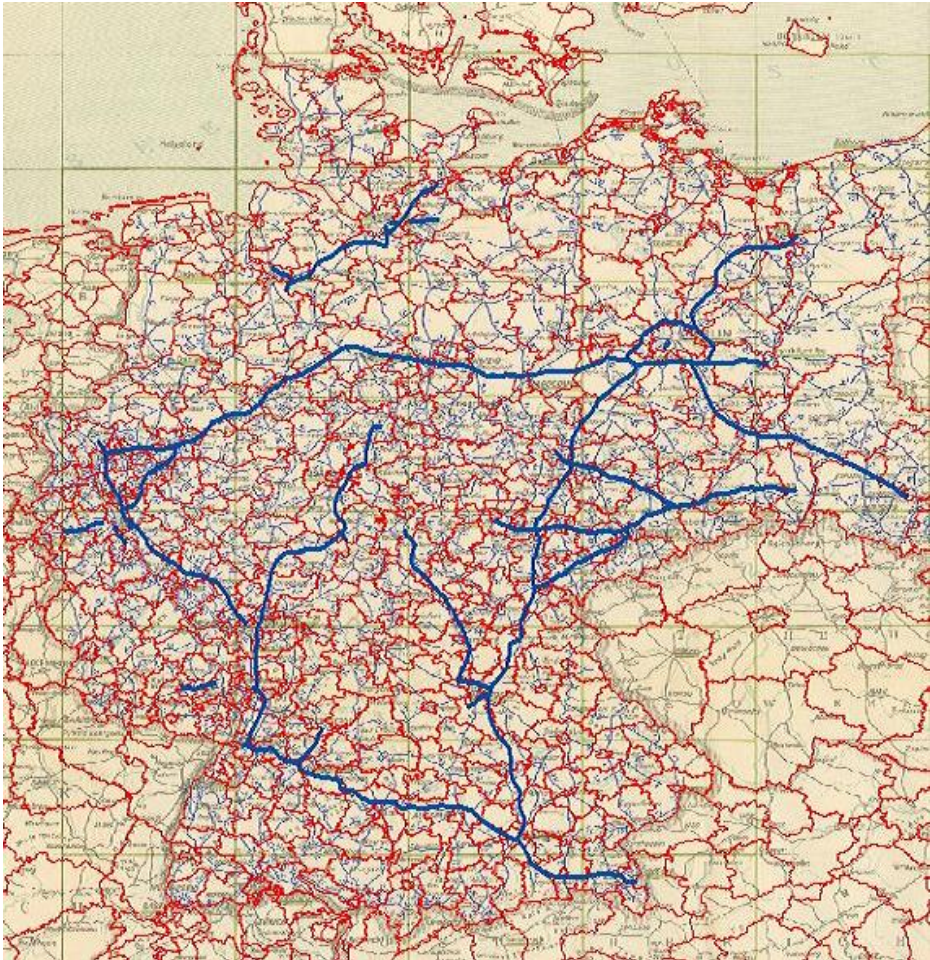
“Potential Market”  $\sum_{j=1}^J L_{jt} f(d_{rj})$  segments. While the first part is the local value of a region, the second part of the equation refers to the distance or travel-time discounted potential market that may be reached from location  $r$  at time  $t$ . It thus accounts for the influences of neighboring regions, which represent potential or accessible markets.

Access to other markets measured by market potential works in both directions. On the one hand, a greater potential market increases economic opportunities, while on the other hand it also can increase competition. With the use of market potential, only the net effect of these opposing effects are observable. For empirical analyses it may be favorable to limit the regional catchment to a specified distance (e.g., 60 minutes’ travel time, or 100 km). In some cases the decay leads to implausible results if it is not limited.

#### 4 Case study: the Autobahn network in Germany

In the following we discuss a comparative case involving the German highway system. The so-called autobahn was initially planned before the Second World War and was strongly influenced by the division of Germany. From the 1970s onwards, the German Federal Highway Development Act planned the future road network 10 to 15 years in advance. The comparative aspect in this case involves the different approaches to analysing transport infrastructure in a highly developed country. In first section the long-term effects of general road infrastructure will be discussed. Afterwards, in second section, current road investment in an established network is the focus.

**Figure 1:** German Autobahn network in 1937



\* The German Autobahn network is depicted in blue. Borders of administrative areas are colored red. German territory changed after the Second World War, hence the map differs from the one included in the next section.

Source: Möller and Zierer (2018).

#### **4.1 Early infrastructural investment with long-term effects**

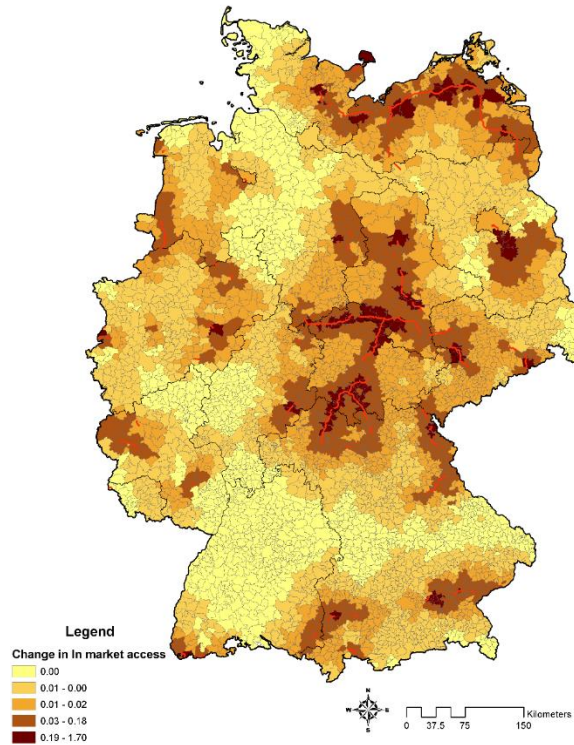
The approach in Möller and Zierer (2018) is in line with the increasing number of studies that used early infrastructure investment (“second nature” advantages) to identify the causal effect of transport infrastructure on population growth and economic outcomes at the regional level. The former authors build on the approach of Duranton and Turner

(2012) by using the historical plan for autobahns and railway tracks in Germany prior to the Second World War. In Figure 1, segments of the autobahn are depicted. The network mainly connects major cities on a West-East axis from the Rhein-Ruhr area to Berlin. On the South-North axis it connects Munich, Nuremberg, Stuttgart and Frankfurt. The network had a total length of more than 3600 km. At that time, driving was still a privilege, which is why the autobahn was mainly established for military purposes.

In order to identify the regional effects of transport infrastructure Möller and Zierer (2018) utilize the “inconsequential units approach”. This means that a region only gets the “treatment” of being connected to the road or rail network if it is located between major cities or hubs. For instance, due to high construction costs railroads were usually built in the form of a straight link between major hubs (see e.g., Hornung (2015) for Prussia). The model assumes that the regions that lie in between major hubs were connected to the network independent of their previous economic importance and, likewise, their growth may have been attributable to rail or road development “treatment” independent of earlier economic performance.

In comparison to the situation in the USA (Duranton and Turner 2012), for Germany Möller and Zierer (2018) found a slightly smaller positive effect for (historic) investment in the length of regional autobahn on the future employment growth of particular regions. The authors compiled a database of regions of Germany containing historical autobahn lengths and employment data per region. They found that a one-standard-deviation increase in the growth of autobahn length between 1937 and 1994 led to employment growth of between 2.7 and 3.4%, and to a wage bill increase of between 3.0 and 3.7% over the period from 1994 to 2008. Compared to Germany, the employment elasticity of express highway length appears to be considerably larger for US regions for several reasons, including car use, fuel taxes, and car use habits. The increase in regional accessibility has a positive effect on labour markets but, according to this study, the development of regional roads has a greater impact on the development of regional labor markets as opposed to the development of interregional roads.

**Figure 2:** Investments into the Autobahn Network: Change in Market Access in Germany



\* Only road segments open to traffic are depicted.

Source: Ahlfeldt et al. (2018).

## 4.2 Current road investment and changes in market access

In line with previous arguments, we look at the case of investment into the German autobahn network between 1999 and 2015. With a total length in 2015 of about 12,950 km, the German autobahn (“interstate highway”) system is one of the densest in the world. It is well known worldwide for having parts with no speed limits. In Figure 2, we depict the road elements that were opened between 1999 and 2015. After German reunification, one major goal was to equalize and foster sustainable economic development in the former states of the German Democratic Republic. Such investments were financed by a special levy, the so-called solidarity tax (*Solidaritätszuschlag*), which is why we see some of the highest increases in market access in the East.

The analysis of Ahlfeldt *et al.* (2018) uses changes in transport-induced labour market access over time to evaluate the impact of effective density on local productivity and the

demand for and supply of labour. This contrasts with the method used by Möller and Zierer (2018), which evaluates the economic success or failure of current road investment. In order to evaluate the effects of road investment, Ahlfeldt *et al.* (2018) built a complete theoretical economic model which incorporates many agents of the spatial economy. This model is built both on the demand side of labour (i.e. firms seeking workers) and on the supply side (i.e. on workers offering manpower), as well as the equilibrium where demand and supply meet. In a nutshell, Ahlfeldt *et al.* (2018) estimate the labour market effects of transport improvements using a framework that allows wage and quantity responses to interact both ways. Agglomeration forces and location fundamentals are separated by taking into consideration the variation in bilateral transport costs: i.e., by allowing all stakeholders to optimize their spatial economic behavior. The theoretical background of the model requires deep understanding of urban economic theory and makes a significant demand on data. The analysis of Ahlfeldt *et al.* (2018) is an excellent example of how to start an analysis of recent road investment in the light of the increasingly detailed spatial data that is available (e.g., from administrative sources, including high precision geo-spatial data). The authors' work is also a good example of how the stress may be placed on the importance of the wider economic effects of transport infrastructure. "Pure" improvements in market access do not necessarily prove the success of an investment, but rather demonstrate the changes that have been induced in the spatial economy. The sophisticated equilibrium model demonstrates how improvements in transport infrastructure increase the likelihood that workers will be better matched with new employers. With this approach, the former provides evidence about the relevance of agglomeration economies as drivers of urban productivity and the unequal spatial distribution of economic activity.

## 5 Conclusion

Investment in public infrastructure has wider economic effects not in the short- but in the long term. We stress that sustainable and reliable infrastructure is a necessity for promoting local development within and across countries. In our examples of transport infrastructure, (early) investment induces an increase in the trade, urbanization, etc. of a country. In general, investment into infrastructure undoubtedly has an overall positive economic effect, although this is significantly context dependent. High investment costs in the short term might be a limiting factor, as outcomes only become visible in the long term. There are also numerous examples of large investments into infrastructure which have not proven to be profitable (e.g., infrastructure for the Olympic Games). The policy implication of this chapter is that a historical perspective should be employed when assessing the impacts of investment into infrastructure, as well as a comparison of current best practices in other countries with a similar history or countries at a similar state of economic development. In this chapter we have employed an economist's perspective, but it is important to involve all stakeholders in decision-making (e.g., city planners, local authorities, and the local community), as the consequences of such activity have effects that last for decades.

**Notes:**

<sup>1</sup> In contrast, Haller and Heuermann (2016) find that spatial spillovers in the job search market might be best described by direct physical distance.

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## Measuring Regional Economic Dynamics

WOLFGANG DAUTH

**Abstract** This article describes the use of some statistical instruments widely used for explaining the interrelationship between the national and regional growth of regions and industries. The uses and limits of the shift-share model as a predictive tool are presented and illustrated with the help of a database containing employment data about the regions and industries of Germany. In addition, a graphical approach to visualizing the growth profiles of regional industries is presented.

**Keywords:** • structural change • local industry structure • local employment growth • Germany

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## 1 Introduction

Economic growth is by no means uniformly distributed within countries. In most industrialized countries, there are vast differences in economic growth across different regions. In the United States, for example, cities like New York, Chicago, San Francisco and many cities in the southernmost states have flourished over the last couple of decades. During the same time period, other cities, most predominantly those in the so-called rust belt such as Detroit and Cleveland, have severely declined. Aside from geography, there are obvious differences between these cases: The flourishing cities on the one hand have experienced particularly strong growth rates in modern service industries and in the high-tech sector. The declining cities, on the other hand, used to be very prosperous due to their reliance on heavy manufacturing, which today is in decline.

According to the Three-Sector Hypothesis (often also referred to as Petty's Law), a country's economy will change its foundation from the secondary to the tertiary sector as the country's economy develops (Murata 2008). This results in the secular trend of structural change that most industrialized countries are currently undergoing: employment is declining in the manufacturing sector and increasing in the service sector.

The above examples of US cities document that this structural change does not occur uniformly in all regions to the same extent. This also applies in the case of Germany.

In southern Germany, there are many regions that have grown over the past three-and-a-half decades. These regions either successfully underwent structural change and overcompensated for the decline in manufacturing with even faster growth of the service sector, or they developed in opposition to this trend and even expanded their manufacturing sector.

Other regions have suffered from structural change. Notable examples include cities in the Ruhr area. While they used to be Germany's powerhouses of heavy manufacturing, they have not recovered from the decline in these industries during the past 30 years.

In this article, we build on the methodology developed by Dauth and Südekum (2016) to examine the patterns of long-term structural change in German regions. The analysis will show that both the speed and the direction of structural change vary substantially. In contrast to what one would expect from Petty's Law, undergoing structural change from a manufacturing to a service economy at a faster pace is not a necessary condition for regional growth. The crucial determinant is regional industrial structure. Regions that had just the right industry mix and which managed to build on this mix appear to have grown particularly strongly.

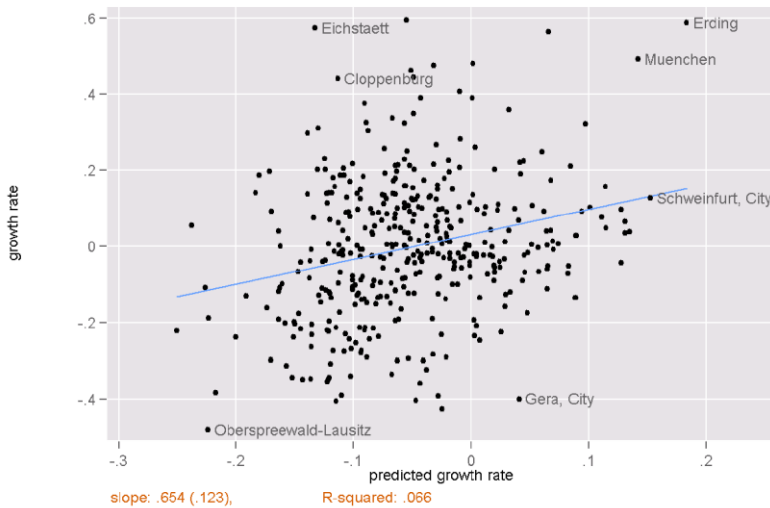
## 2 Measuring national and regional growth

The tool most commonly used to analyse the structural components of regional economic growth is so-called *shift-share analysis*. The basic idea of shift-share analysis is that regional growth can be disentangled into components idiosyncratic to each region and the growth related to the industries located in these regions. Bartik (1991) generalizes this idea and suggests that, in the absence of regional idiosyncrasies, *the rate of regional employment growth* can be calculated using the weighted average of the national growth rates of each industry:

$$\widehat{gr}_r = \sum_{i=1}^N \frac{E_{irt}}{E_{rt}} \frac{E_{it+1} - E_{it}}{E_{it}}$$

where  $E$  denotes the number of employees and the subscripts  $i, r, t$  denote industry, county, and time, respectively.  $\widehat{gr}_r$  (i.e. *the estimated rate of regional employment growth*) is commonly used as an instrument for predicting local employment growth that is not correlated to local characteristics. However, its predictive power is limited.

**Figure 1:** Actual versus predicted regional employment growth in Germany (1994–2014)



The scatterplot of Figure 1 displays the actual employment growth over the period 1994–2014 in 402 German counties (Kreise and kreisfreie Städte) versus the *estimated rate of regional employment growth*; i.e., the weighted average of the national industrial growth rate.

Figure 1 is based on the author's own calculations using the database Establishment History Panel (BHP) by the Research Data Centre of the German Federal Employment Agency and the Institute for Employment Research (IAB) in Nürnberg (BHP 7514). The database classifies economic activities into 222 groups. In this article these groups are called industries or sectors.

The above figure shows that for a wide range of districts, actual employment growth can be predicted with the help of the shift-share model.

For example, counties like Munich and Erding are among the fastest growing regions in Germany. Since they also rank among the regions with the highest predicted growth rate, we assume they had a regional industrial structure similar to the German national industrial structure and also grew in a comparable way to national growth as a whole.

On the other hand, the East German county of Oberspreewald-Lausitz is located at exactly the opposite end of the spectrum: it is the most rapidly shrinking county in Germany in terms of employment, which is precisely what its economic structure predicts. All these regions have one thing in common: they have experienced the same (positive or negative) trend of industrial growth as the aggregate of the country, just at a faster pace.

However, the statistical relationship between actual and predicted growth is positive but weak. The predicted growth rate can only explain 6.6% of the total variation in growth rates. Accordingly, there are many regions that deviate from the rule.

On the one hand, there are counties like Eichstätt and Freising, which rank among the fastest growing regions, but the shift-share instrument predicts negative growth in these counties.

On the other hand, counties like Schweinfurt and Gera exhibit average or low growth (respectively), although they were predicted to grow faster than average.

In sum, these deviations seem to be more the rule than the exception.

The bottom line is that regional industrial structure predicts regional growth only to a certain extent. This is good news for regions that for historical reasons have an unfavourable industrial structure, as they still have the potential to experience exceptional growth in the rate of employment.

## 2.1 Local profiles of industrial change

The previous analysis demonstrated that local industries do not necessarily grow at the same speed and in the same direction as their national aggregates. Growth of local industries is also determined and explained by a wide range of idiosyncratic (e.g. region-specific) components. The interplay of the latter can cause regions to grow even though they were ex-ante specialized in nationally declining industries.

The following equations replicate the procedure proposed by Dauth and Südekum (2016) for German counties in the period since German reunification. Consider the rate of employment growth of a region  $r$ . This rate can be rewritten as the average growth rate of each industry in this region  $w_{ir}$ , weighted by its share in total regional employment:

$$gr_r = \frac{E_{rt+1} - E_{rt}}{E_{rt}} = \sum_{i=1}^N \frac{E_{irt+1} - E_{irt}}{E_{rt}} = \sum_{i=1}^N \frac{E_{irt}}{E_{rt}} \frac{E_{irt+1} - E_{irt}}{E_{irt}} \equiv \sum_{i=1}^N w_{ir}$$

Similarly, the rate of national employment growth  $gr_{nat}$  can also be depicted as the weighted average of the national industries' growth rates  $w_i$ :

$$gr_{nat} = \frac{E_{t+1} - E_t}{E_t} = \sum_{i=1}^N \frac{E_{it+1} - E_{it}}{E_t} = \sum_{i=1}^N \frac{E_{it}}{E_t} \frac{E_{it+1} - E_{it}}{E_{it}} \equiv \sum_{i=1}^N w_i$$

An intuitive measure of whether a region grew faster or slower than the national average is the difference between regional and national growth rates. We can call this the “excess growth rate” of a region:

$$gr_r - gr_{nat} = \sum_{i=1}^N w_{ir} - w_i \equiv \sum_{i=1}^N \Delta w_{ir}$$

Note that in the last equation the difference between the regional and the national growth rates is the sum of the difference of the local industries' growth rates  $w_{ir}$  and their national counterparts  $w_i$ , which is denoted as the excess growth rate of a local industry  $\Delta w_{ir}$ . In other words, summing up the excess growth rates of all industries gives the region's excess growth rate.

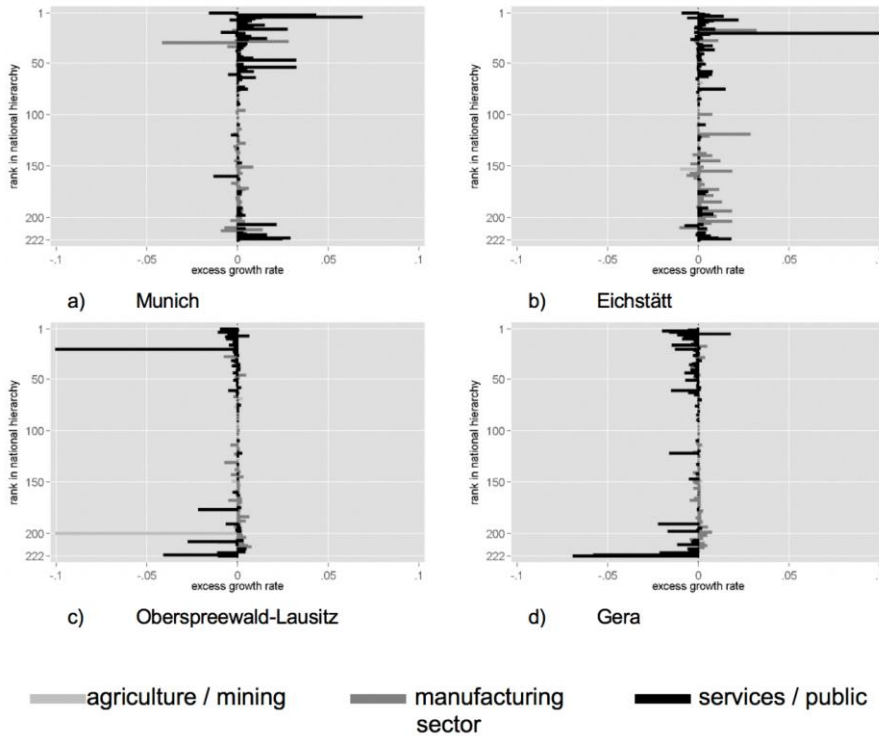
Comparing the excess growth rates of different industries in the same region provides interesting information about the economic development of that region. This is best done

graphically, whereby all of a region's industries are first ranked according to their rank in the national hierarchy of industry growth rates. Then, for each industry, the excess growth rate is plotted against its rank.

As illustrative examples let us explain the growth/decline of employment in four German cities during the period 1994–2014 by examining the different dynamics of their respective industrial structures:

- Munich is the biggest city in the Free State of Bavaria. Employment in Munich has grown at a higher-than-average rate, mainly due to the above-national rate of growth of service industries that also increased on the national scale. In other words, in Munich the excess growth rates for most service industries were positive, a tendency which has determined the shift in the sectoral composition of Munich's economy. As for the manufacturing sector, Munich underwent the long-term trend of deindustrialization much more quickly than the county average.
- Eichstätt is a smaller town in the Free State of Bavaria. Employment in this town also grew, but predominantly in those industries that declined nationally. This is why the shift-share instrument fails to predict this region's exceptional growth. For most industries in Eichstätt, the excess growth rate – which was above the national industry-specific average growth rate – was positive.
- Oberspreewald-Lausitz is a district in the southern part of the State Brandenburg, East Germany. Employment in this district has significantly declined, predominantly in those industries that also nationally declined. Moreover, for some agricultural and service industries in this district the decline was much more significant than the respective national sector-specific averages.
- Gera is the third-largest city in the State of Thuringia, East Germany. Employment in Gera in both nationally growing industries and in nationally declining industries has shrunk. Moreover, for a wide range of service industries in this district the decline was much more significant than the respective national sector-specific average.

**Figure 2:** Profiles of local industrial change in four example regions



\* Notes: The figures display the excess growth rates of local industries ordered by the respective national industry growth rates (fastest growing industries on top). Bars extending to the right denote higher local growth compared to the national average, and bars extending to the left denote lower growth than the national average.

### 3 Conclusion

Shift-share analysis can be used as an initial explanation for regional employment growth. However, in understanding and predicting regional growth, such a top-down approach has its limits. It is also important to account for the idiosyncratic growth potential and weaknesses of the most important industries in a region.

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## Factors and Policy Measures Influencing Local Economic Development: An Overview of the Conceptual Framework

MÁRTA KISS & KATALIN RÁCZ

**Abstract** The aim of this paper is to survey a wide range of publications<sup>1</sup> in order to identify the factors influencing Local Economic Development (LED). We offer a classification of the drivers of LED, including local endowments, collective and institutional behaviour, autonomous economic processes and policy measures implemented by public, private and non-profit stakeholders for promoting LED.

**Keywords:** • factors of LED • settlements • endowment • planning • policies  
• co-operation

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## **1 Towards a standard conceptual framework of local economic development**

Qualitative research, based predominantly on case studies, is the most frequently applied method of analysing local economic development (LED).

Capková (2005) has compared and assessed the local economic development practices of settlements in a wide range of Central and Eastern European countries. In doing so, she identified certain major groups of features and research questions which cover both the political-administrative background and financial-economic dimensions. In her analysis, LED involves measures and incentives in the following major policy areas: attracting external investment and developing the local business environment. Capková (2005) highlights the importance of strategic planning and partnerships by taking into consideration the differences between urban and rural localities and the role of EU subsidies. Capková (2005, 5) has called for the systematic collection of data about LED.

Wong (2002) attempted to develop a quantitative LED indicator system using a 'valuative-theoretical approach' method that was developed along three (social, economic, and physical) dimensions. The author defined an analytical framework consisting of 11 factors (which was later supported by the relevant 11 indicators), the purpose of which was to promote the definition and formulation of policy issues and to facilitate the process of planning and decision-making. The first group of factors is formed by 'traditional' factors such as physical factors, location, human resources, finance and capital, infrastructure, knowledge and technology, and industrial structure. The factors of institutional capacity, entrepreneurial culture, community identity and image, as well as quality of life, are called 'spiritual' (i.e. softer, less tangible factors) by Wong (2002).

Wong (2002) notes that the theoretical and empirical justification of soft (intangible) factors is weaker because the cause-effect relationships between these factors and LED processes are generally unclear, so their measurability is more difficult. She also notes that the exact content of the factors (indicators) is very different from country to country. A corresponding piece of empirical research, an expert survey among LED operatives, was carried out in Great Britain. One of the lessons learnt was that LED practitioners as a rule expect immediate results from traditional LED factors, and activate soft factors only afterwards. Human resources were considered the most important of the former factors (Wong 2002).

Mezei (2008) investigated Hungarian settlements and evaluated domestic local economic development practices and development tools with the help of indicators developed specifically for Hungarian conditions. Her data were collected using a questionnaire method by applying a system of six evaluation aspects, as follows: LED planning, financial situation, enterprise development, partnership, institutional system, and infrastructure development. Here, the investigation of partnership relations was a new

element compared to Wong's criteria (2002) and, according to the results of the research, proved to be a highly influential factor.

Kiss and Racz (2019) evaluated LED strategies of Hungarian settlements using a qualitative case study method. The system of criteria used in their paper is partly based on current theories of economic development and partly on recent trends in evaluation (Wong 2002). In particular, their analysis uses a method characterized by five groups of LED factors which are supported by additional indicators for each of these factors. The following part of this paper offers an overview of these factors.

## **2 The first group of LED factors: main characteristics of the settlement**

These factors are as follows:

- The size of the settlement with special respect to its relative size considering the region's characteristics;
- Determining geographical/locational features, such as the distance from the center of the region, access to labour markets, access to other markets and to suppliers;
- Infrastructure and other physical factors, such as the amount of available land, the accessibility and quality of roads, sewerage and other utilities;
- The determining social characteristics of the settlement and population, such as the number of enterprises, educational level, economic status of the population, etc.

According to the relevant literature, the size of a settlement is a major factor in LED (see e.g. Bennett 1991; Capková 2005; Mezei 2008). Bennett (1991) distinguishes between four types of LED in an international context, whereby settlements are classified according to their size, the focus of LED, and the development model that is followed. In particular, Bennett (1991, 25–26) uses the following classification: 1. Large cities and world cities; 2. Metropolitan areas; 3. Central places with specific hinterlands or peri-urban commuting areas; and, 4. Dispersed rural areas with no accessible local market. Capková (2005, 14) demonstrates that large urbanized cities are much more committed to economic development compared to their smaller counterparts, and this can be explained by their better access both to a wider scope of expertise and to greater financial capacities.

Surveys of Hungarian settlements and the associated analysis have shown that the size of local government determines to a large extent both the possibilities and the practice of local economic development (Mezei 2008; Ritter and Nagy 2017; Molnár *et al.* 2017).<sup>1</sup> In larger settlements, classical economic development programs are being carried out as a rule, while the competitiveness and attractiveness of smaller settlements tend to be facilitated by so-called 'special economic development' programs (Mezei 2008, 57). Settlements in Hungary depend strongly on development resources. Regarding access to development resources, as a rule larger settlements are in a worse position than smaller ones, therefore they are compelled to spend relatively more on economic development

goals from their own budgets. The research also states that co-operation with local businesses is largely dependent on size: the smaller the settlement, the more unlikely and uncertain the partnership between local government and local businesses. Moreover, business-to-local-government relations additionally depend on the social characteristics of the settlement (educational level of the population, labor market characteristics, number and nature of enterprises, etc.) and on the partnership-building skills of local management (Mezei 2008, 53–55). Social characteristics also depend on the history and traditions of the settlement; for example, there are settlements which in the past were populated predominantly by agricultural laborers, and these differ in many respects from other settlements which have a significant entrepreneurial past.

Location-based factors such as access to product markets and suppliers are frequently mentioned in the relevant literature (e.g. Wong 2002, 1837). In Hungary, besides these geographical location factors, labor market conditions are important as well. Location-based benefits are also influenced by the availability of infrastructure, such as transport and communication networks.

### **3 The second group of factors: resource endowment**

This group consists of the following factors of local development:

- The financial resources of the settlement, such as own incomes, state aid, and EU support;
- Human resources, such as qualified administrative or management experts;
- Institutions and organizations engaged in LED such as NGOs, cooperatives, etc;
- Technological resources such as incumbent local industrial installations.

Capital investment is a major driver of LED (Wong 2002; Capková 2005), in spite of the fact that in most cases the flow of finances lies outside the control of local governments. Instead, in this age of globalized finances and all-pervading information technology, significant decisions about investment are taken by transnational corporations (Wong 2002, 1841). Although the exact relationship between financial decentralization and economic development is still unclear, it can be stated that greater financial freedom facilitates local development (Capková 2005). The former author therefore sees a certain level of financial autonomy as one of the most important factors in LED practice. If expectations about increased social responsibilities are coupled with scarce local financial capacities and limited autonomy, this combination of circumstances will result in tension, emphasizes Capková (2005).

Wong (2002) demonstrates the difficulties of assessing institutional capacity and recommends the application of qualitative methods for this purpose. The results of his expert survey show that human resource allocation and institutional capacity are among the most important LED factors. However, some researchers doubt that greater

institutional capacity results in better or more progressive decision making (see e.g. Clarke 1995; Wong 2002).

Capková (2005, 197) notes that local government capacity and the efficiency of policy decisions are more closely related to socioeconomic factors (education, poverty, etc.) than to geographical location. She considers the existence of administrative capacity as one of the key factors of LED because, according to the author's research, the capacity of local government is greatly influenced by the quantity and quality of available local human resources (skilled officials and professionals) (Capkova 2005). Typically, there is an abundance of potentially less skilled employees, but a scarcity of people with adequate qualifications. Therefore, the education of a local professional team should be the focus of economic development. According to Getler and Wolfe (2004), the knowledge management of local society depends on the means by which local actors and institutions meet, and the depth of their communication and co-operation with each other. For an institution to learn, reflexivity and feedback is needed.

Overall, it can be concluded that the availability of institutional and technological capacity and a certain level of qualified human resources are essential for successful economic development.

#### **4        The third group of factors: strategic planning, projects, programmes and other policy instruments of LED**

This group consists of the following factors:

- Supporting measures of the central government, e.g. subsidized projects;
- Various forms of strategic planning, e.g. long-term planning or plans associated with ad hoc programmes / projects;
- Adjusting the application of various development instruments to the selected direction of development objectives (community-focused / business-focused / holistic).

International studies have shown that providing support for private investment and creating jobs are the most typical economic development activities of local governments. However, as recent research shows, there is a growing trend for local governments to initiate activities beyond their traditional role to serve wider social interests, such as supporting minorities, disadvantaged groups, and other vulnerable target groups of local policies. Another example of an LED objective that goes beyond economic growth is striving for a fairer distribution of the costs and benefits of economic development (Morgan 2009, 2). In Hungary, local economic development initiatives are characterized by a strong social orientation (Czene and Ricz 2010; G. Fekete 2011). Frequently, these initiatives are institutionalized as social land programs or social cooperatives (Kiss and Racz 2019).

Local governments can choose from a very wide range of measures to develop the economies of settlements. Surveys conducted on an international level have revealed that the most typical areas of activity are the following: infrastructure development, using real estate for private sector development, supporting businesses, facilitating cooperation and networking, lobbying for settlements, promoting local agendas at the national level, developing and implementing LED strategy, and supporting LED with specific planning exercises and business case development (Pugalís and Tan 2017).

Leight and Blakely (2017, 139–141) identified four roles for local government: coordinating various actors; facilitating action and events that improve the cohesion of the local community; stimulating and promoting the creation of local businesses; and, finally, local governments sometimes also become entrepreneurs or developers themselves. An efficient activity of many local governments is using common land or buildings for economic purposes in order to benefit the community. On the other hand, Capková (2005, 10) has identified the following types of LED instruments: financial instruments, property-related instruments, marketing, infrastructure development and providing technical and information assistance.

Research on approaches to LED in the settlements of Eastern European countries has revealed that most settlements have organized their development concepts around a single project or a few items from projects, but the resulting plans lack a strategic approach and do not serve as an organic and sustainable basis for the development of the local economy (Capková 2005; Mezei 2008). Some researchers have called this approach ‘ad-hoc project-based development,’ and contrasted it with strategic, ‘programme-based development’ (e.g. CCG 2012; Kiss 2018). On the other hand, Bennett *et al.* (2004), following an examination of the new tendencies of the economic development strategies of the United Kingdom, outlined three main directions: ‘community-focused strategies’ which build on the needs of communities, ‘enterprise-focused strategies’, and a combination of these two approaches, also called the ‘holistic approach’.

## **5 The fourth group of factors: co-operation and co-ordination**

This group consists of the following factors:

- The range of local actors involved in LED, such as local government, local businesses, professional associations, civil organizations, etc.;
- The extent and type of co-operation within the municipality and with external stakeholders, and the duration of these forms of co-operation (e.g. long-term co-operation, or co-operation limited to a specific project);
- The methods used to promote co-operation (e.g. top-down, bottom up);
- The styles and means of co-ordination (e.g. paternalistic, and the business approach).

Ritter and Nagy (2017) have identified the range of local actors involved in economic development as follows: local government, local businesses, professional associations, civil organizations, central government, local population, external experts and consultants, higher educational institutions and research centers in the region. According to their results, the actors most involved in local development agree that the key to success is to rely on the expertise of external specialists (such as the government and universities). In practice, the organizations of central government typically cooperate with local governments and with local or regional companies in the field of economic development, while relationships with universities are rare.

The success of local economic development depends on the co-operation of those who control the resources, according to Mezei (2008).

Bennett *et al.* (2004), from an analysis of LED in Great Britain, also highlight the importance of building partnerships. However, the authors also point out that cooperation is not always successful. According to their observations, partnerships between local governments and socially engaged non-profit organizations are more frequent than partnerships with businesses.

Frequently, it is the responsibility of local governments to co-ordinate a wide range of stakeholders of LED. Leight and Blakely (2017) have pointed out that local governments coordinate predominantly the local activities of government agencies, local communities and enterprises. The aim of coordination is to ensure that the above-described stakeholders follow identical aims, and that projects are consistent with state and local policies. According to the authors, coordination between state and local governments in issues of LED is more efficient on a regional level than on a local level; and regional organizations of local governments can be catalysts in this process (Leight and Blakely 2017, 140). Capková (2005) emphasizes two types of governance: 'paternalist', and the 'business' approach. In her opinion, the latter approach is more desirable. However, case studies of LED strategies investigated in Hungary have proved that a paternalistic approach to leadership can work under certain conditions (Kiss and Racz 2019).

## **6 The fifth group of factors: innovation and sustainability**

This group consists of the following factors:

- Innovative LED methods, solutions, and processes;
- Factors and predictors of sustainability (identification of needs, long-term strategies, a combination of funds, the improvement of participants' knowledge and competences, networking, mobilization of the local community, monitoring of innovative solutions).

Technological innovation and knowledge infrastructure are important competitive forces in economic development (Schumpeter 1934; Wong 2002). Empirical research has

demonstrated that regions and settlements where the competitive advantage of actors is based on innovative ideas maintain their position permanently in the long term. On the other hand, in the competition between territories those actors which rely on outdated technologies, sectors, institutions and organizational processes fall behind (Bajmócy 2011; Lengyel and Bajmócy 2013).

From an analysis of innovative methods, solutions and processes for LED, Bajmócy (2011) highlights that the content and focus of local innovations always appear as a specific combination of local challenges and endowments. Lengyel and Bajmócy (2013) emphasize that local governments involved in local development play a key role in coordinating the interactive learning processes of local actors and in disseminating innovation.

G. Fekete (2013) investigated innovative LED solutions in the EU. According to her overview, innovations can be embodied:

- In new partnership agreements;
- In tailor-made training;
- In new ways of promoting training activities and institutions;
- In the resourceful organization of advocacy and public services;
- In novel approaches to employing and re-employing unemployed persons;
- In creating jobs for members of vulnerable strata of society (e.g. for disadvantaged people in local public institutions);
- In the promotion of self-employment by setting up consultancy services;
- And in facilitating non-market modes of local exchange and trade, e.g. developing markets and services of the social economy.

Keller *et al.* (2016) investigated the conditions of the long-term viability of community economic development programs and found that the sustainability of these types of local development programs depends essentially on the structure and size of the associated networks of stakeholders. Complex programs with multiple goals and complex systems have greater potential for sustainability if the network of participants is powerful and heterogeneous. Németh (2014) evaluated local development programs that proved to be sustainable in the long term and found that such programs had in the first place responded to local challenges and had met local needs by using local resources.

Picciotti (2017) examined the conditions of sustainability of social enterprises involved in local economic development. In particular, he investigated the mission statements of these organizations and found that organizations that proved to be sustainable were those which actually succeeded in contributing to solving the problems which gave birth to the organizations in the first place. Sustainable social enterprises were able to generate additional local development projects and became the driving forces behind sustainable local development. According to the author, sustainable operations are primarily driven



by the following factors: the accurate identification of needs, continuous improvements in participants' knowledge and competences, efficient networking, mobilization of the local community, and continuous learning about organizational solutions, models and developmental pathways from other organizations.

#### Notes:

<sup>1</sup> The following publications offer a wider overview of LED: Syrett (1995); Bartik (1991); Bennet *et al.* (2004); Pearce and Mawson (2003); Tello (2010); Pugalís and Tan (2017); Capkova (2005); Mezei (2008); G. Fekete (2013); Ritter and Nagy (2017).

<sup>1</sup> Molnár *et al.* (2017) point out – among other things – that farm size and expertise are related to each other: in the case of economic development programs for employment in larger settlements, there is already a need for a type of expertise (managing people and small businesses) which is usually not provided by an ordinary mayor or office worker.

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## **Legal and Institutional Arrangement**



## Comparative Local Governments in Europe

SIMONA KUKOVIČ & MIRO HAČEK

**Abstract** Local authority in Europe is a product of centuries-old tradition. Stoker (1991, 1) even says that local government is a key element in the political system of European liberal democracy, civilizational acquisition, and also a theoretical and practical component of any modern democratic political system. The most basic definition of local authority is that it is the level of government closest to citizens and has the task of representing the significance and views of the locality. In Europe, diverse and different arrangements or designs of local authorities have developed which differ both in scale, structure, and tasks, as well as in terms of their relations with regional and national levels of authority. A common feature of these systems is how they originated from their own traditions and historical forms of development. The second part of this featured chapter will concentrate on the prevailing typologies of local government that can be used in comparative research about local authorities in different national settings. On the one hand, there are many typologies which can be used in academic discussions; on the other hand, their usefulness is somewhat questionable because none of them cover all countries – for instance, many of them do not include the "new democracies" of Central and Eastern Europe.

**Keywords:** • local government • community • typology • European Charter of Local Self-Government • Europe

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## **1 Introduction: The European Charter of Local Self-Government as the foundation**

Local authority is a product of centuries-old tradition in Europe. Stoker (1991, 1) even claims that local government is a key element in the political system of European liberal democracy, a civilizational acquisition, and a theoretical and also practical component of all modern democratic political systems. The simplest definition of a local authority is that it is the level of authority that is closest to citizens and has the task of representing the significance and views of the locality. The exercise of local government is a demanding task which relates primarily to the division of powers between the state and local communities (Brezovšek *et al.* 2008, 120). We may talk about local government only if the state recognizes the legal existence of local communities, grants them the right to decide about certain issues – which it does not interfere with –, and provides them with the necessary means for regulating these matters. Greer *et al.* (2005, 11) define three of the most important normative elements on which local government is based in Europe. The first element is autonomy, which indicates the degree of decision-making power between the central and local authorities. The degree of decision-making at the local level prevents the concentration of political power at the central level and allows for different political choices in different local environments. The second element is democracy, which defines the local authority as a political platform, and opportunities for citizens' participation. The existence of local government promotes the population's participation in managing local affairs. The third element is efficiency, since local authorities are more efficient at providing public services and finding solutions to local problems and adapting measures to local conditions.

The diversity of regulations or models of local authorities is respected in the European Charter of Local Government, which is the basic document and European standard for local authorities, as well as the standard for the basic democratic system institutions in the European Union Member States. The European Charter of Local Government was drawn up by the Council of Europe and has significantly contributed to the development of local authorities and local democracy. It was adopted on 15 October, 1985 in Strasbourg, and entered into force on 1 September, 1988, when it was ratified by the first four Council of Europe member states.<sup>1</sup> By ratifying the European Charter of Local Government, countries commit to adhering to the principles and rules of the Charter. Thus, the countries that have ratified the Charter must ensure the legal basis of local government through a national normative framework, meaning that the status of local government must be recognized in national legislation. Countries need to clearly define the field of activity and the structure of local government in terms of methods and criteria for allocating competences. At the same time, they also define the capacity of local authorities to manage a substantial proportion of public affairs through their councils (consisting of democratically elected representatives), their executive bodies, and internal administrative structures with own staff. Local authorities should be provided with appropriate financial resources (namely, their own resources and property), the right to collect local taxes, a system of financial equalization, a grant system, access to capital



markets, and resource management. Local authorities must have a guarantee of autonomy, which is reflected in the status of elected representatives, the protection of borders of local communities, the restriction of control over local community and judicial means. They must also enjoy the right of association and the principle of consultation, which involves the participation of local communities. If intermediate levels between local government and the national authority are introduced, it is necessary to ensure the democratic functioning of these levels in accordance with Article 13 of the Charter (1985). Finally, it is necessary to ensure the realization of political rights, which is reflected in the right to vote and the democratic electoral process, freedom of expression and association, the right to inform citizens and their participation in all forms of local democracy (Brezovšek and Kukovič 2015, 218–219).

Among the main objectives of the Charter (1985), which are laid out even in the preamble, the following are included: the creation of effective local governance which is as close as possible to citizens and, in accordance with the principles of democracy and the decentralization of power, a focus on cross-border cooperation, strengthening inter-municipal relations, and removing administrative and technical barriers to cross-border cooperation, and achieving a higher level of communication in the administrative field and respecting the principles of democracy in terms of the rights of citizens to participate in the management of public affairs.

In the third article the Charter (1985) defines local self-government as the right and ability of local authorities to regulate, within the limits of the law, a substantial proportion of public affairs within the framework of their tasks and for the benefit of the local population. This right is exercised through councils and assemblies consisting of members elected by free and secret ballot on the basis of direct, equal and universal suffrage. More precise activities are defined in the fourth article of the Charter (1985), which is based on six important principles:

- The basic competencies and tasks of local authorities are prescribed by the constitution or by law. This provision does not preclude the transfer of powers and special-purpose tasks to local authorities in accordance with the law;
- Local authorities have the freedom to exercise their own initiative about every matter that is not excluded from their jurisdiction or is not the responsibility of any other authority;
- Public tasks should, if possible, be implemented by those authorities that are closest to citizens; the assignment of a task to another authority should be justified by the scope and nature of such task, as well as the requirements of efficiency and effectiveness;
- The competencies awarded local authorities must be complete and exclusive, and they should not be undermined or restricted by central or regional authority, unless determined by law;

- In the powers delegated to them by the central or regional authorities, local authorities (as far as possible) have to be given the freedom to make decisions about how to adapt their implementation to local circumstances;
- As far as possible, local authorities must be promptly and appropriately consulted about their opinions when planning and deciding in all matters that directly affect them.

In addition to the principles listed in the analysis of the provisions of the European Charter of Local Government (1985), we should not overlook the ninth paragraph, which regulates the field of financial resources and principles that should be observed. The first is the principle of relevance, which provides that local authorities, within the framework of national economic policy, are entitled to adequate financial resources which they may freely dispose of within their jurisdiction. The principle of proportionality provides that the financial resources of local authorities must be proportionate to the tasks laid down by the constitution and the law. At least some proportion of the financial resources of local authorities must originate from local taxes and contributions, the amount of which can be determined by the local authorities themselves. This is the essence of the principle of self-financing. The flexibility principle states that the financial systems by which resources are made available to local authorities should be sufficiently diverse and flexible that, as far as practicable, they are in accordance with the evolution of the actual cost of carrying out their tasks. In order to protect financially weaker local communities, the principle of equalization is applied, which provides that it is necessary to introduce procedures for financial equalization or other appropriate measures to correct the effects of the unequal distribution of financial resources and the financial burden they involve. Such procedures or measures, on the other hand, must not diminish the freedom of decision-making of local authorities in their field of jurisdiction. The principle of cooperation is to be implemented in such a way that local authorities need to be consulted about the appropriate way to allocate redistributed resources. The principle of autonomy relates to subsidies or grants to local authorities that should not, as far as possible, be strictly dedicated to financing certain projects. The provision of such resources should not interfere with the fundamental freedom of local authorities to freely decide within their own jurisdiction. Finally, the principle of borrowing is highlighted, which holds that local authorities should have full access to the domestic financial market when taking out loans for larger investments, within the limits of the law.

In the twentieth century local government systems in Europe made tremendous progress, and the European Charter of Local Self-Government (1985) may be thanked in large part for that. Local authorities have become a democratic indicator of particular political systems and have contributed to stability and security in Europe. The principle of subsidiarity, which represents the decentralization of public affairs or competences to the most appropriate (as close as possible to the citizen) level has established itself again and played a decisive role. The principle of subsidiarity is crucial for understanding the role of local authorities in contemporary democracies, since it is a fundamental philosophical principle of modern local governments, a way of thinking, and also a fundamental

criterion for the critical assessment of local government in any particular country. In institutional, administrative and organizational terms, it means constant reflection on the division of competences with regard to the organization and decision-making of public affairs and the means of their implementation. Of course, the focus of attention is on the citizen, who is equipped with modern rights and freedoms. The principle of subsidiarity thus aims at constantly balancing the freedom of the individual and various authorities. However, the state and international institutions, especially the European Union, must take into account the role and position of local and regional authorities in each country. Under international law, the principle of subsidiarity is a fundamental principle of European integration, but it is not only related to the vertical division of power or public affairs to local, regional and national authorities, but also to the issues of protecting the autonomy and freedom of the individual, the size of local communities, their funding, the functioning of local administrative apparatus, regionalization, etc. (Vlaj 2005, 26). Although subsidiarity is a dynamic concept, it needs to be interpreted in line with the changes that are taking place in society, the institutional structures of the EU member states, the international environment, and technology. The Maastricht Treaty defines the European Union as an association in which decisions are taken as close as possible to citizens and, from this point of view, local and regional authorities play a central role because they are close to European citizens and are a key factor in the future implementation of European Union initiatives and regulations (Brezovšek and Kukovič 2015, 220–221).

## **2 Typologies of local government systems**

Local government systems are usually perceived and studied as independent variables in dealing with (possible) differences in human resources patterns, professionalism, the role of mayors in local and multi-level governance arrangements (vertical and horizontal networking), the interpretation of the notion of democracy, as well as (de)centralization and attitudes towards the modernization of the public sector (Heinelt and Hlepas 2006, 21; Brezovšek and Kukovič 2012, 27). Making a decision about the most appropriate typology of local government system that could be used in comparative research into local authorities in different countries is problematic. On the one hand, there are many typologies that can be used in academic debates; on the other hand, their usefulness is questionable because none of them cover all countries – many do not include the "new democracies" of Central and Eastern Europe. Thus, it is essential that existing typologies are adapted and updated (Heinelt and Hlepas 2006, 21; Brezovšek and Kukovič 2015).

## 2.1 The vertical power dimension

One comparative analysis of local authorities uses different divisions of the vertical power dimension or the division of powers between local and higher levels of government. For example, Bennett (1993; Kukovič 2011, 60; Kukovič 2015, 33–34) distinguishes between (1) a *dual structure*, where on a local level both local governments and state agencies simultaneously operate, but with different competencies (example: United Kingdom); (2) a *fused system*, where local authorities and their competencies are defined both locally and by a higher level of authority (for example: Poland, Czech Republic, and Hungary); and, (3) a *mixed system* (the case of Denmark and Sweden). Bennett (1993) classifies the new democracies of Central and Eastern Europe (Hungary, Poland, and Czech Republic) as having fused systems. In the past, this typology was not widely accepted, since all European countries were classified as having fused systems or moving towards the fused system, with the exception of the United Kingdom (dual structure) and Denmark and Sweden (both mixed systems). Such a typology was also considered to be too simple to take into account differences not only connected to some aspects of vertical power relations, but also in conjunction with the possible effects rising from these relations. In addition, fused systems have undergone radical changes in past decades – in many countries, territorial reforms (new levels of government, amalgamations, etc.) and functional reforms (decentralization, devolution, new public management) have been implemented, which has increased the differentiation between such systems (Kersting and Vetter 2003; Kukovič 2015).

Page and Goldsmith (1987), and later, John (2001) make a distinction between the *Northern* and *Southern* European countries on the basis of three indicators. For the first time, they distinguish according to the number and type of functions assigned to the subnational authority; second, the legal discretion open to local policy makers; and third, the access of local politicians to central authority (John 2001, 26). Their key idea is that there is an inter-relationship between these indicators. It is clear that the policies that are enacted, as well as the corresponding leadership roles which are to be assumed by the mayors, vary greatly depending on the pattern of this interaction. The proposed dichotomy of local government systems claims that the Southern European systems are characterized by municipalities with some functions and competencies, a low level of legal discretion, and the significant access of local politicians to the central (and regional) level. In other words, local politicians can have a strong influence on the central level of authority, but they represent politically weak municipalities. On the other hand, Northern European systems are marked by the strong decentralization of functions, a high degree of discretion, and the low access of local politicians to the central government.

The reasons for the differences between the countries in Northern and Southern Europe have their roots in the historical development of the latter. In Southern Europe, a model of the Napoleonic state spread across all modern national countries which developed a unified administration throughout their territories, and managed the country's educational systems directly from the country's capital. The central authority looked at local elites

with mistrust and therefore built its own territorial organization with a directly established administrative body. In the twentieth century, social states began to appear in Southern Europe, creating new competencies for central authorities. Local authorities thus far have embodied local cultural and political identities which are represented at higher authority levels through local politicians, who mostly act as local patrons and use different networks to access national and regional centers of political power in order to represent local affairs (Page 1991; John 2001). High accessibility and low legal discretion are linked to the tendency of actors (both local and national politicians and central and regional officials) to exist within big and dysfunctional bureaucracies. The purpose is to exploit uncertain areas through extortion and/or using clientelist-networking techniques. Local politicians are forced to act within a given framework of territorial representation and political localism. The size of local communities is still small, because within a given context, community identity has been more important than the effectiveness of public services. Southern European countries therefore have many levels of authority – partly as a means of increasing the potential for territorial representation (Brezovšek and Kukovič 2012, 29–30; Kukovič 2015, 34–35).

In the Northern European countries of the eighteenth and nineteenth centuries, central (state) power did not develop a centralized bureaucracy but, along with local elites, implemented national policies (Page 1991). Education was decentralized – under the jurisdiction of local institutions – and in many countries the Protestant church remained part of the state. Strict and impartially enforced national legislation, as well as a professional and effective civil service, secured the unity of modern statehood. Later, when countries responded to demands for equality, legal entitlement and social security, a social protection system was established whereby local authorities were responsible for social public services. Northern democracies, based on the independence of power of the local level to decide on important issues, developed a theory of local government which became the "small political system" (John 2001, 30). Local politicians had to achieve results, notably through the use of local resources and with an emphasis on providing local public services. Since the early 1950s many municipalities have merged, thereby increasing efficiency and providing better public services. In the countries of Northern Europe there are only a few levels of authority (Heinelt and Hlepas 2006, 23–24; Brezovšek and Kukovič 2012, 30; Kukovič 2015, 35–36).

This typology of the local-level governance of Northern and Southern Europe has clear advantages: it is simple, and it avoids a legalistic approach, typical of traditional typologies – the old institutionalism, that has long prevailed in comparative analyses of governments, including the analysis of local authorities. Instead, this typology clearly opens up space for reflection and inspires sociological and, above all, historical institutionalism. Naturally, there are also some disadvantages: Page and Goldsmith (1987) only studied Sweden, Norway, Denmark, the United Kingdom, France, Italy and Spain (unitary states), but did not take into account the federal systems of Germany, Austria and Switzerland. In a later study, John (2001, 35), following the example of the typology of Page and Goldsmith, also included Belgium, Greece and Portugal into the

southern group, and Finland, Ireland and the Netherlands in the northern group, but Germany and Switzerland were again excluded. Furthermore, at the time when Page and Goldsmith's (1987) typologies were originally developed, the countries of Central and Eastern Europe could not be included in the analysis; later, John (2001) confined himself only to classifying the countries of Western Europe. At this point, the question arises whether the similarly classified group of countries, especially the northern group, would become more heterogeneous if other countries were also included in the analysis (Heinelt and Hlepas 2006, 23–24; Brezovšek and Kukovič 2012, 30–31, Kukovič 2015, 36).

In a slightly later study, Goldsmith (1992, 395) developed a typology of local governments based on the goals or principles emphasized by a particular model:

1. The *clientelistic/patronage model* strongly assumes that the primary task of local politicians is to ensure that the interests of the community are well supported (in respect of special public goods and services), and are represented at higher levels of government (this model is represented by France, Italy and Greece);
2. The *model of economic development*<sup>2</sup> assumes that the most important task of local government is to promote the economic development of the city; basic services and citizen protection (fire safety, police and transport networks) form the basis for creating development policies; local politicians are also expected to strengthen local economic development (as represented by the United States of America);<sup>3</sup>
3. In the *model of the welfare state*, the effective exercise of public services (in conjunction with national standards of equity and redistribution) has been shaped by local governments; usually local interests are not only represented through individual representatives, but through local government associations at the national level; local politicians are expected to be good managers; in addition, the effective provision of public goods places great emphasis on paid and professional civil servants, which is criticized by some as local bureaucratic paternalism (representatives of this model include Germany, the Netherlands, the UK, and the Scandinavian countries);
4. In some welfare states (especially in the United Kingdom), a *consumer model (market-enabling model)* has been developed based on the experiences of the United States of America, in which local authorities have moved away from the role of service providers in order that public services may be delivered (either alone, or in cooperation with the local administration) by other agencies; the main difference compared to the model of economic development lies in the fact that local authority is limited in such a way that it allows only assumes functions related to market mechanisms for the economic development of the city (Heinelt and Hlepas 2006, 24–25; Brezovšek and Kukovič 2012, 31–32; Kukovič 2015, 36–37; Brezovšek and Kukovič 2015, 226–227).

The above-described typology, based on the criteria of the specific objectives and principles of a particular model, certainly represents an interesting perspective, but these criteria are not enough to permit a final classification of local governments: the so-called clientelist model is (no longer) suitable for applying to all metropolitan municipalities of

Southern Europe, since instead of this a model of economic development has emerged. In addition, in the municipalities of Northern Europe the dominant model is a mixture of welfare state and consumer model (Heinelt and Hlepas 2006, 25; Kukovič 2015, 37).

Hesse and Sharpe (1991) have responded with their typology to the issue of greater heterogeneity in groups when other countries are added. Their typology of relations between local and central authorities is a convincing synthesis of the aforementioned typologies. Hesse and Sharpe (1991) make a distinction between three types of local government systems that reflect both the division of powers in the provision of public services, as well as political power and influence at the local level compared to a higher level of government. In addition, they divide the Northern European group of Page and Goldsmith (1987) into two parts, and include a larger number of countries. (1) The first component of their typology is a *Franco group*, characterized by the fact that the local authority covers territorially defined communities and forms territorial structures for the dissemination of interests at a lower level of governance. The mayor is expected to represent the interests of his local community at higher levels of governance. This group includes France, Italy, Belgium, Spain, Portugal and Greece. (2) The second cluster is an *Anglo group*, including the United Kingdom and Ireland, as well as Canada, Australia, New Zealand and (in some respects) the United States of America. This group is characterized by the weak legal and political status of local authorities which are nevertheless important in the shaping and delivery of public services; local authorities therefore have more of a functional role than a political one. The weak formal political status of a local government must be considered in accordance with the principle of the national supremacy of parliament; that is, its central role in the unitary political system. This is also reflected in, on the one hand, the weak position of the mayor as a political leader and, on the other, the power of municipal administration and councillors in relation to the provision of public services. (3) The third group is a *Nordic and Central European group* and includes the Scandinavian countries, Germany, Netherlands, Austria and Switzerland. In this group there is strong emphasis on the shaping and implementation of public services by local authorities (comparable to the Anglo group). Local government is thus institutionalized (with a strong constitutional position and relatively high levels of financial independence) as an autonomous decentralized level of policy making (Heinelt and Hlepas 2006, 26; Kukovič 2015, 38; Brezovšek and Kukovič 2015, 227).

A similar typology is offered by Loughlin (2001, 5), who distinguishes between the *Anglo-Saxon group* (the United Kingdom, United States, Canada (excluding Quebec) and Ireland), the *Germanic group* (Germany, Austria, the Netherlands, Spain (after 1978) and Belgium (after 1988)), the *French group* (France, Italy, Spain (before 1978), Portugal, Quebec, Greece and Belgium (before 1988)) and the *Scandinavian group* (Sweden, Norway, Denmark and Finland). This typology includes and emphasizes broader aspects of a country's traditions – such as relations between the state and society, policy styles, prevailing approaches to the academic disciplines of public administration, and others – and is not focused solely on central-local power relationships. The latter links to only one component of Loughlin's typology (2001), which is the dimension of the form of political

organization and the form of decentralization, so we do not analyse this typology more precisely.

Both typologies – Hesse-Sharpe (1991) and Page-Goldsmith (1987) – share a common deficiency; namely, the exclusion of the new democracies of Central and Eastern Europe. Although these countries have some characteristics in common with the countries of the North and Central European Group (with regard to local jurisdiction, and the fiscal and financial discretion of local governments), theoreticians (for example, Hesse and Sharpe 1991) do not classify them into existing typologies due to their historical specificities<sup>4</sup> and, in particular, due to their new radical decentralization, but rather classify<sup>5</sup> them into a special group called the Central and Eastern European Group.

## 2.2 The horizontal power dimension

In analysing the horizontal division of power, the typologies of local government systems focus on the relations between the local legislative council and the mayor and civil servants, and allow for relevant observation (Kukovič 2011, 62–63; Kukovič 2015, 45). Researching the differences in the roles and responsibilities of the mayor, the council, and the municipal administration is important because they can be cross-examined according to the three (or four) types of local government systems already described (Hesse and Sharpe 1991), and the differences between them may even be highlighted (Heinelt and Hlepas 2006, 29). The overall general difference is reflected in the legislative division between the legislative and executive functions. From an institutional viewpoint, we can identify three main types among European local government systems. Their institutional characteristics, according to Wollmann (2008, 280–283), are summarized in the following dichotomies.

### *1. Monistic competence model versus dualistic competence model*

The distinction between the monistic and dualistic competence model of local government is based on the distribution of competencies and responsibilities between the elected municipal council and the municipal administration. In the dualistic system, functions are separated; in the monistic system functions are united. More specifically, in the monistic model of local government, the elected municipal council is the highest decision-making body; and the municipal administration, without the authority to autonomously decide, only acts in accordance with the instructions of the municipal council which also supervises the administration. The monistic (competence) model has historical foundations in the English and Swedish systems of local government. In a dualistic system, the elected municipal council is recognized as the main policymaking body, but the head of the municipal administration has certain competencies to make decisions that do not originate from the municipal council. The dualist (competence) model developed in France during the French Revolution. It is based on the revolutionary municipal legislation of 1789, insofar as the organization of French local authority was made similar to the local parliamentary system since the distinction between the legislative municipal council and the executive function occupied by the elected mayor



(Moreau 2002, 76) was introduced at that time. While French revolutionary innovation (in all respects) was short-lived, the dualist (competence) model became the basis for local government systems in some continental European countries, such as Germany (Wollmann 2008, 281).<sup>6</sup> This classification can also be used to explore additional differences; for example, (1) the role of the mayor in the implementation (or lack) of an executive function; (2) the performance of the executive function independently or together with the collective body; and (3) the manner in which the mayor is elected (Wollmann 2004, 151–152; Kukovič 2015, 45–46; Brezovšek and Kukovič 2015, 229).

## *2. The uniform task model compared to the dual task model*

The second classification distinguishes between a single and a dual model of tasks. In a single model of tasks, all tasks that are designated as local, original tasks are exclusive decisions of an elected municipal council, which is also responsible for these public tasks. Such a system can be observed in Sweden and other Scandinavian countries, and is linked to the English system of local authorities in terms of how activity which follows tasks is assigned to local authorities by a parliamentary act (for example, decisions about issuing building permits, which is a task of the municipal council). There are two types of tasks in the dual model. First, the original tasks that originate from the traditional general powers of the local government (in accordance with the applicable jurisdiction legislation) and for which (as in a single model of tasks) the elected municipal council is responsible. Second, local authorities perform delegated tasks assigned to them by the state (central authority) for which the executive body of the local government (mayor) is responsible. The foundations of the dual model of tasks can be found in French local legislation of 1789, in which the mayor was given a dual role – he acted as a representative of local interests and also as a representative of the state. Similarly, we can identify the features of the dual model of tasks at the beginning of the nineteenth century in the municipal legislation of the German states; this also became an integral part of the German-Austrian tradition of the local government, later spreading to the local government systems of Central and Eastern Europe.<sup>7</sup>

In the dual model of tasks, we talk only about false (instead of true) municipalization or administrative decentralization; in contrast, the single model of tasks is characterized by true municipalization or political decentralization. The transfer of jurisdiction in the case of false municipalization or administrative decentralization has important consequences for municipalities, which are reflected both in the internal relations between the municipal council and the executive authority (the mayor), as well as in external relations with the state. From the viewpoint of internal relations, only the local executive body (the mayor) is responsible for the implementation of delegated tasks in a false municipalization, while the elected municipal council (at least formally) cannot influence the implementation of these tasks. From the viewpoint of external relationships, the local government is subject to functional (administrative) supervision, which goes beyond legal control and also addresses the suitability of local activities. The opposite is the case in true municipalization (political decentralization), since the elected council is the highest decision-making body in internal relations, while the external relationship of the local

government with the state is based only on the legal supervision of state. Although the described relationships are often blurred in practice, this distinction is important, especially in the case of conflicts (Kuhlmann and Wollmann 2014, 248–249; Kuković 2015, 47–48).

### 3. *The separationist model versus the integrationist model*

The distinction between the separationist and integrationist model refers to the relationship between central and local governments and could also be classified using the previously described dimension of vertical power. However, since this division connects a single model of tasks and a dual model of tasks, it is classified as a horizontal power dimension. In a single model of tasks, the control of the central authority over the performance of the tasks of the local government is usually limited to supervision over legality. This means that, both institutionally and functionally, local and national levels are divided, which in the academic literature is also described as the separationist model. The Swedish system perfectly corresponds to the separationist model (the control of the Swedish central government over local governments is very loose, with minimal interference in operations). The English local government system was also characterized by a separationist model during the late nineteenth century, but later (during Thatcherism) increasingly took on the elements of the dual model of tasks, since the central government received the competence to strictly oversee local governments, as well as the possibility of intervening intensively in their operation. When performing the transferred tasks in a dual model, the local government falls under the control of a central government, which usually does not only involve reviewing the legality of operations, but also covers the relevance, achievements and efficiency of the tasks. This type of central government supervision over local government tends to combine both the institutional and functional levels to the point where the local level is incorporated into the central one. The latter concept is described in the academic literature as the integrationist model (Wollmann 2008, 282).

On the basis of the three model dichotomies described above, Wollmann (2008) proposes a typology of two groups (families) of countries; namely, the *English-Scandinavian family* (illustrated by England and Sweden), which has a rooted monistic competence model and the foundations of a single model of tasks and is historically connected to a separationist model (which no longer applies to the English system). The second group is a *European continental family*, illustrated by Wollmann (2008) using France and Germany, characterized by a dualistic competence model and a dual model of tasks, with inclination towards an integrationist model.

The next typology is summarized by Bäck (2005, 82–83; see also Heinelt and Hlepas 2006, 30), who (on the basis of a comparative constitutional analysis of national governments and taking into account the differences between the monistic organization compared to the dualistic, and majority decision-making compared to the consociational form of democratic decision-making at the local level) proposes a differentiation between the *assembly government*, *parliamentarism*, *presidentialism*, and *semi-presidentialism*.<sup>8</sup>

In the model of assembly government, the executive is in the hands of a proportionally assembled committee of the assembly: this represents monism in conjunction with consociationalism. This model can be found in the pre-reform era in Sweden, Norway, the United Kingdom and Poland. In the parliamentary model, the executive is in the hands of a collective body appointed by the council, but the collective body is not drawn up proportionally, but following (with some deviations) the majority principle. This involves a combination of monism and majority decision-making. The parliamentary model is typical of Italy and the Netherlands before reforms, and after reforms for Sweden, Norway and for some cities in the United Kingdom (for example, Bristol). The model of presidentialism is characterized by a combination of a dualistic and majority principle in the context of a separately elected mayor who appoints his cabinet regardless of the political composition of the council. The model of presidentialism is characteristic (after reforms) of Greece, Italy, New Zealand and Poland, and also some cities (for example Stoke-on-Trent) in the United Kingdom. The model of semi-presidentialism is found after reforms in the Netherlands and in some cases (for example, Hannover and Heidelberg) in Germany. For semi-presidentialism it is characteristic that a collective executive body, appointed by the council, surrounds the mayor. This represents a combination of dualism and consociationalism or majority decision-making, depending on how the council appoints this collective executive body.

The difference between a monistic and dualistic system is not always as clear in practice as it may seem from a legal point of view. This is especially true when executive functions are contained in different committees, or where, in a dualistic system, the local council can intervene in administrative matters and, consequently, in executive functions. Moreover, it should be emphasized that majority and consociational forms of decision-making do not depend only on the formal (legal) rules defined in municipal statutes, and/or on the electoral system. Instead, they rely on a socially determined and locally accepted *relevance logic* (March and Olsen 1989), or even on a pragmatically oriented political *effects logic*, taking into account the actual relationships at the local level. The latter also served as background for the development of Bäck's (2005) typology, but does not take into account the systematic relations between the political organization and the administration (Heinelt and Hlepas 2006, 30; Brezovšek and Kukovič 2012, 34–35; Kukovič 2015, 49; Brezovšek and Kukovič 2015, 232–233).

Based on consideration of institutional factors, Mouritzen and Svava (2002) have also developed a typology of local government systems aimed at the horizontal power dimension. Mouritzen and Svava (2002) describe apex leadership as the contact between civil servants at the top of the administrative sphere and politicians at the top of the political sphere. They assume the possibility that both groups keep a distance and carefully manage the exchange of resources with other groups. But it is also possible that there is a positive correlation between the two spheres, thus creating the combined leadership of civil servants and politicians (Mouritzen and Svava 2002, 7; Kukovič 2011, 63; Kukovič 2015, 51). The idea of the apex comes from Peter Self (1972, 150–151), and describes the events at the apex as a mix of leadership; this may be visualized as an arch

whose left part represents a political process, and whose right part represents the administrative process. At the apex of the arch there is contact that represents the critical point at which the political and administrative flows meet, and where the political and administrative influences that were created at lower levels blend together.

The reasoning of Mouritzen and Svava (2002) is based on the hypothesis that the structural features of a local government in a particular country reflect a balance or compromise between three organizational principles; namely, the *rule of the people* (unprofessional public), *political leadership*, and *professionalism*. Mouritzen and Svava's (2002) typology is based on four models:

1. First is the model of a *strong mayor*, which is characterized by a situation in which the elected mayor oversees the work of the majority of the municipal council and is also fully responsible for all executive functions. The director of the municipal administration performs tasks determined by the mayor; thus, he is subordinate to the mayor because he can recruit and dismiss him without the consent of other politicians or political bodies. In addition to the director of the municipal administration, the mayor can also employ political advisers who assist him in performing his duties. In this form of government, the principle of political leadership is strongly emphasized.
2. Second is the *committee leader model*, in which one person is an obvious political leader of the municipality and can (but may not) have the title of mayor. A political leader can have control (or not) over the municipal council. In this model, the executive powers are divided. A political leader may be responsible for some executive functions, while for others the collective body is competent; i.e., standing committees, consisting of elected politicians and the director of the municipal administration. In this model there is a uniform mix of all three organizational principles.
3. In the *collective model*, the decision-making responsibilities are in the hands of the collective body, the executive board, which is responsible for all executive functions. The executive committee consists of elected local politicians and the mayor, who presides over the committee. The greatest emphasis is placed on the principle of the rule of the people (members of the collegial body are elected by the people), while the principles of political leadership and professionalism adapt to this.
4. In the local *council-manager model*, all executive functions are in the hands of a professional administrator (city manager), appointed by the local council. Although the council has general policy oversight, its scope is limited to administrative matters. The local council is a relatively small body; the mayor, who formally presides and is responsible for ceremonial functions, manages the council. The emphasis is put on the principle of professionalism, while the principles of the rule of the people and political leadership are limited (Mouritzen and Svava 2002, 55–56; Kukovič 2011, 66–67; Kukovič 2015, 53–54; Brezovšek and Kukovič 2015, 236–237).

Mouritzen and Svara (2002) conclude that the strong mayoral model is formed in countries with a relatively small local public sector and relatively small organizations. The committee leader model is present in countries where local governments play a very important role (Sweden and Denmark), but also in countries in which the role of local government is moderately important, but serves a very large population (the United Kingdom). As a result, the directors of municipal administrations in these countries lead large organizations. For a collective model, relatively small organizations are typical. The council-manager model is found in countries with a small to moderately large local public sector where organizations employ 100 to 200 public employees (Brezovšek and Kukovič 2012, 42; Kukovič 2015, 55).

**Table 1:** Groupings of countries according to Mouritzen and Svara's (2002) typology

Model	Countries
Strong mayor model	France, Germany (without federal state of Hessen), Austria (six out of nine federal units), Greece, Hungary, Italy, Poland, Portugal, Spain, England (in cases where mayor is directly elected)
Committee leader model	Denmark, England (in cases of alternative arrangement), Sweden and three Austrian federal units
Collective model	Belgium, Czech Republic, Holland, Switzerland, England (in cases of leader-cabinet model), German federal state of Hessen
Council-manager model	Ireland

Source: Kukovič (2015, 56).

An additional proposal for the division of local governments is given by Berg and Rao (2005, 9–10). Analysis of the transformations of local governance structures suggests that three groups of countries may be formed. The *first group* of countries are those in which radical changes in local leadership have gone in the direction of strengthening the role of local executive authorities (for example, the Netherlands, Germany and the United Kingdom). Countries in which structural changes were limited to some individual (usually larger/urban) municipalities may be classified into the *second group* of countries (for example, Norway, Spain and Denmark). The *third group* of countries includes those in which there were no significant changes in local leadership (for example, Switzerland, Sweden, the United States of America, France and Belgium) (Kukovič 2015, 57; Kukovič and Brezovšek 2015, 239).

Taking into account the local-leadership-related discussion of Mouritzen and Svara (2002) and the idea of transforming local management structures (Berg and Rao 2005), Pawlowska and Radzik (2007) developed local leadership models based on three criteria: the 1) institutional and 2) legal conditions of local leadership, and 3) the *raison d'être* or purpose of local government, i.e. the provision of services or the expression of the will

of the local community and the adaptability of local structures to management arrangements. These criteria make it possible to distinguish between three models of local leadership (Pawlowska and Radzik 2007, 3–4):

- The *technocratic model* is aimed at providing public services with weak political influence. The formation of local policies is based on seeking consensus and on pragmatic activities. The search for consensus does not exclude political frictions that appear during elections which are later neutralized; for example, through the principle of proportionality and the appointment of collective bodies, which prevents political trade-offs. This form of leadership can be described as "dynamic stabilization": leadership rules are general and allow for a considerable degree of autonomy in institution building, while in the transformation of local leadership, internal (endogenous) factors are dominant. This model of local leadership is typical of the Nordic countries (in particular, Finland); but in the group of Central and Eastern European countries, its elements can be traced in the Hungarian system.
- The *bureaucratic model* is characterized by strong institutionalization of leadership and political relations. The local leader has the stable political support of the party, which has a majority in the municipal council; he is protected by his functions and he acts as a civil servant. Because local functions are mostly administrative in nature, this model is called bureaucratic. In addition, the institutional framework of the local leader is very conservative and immune to the factors of change. Both of these characteristics prevent changes in local leadership. Change factors are mostly external (exogenous). The bureaucratic leadership model is typical of the countries of Southern Europe, especially of France. In the group of Central and Eastern European countries, we can find the characteristics of the bureaucratic model in Estonia, Lithuania and Latvia.
- The *transformational model* is characterized by weak leadership institutionalization, but it is reinforced by clear separation and a considerable decision-making power and also executive competencies. The provision of public services and political discourse are of paramount importance to the local leader. In contrast to the technocratic model, where leadership dynamics are stable and there are almost no changes, in the transformation model the leadership dynamics are uneven. However, changes in leadership do not stem from the existing legal and institutional framework, but are the result of citizens' dissatisfaction and pressure or have emerged as an effect of national policy. This model of leadership can be found in England and Ireland, while in the group of Central and Eastern European countries it is closest to the Polish system of local leadership (Kukovič 2015, 58–59; Brezovšek and Kukovič 2015, 239–240).

### 3 Conclusion

In Europe, there are very different regimes or models of local authorities that differ in size, structure, tasks, and relationships with the state. A common feature is their emergence from their own traditions and historical development. It is expected that different models of local authorities will also be preserved in the future, as there cannot

exist only a single model either within individual federal states, let alone at the pan-European Level.

Understanding the importance of local authorities when assessing the democratic nature of a society is extremely important, as local authorities are at the centre of professional and political attention. Local government denotes the right and ability of the local community to prescribe and regulate a significant proportion of public affairs of a local nature within the bounds of the constitution and laws according to its own responsibility and in the interests of the local population (Vlaj 2005, 25). The true role of local systems is thus located in the vertical division of power. With a division of power between the state and local communities, the power of the state (centre) is limited in a way that there is less opportunity for its alienation and abuse. Such a system in a democratic country allows public services to be more effective and efficient than if all power was centralized (Brezovšek and Kukovič 2015, 221–222). There is a constant focus on the individual in terms of the need to satisfy their modern needs and the quality of their life in their place of residence. Also increasing is the importance of cross-border networking and the international cooperation of local communities. Local communities are not closed systems, but systems that are open to the outside, to the wider local community, the state, the European Union, and also to global society.

#### Notes:

<sup>1</sup> Countries that decide to ratify the European Charter of Local Self-Government accept their obligation to incorporate at least two-thirds of its provisions.

<sup>2</sup> Also 'Boosterism' or the 'Growth machine' model (Heinelt and Hlepas 2006, 25).

<sup>3</sup> See also Peterson (1981) and Svara (1998).

<sup>4</sup> Here we refer to the tradition of past political regimes and arrangements, dependence on the democratic path, and the transition and consolidation of democracy.

<sup>5</sup> See *European Mayor: Political Leaders in the Changing Context of Local Democracy*, ed. Bäck et al. (2006).

<sup>6</sup> The dualistic (competence) model was especially emphasized in the Prussian Town Act of 1808, in which the dualistic collective form was drawn up, as well as in other German states of the time, where a dualistic (competence) model was adopted in the form of a municipal council and individual mayor.

<sup>7</sup> Here, too, we refer to the example of building permits that, in accordance with the dual model of tasks in terms of the responsibility of the local authority, have been a delegated task in France and Germany, which (in accordance with the dualistic competence model) the local executive branch of the authority or administration (the elected municipal council) has no influence or control over in terms of responsibility for implementation.

<sup>8</sup> We highlight the problems of adopting the terms assembly government, parliamentarism, presidentialism, and semi- presidentialism, which are increasingly being used in European scientific terminology, for the purpose of studying and naming the typologies of local authorities. Due to the diversity of state and local political composition, it should be emphasized that the typographical classification of local authorities is only metaphorical.

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## **The Protection and Promotion of Linguistic Minorities: The Italian Law of Diversity at the Local Level**

SIMONE PENASA

**Abstract** The protection of linguistic minorities is a traditional topic within the study of the legal environment. In evaluating the protection and promotion of minority languages, the evolution of legal tools and constitutional principles is especially relevant, as is the role played by the international and supranational levels. The paper outlines a general conceptual and legal framework, and as a case study focuses on the legal arrangement of linguistic diversity in Italy. Special attention is paid to Italian Framework Law 482/99, which, as an application of the Constitution, recognizes twelve minority languages and provides for their protection in that country. Subsequently, the paper focuses on the role of local communities in effectively implementing the international and constitutional principles aimed at protecting and promoting linguistic minorities.

**Keywords:** • linguistic minorities • protection • legal framework • Italy

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## 1 Conceptual framework and theories

According to Eurobarometer<sup>1</sup> (2012), within the European Union linguistic pluralism is a widespread phenomenon. In the EU there are twenty-three officially recognized languages, more than sixty indigenous regional and minority languages, and many non-indigenous languages spoken by migrant communities. Thus, Europe expresses and is qualified by its own diversity in cultural and linguistic terms. It is useful to systematize and briefly analyse the current legal standard of linguistic protection and promotion at the European and international level.

Linguistic diversity conveys cultural, social and even religious plurality. It can be managed at the national level according to four main approaches of constitutional protection, which are inevitably dynamic and partially overlapping (Toniatti 1995, 206):

1. Repressive nationalist state: “The uniform national identity of the population is ideologically over-inflated (sometimes by the proclamation of a state religion) in terms of its exclusiveness and superiority,” by eventually legitimating policies which officially deny the mere existence of minorities.
2. Agnostic liberal national state: this approach envisages “the coincidence between the nationality (i.e. individuals belonging to the nation) and the citizenship of the population”; accordingly, it is indifferent to the existence and maintenance of cultural and religious identities of minorities, but it provides at the same time substantive rules and judicial instruments for the protection of the fundamental freedoms of individuals. The systems in France and the US, which grant formal equality to all their citizens irrespective of ethnic, religious and linguistic characteristics, are examples of this approach.
3. National state of multinational and promotional inspiration: this is characterized by “the predominance of a national group (the majority) and the presence of one or several minority groups, the recognition, protection and promotion of which are an integral component (...) of the constitutional order and its fundamental values”; this approach tends to provide institutional and legal ad hoc solutions in territorial areas where minorities are historically settled (examples include Italy and Spain).
4. Paritarian multinational state: “[D]espite the numerical difference between the distinct national communities, the constitutional order is framed (...) in order to incorporate and reflect the multinationality of its permanent social pattern on a paritarian basis”; this approach is reflected both in the territorial organization of the institutional system and in substantive legislation (examples include Bosnia-Herzegovina, Belgium, and Switzerland).

As for the legal definition of linguistic minorities, there is no common, shared and universal agreement. According to the European Court of Human Rights, “such a definition would be very difficult to formulate,” and the notion is not defined in any international treaty (Council of Europe 2004, 31). At the international level, the definition provided by Francesco Capotorti is generally accepted as common conceptual ground,

even if it lacks a binding nature: “A group numerically inferior to the rest of the population of a State, in a non-dominant position, whose members – being nationals of the State – possess ethnic, religious or linguistic characteristics differing from those of the rest of the population and show, if only implicitly, a sense of solidarity, directed towards preserving their culture, religion or language” (Capotorti 1977, 96).

It is thus possible to distinguish a set of indicators which can help to legally identify a minority, and which States are generally free to adopt. Minorities can be distinguished according to sets of criteria, such as:

- Objective criteria: e.g. distinguishing features, numbers, non-dominance; citizenship/durable ties with territory;
- Subjective criteria: e.g. awareness, acknowledgement and social relevance, will to preserve their characteristics and separate identity.

It must be highlighted that “[w]hat matters, in legal terms, is the legal recognition of a minority position and its subsequent legal treatment,” and that “[s]uch recognition ultimately depends, among others, on a political choice” (Deerso and Palermo 2013, 190).

In order to accommodate linguistic plurality within a constitutional state, a new theory has been proposed among scholars: the idea of diversity legislation, also called the “*Law of Diversity*”. According to this approach, “[t]he Law of Diversity indicates the complex bunch of legal instruments that can be adopted at all possible levels in order to deal with the requests for accommodation of potentially endless claims for diversity” (Palermo 2007, 70). The Law of Diversity metabolizes the large variety of instruments of protection, different legal sources and interrelated institutional levels as well as the great number of different actors which characterize the law of diversity, by awarding value to:

- Asymmetry regarding its application as well as single legal and institutional instruments;
- Pluralism of legal sources and of subjects involved (not only States but also the same minoritarian communities);
- Negotiation of its content in a quasi-contractual framework (Palermo and Woelk 2005).

Therefore, it is “inevitably subject to constant revision, in terms of (...) proportionality, efficiency and sustainability, and directly linked to the changes of the [*sic*] societal reality” (Palermo and Woelk 2005, 9).

## 2 International declarations, legislations and treaties

Given the characteristics of the Law of Diversity – multilevel approach, plurality of legal sources – the description of the state of the art in this context will be focused essentially on the international level, where it is possible to detect legal standards capable of orienting States in adopting ad hoc measures for the protection and promotion of minorities.

In the European framework, the role of the Council of Europe<sup>2</sup> is especially relevant, while the European Union suffers from of a lack of specific competence in the field. In very general terms, in the EU the legal instruments on minorities become relevant:

- By formally recognizing the protection of minorities within the binding criteria (the Copenhagen Criteria) which candidate States for EU accession must comply with by reforming their constitutional and legal frameworks;
- By applying the principle of non-discrimination for the purposes of minority protection (see for instance the implementation of the “Race Directive”<sup>3</sup> by the European Court of Justice<sup>4</sup> (OSI 2012);
- By acknowledging cultural diversity as one of the essential values on which the Union is built.

At the global level, the United Nations provides standards which may also be applicable in the context of minority protection. According to the International Covenant on Civil and Political Rights (ICCPR), “In those States in which ethnic, religious or linguistic minorities exist, persons belonging to such minorities shall not be denied the right, in community with the other members of their group, to enjoy their own culture, to profess and practise their own religion, or to use their own language”.<sup>5</sup>

As is broadly known, this instrument, although legally binding, is not guaranteed by specific judicial remedies such as those that occur in the context of the European Convention on Human Rights, thus its effective fulfillment by Member States is guaranteed<sup>6</sup> by the UN Human Rights Committee, a body of independent experts that monitors implementation of the Covenant by States through a mechanism based on cycles of monitoring activities and recommendations sent to States. In General Comment no. 23, the Committee<sup>7</sup> states that “this article establishes and recognizes a right which is conferred on individuals belonging to minority groups and which is distinct from, and additional to, all the other rights which, as individuals in common with everyone else, they are already entitled to enjoy under the Covenant” (OHCHR 1994, Point 1) and that “States parties, therefore, have an obligation to ensure that the exercise of these rights is fully protected and they should indicate in their reports the measures they have adopted to this end” (OHCHR 1994, Point 9).

The UN Declaration on Rights of Persons belonging to National, Ethnic, Religious and Linguistic Minorities (1992) is a non-binding instrument. It declares that “States shall

protect the existence and the national or ethnic, cultural, religious and linguistic identity of minorities within their respective territories and shall encourage conditions for the promotion of that identity. States shall adopt appropriate legislative and other measures to achieve those ends” (ECRML 1992, Article 1).

At the European level, as anticipated, the Council of Europe framework is the most remarkable in the field. Although the European Convention of Human Rights (ECHR) does not contain any expressly “minority-oriented” provisions, many articles have been activated before the European Court of Human Rights (ECtHR) in relation to individuals belonging to a linguistic or religious minority:

- Article 8: Right to respect for private and family life;
- Article 9: Freedom of thought, conscience and religion;
- Article 10: Freedom of expression;
- Article 11: Freedom of association; and
- Article 3 of Protocol no. 1: Right to free elections.

On these legal grounds, the ECtHR has become one of the driving actors in enhancing the protection of minorities in Europe. In its case-law,<sup>8</sup> the Court stated that “the existence of minorities and different cultures in a country was a historical fact that a ‘democratic society’ had to tolerate and even protect and support according to the principles of international law” (Council of Europe 1998, 20) and that “democracy does not simply mean that the views of the majority must always prevail: a balance must be achieved which ensures the fair and proper treatment of minorities and avoids any abuse of a dominant position” (European Court of Human Rights 1981).

As assessed by the European Commission for Democracy through Law (Venice Commission 2007), the role of the ECHR is limited to protection against excessive state interference in the classical human rights of individuals belonging to a minority, while it has produced very limited results under the prohibition of discrimination as concerns the obligation of States to implement special measures on behalf of minorities to compensate for their vulnerable and disadvantaged position (Venice Commission 2007).

As to the “minority-specific” legal tools in the Council of Europe framework, two international treaties play a crucial role in setting common standards for States: The European Charter for Regional and Minority Languages (ECRML 1992) and the Framework Convention on National Minorities (FNCM 1995, entered into force on 1 February 1998).

The ECRML is a standard-setting instrument in terms of managing linguistic and cultural diversity more specifically than a traditional minority-rights treaty. It does not provide a catalogue of rights for individuals belonging to a linguistic minority, as the target of guarantees are languages traditionally spoken within the territory of Europe. Leaving to the States Parties a wide margin of appreciation, the Charter in its Preamble proclaims

that “the protection and promotion of regional or minority languages in the different countries and regions of Europe represent an important contribution to the building of a Europe based on the principles of democracy and cultural diversity within the framework of national sovereignty and territorial integrity” (ECRML 1992, Preamble). Interestingly enough, the Charter, differently from the Framework Convention in which a definition of national minority is not provided (see below), defines “regional or minority languages,” which are languages that are traditionally used within the given territory of a State by nationals of that State who form a group numerically smaller than the rest of the State's population; and that are different from the official language(s) of the State (Article 1). Thus, the languages of migrants are expressly excluded from the scope of application of guarantees provided by the Charter.

Another distinctive feature of the Charter is its “à la carte” nature: States Parties are free to select, within all activities indicated in the Charter’s text in different contexts of private and public life (Education; Judicial authorities; Administrative authorities and public services; Media; Cultural activities and facilities; Economic and social life; Transfrontier exchanges), a minimum number of measures in order to fulfil the treaty’s obligations (Article 2). This feature inevitably broadens the discretionary power of States in implementing the Charter’s provisions.

The monitoring mechanism of the Charter is performed by a Committee of Experts, which periodically assesses the level of implementation of duties guaranteed by States Parties: this system does not provide for a judicial body legitimated to declare violations of the treaty (see the ECHR system), but guarantees on the one hand flexible accommodation to the concrete circumstances and specific characteristics of languages, although on the other hand faces the risk of excessively “diluting” States’ obligations, considering the vagueness and generality of principles and purposes declared in the Charter’s text.

The Framework Convention on National Minorities (FNCM 1995) provides, differently from the Charter, a developed catalogue of rights for individuals belonging to a minority. Within the Convention it is possible to distinguish three different and complementing levels of protection:

- The freedom to be (not be) part of a minority (“every person belonging to a national minority shall have the right freely to choose to be treated or not to be treated as such and no disadvantage shall result from this choice or from the exercise of the rights which are connected to that choice” (Article 3);
- The right not to be discriminated against (“any discrimination based on belonging to a national minority shall be prohibited” (Article 4);
- And a set of linguistic rights, such as the right of every person who belongs to a national minority to freedom of peaceful assembly, freedom of association, freedom of expression, and freedom of thought, conscience and religion (Article 7), the right



to use freely his or her minority language in private and in public (Article 10) and the right to learn his or her minority language (Article 14).

An ad hoc Advisory Committee of experts assists the Council of Europe Committee of Ministers in evaluating the adequacy of the measures taken by States to give effect to the principles set out in the Convention (Article 26). States Parties are obliged to periodically transmit full information about legislative and other measures taken (Article 25), and the Committee of Ministers sends accordingly a set of recommendations to each State Party to overcome eventual omissions or failures in compliance with the treaty's obligations. The latter have political relevance only through constant dialogue between European and national authorities. This soft law is becoming increasingly effective in driving developments that occur in the context of minority protection and promotion at the national level.

Therefore, diversity legislation is characterized by different but interconnected normative systems which combine the global (UN system), regional (European) and national level, wherein the latter can be further complemented by various measures of minority governance at regional and local levels (Regions, Provinces, Municipalities).

### **3 A comparative case study**

The goal of the case study is to clarify the essence and function of the main features of diversity legislation (also called the Law of Diversity) and to understand how it may effectively work within a national legal system. Moreover, an analysis of whether and how international standards can be implemented by States is also provided. The case study focuses on the Italian legal system of protection and promotion for linguistic minorities. Even if this evidently represents a single legal order, the case is relevant due to the characteristics of Italy's form of state, in general terms, and – more specifically – due to the specific aims of minority protection and the structure of its legal mechanisms and tools of implementation.

On the one hand, Italy is classified as a regional State wherein sub-national governmental entities (Regions, Provinces, Municipalities) are entitled to a significant number of functions and powers, both of legislative and administrative nature, which also become relevant in the “minority protection” context. In general terms, Regions share competences with central government in key areas concerning the protection and promotion of linguistic minorities, such as education and culture.

The distribution of competences among different frames of government is essential in diversity legislation, as by exercising normative autonomy Regions where linguistic minority groups are settled can choose to implement specific promotional measures which are specifically targeted to the concrete characteristics (numerical, cultural, linguistic, economic) of the involved minorities which apply exclusively within the

territory of the concrete Region or even within a circumscribed area within the Region. A limited number of Regions are entitled at the constitutional level to a special legal regime (Regions with a Special Autonomous Statute), thus exercising a higher level of legislative function than ones attributed to “ordinary” Regions.

This differentiated status derives and was originally justified mainly by recalling the historical presence in the respective regional territories of relevant linguistic minorities, the protection of which had legitimated their special institutional and legal status (French-speaking minority in Aosta Valley, a German-speaking one in Trentino-Alto Adige/South Tyrol and a Slovenian-speaking one in Friuli Venezia Giulia).

Different linguistic minorities settled in different Regions can thus legitimately receive different legal protection according to the more effective, suitable and adequate design of promotional measures. This can involve the use of minority languages in public administration, in school, and also the implementation of special guarantees for the political representation of linguistic minorities and economic support for their activities. Thus, the regional and decentralized nature of the Italian form of government reveals itself as functional in strengthening the asymmetry and differentiation of measures aimed at protecting and promoting linguistic minorities, which are two of the main features of the Law of Diversity.

On the other hand, Italy represents a paradigmatic example of a national State of multinational and promotional inspiration<sup>9</sup> wherein the recognition, protection and promotion of minorities are an integral component of the constitutional order. Article 6 of the Italian Constitution states that safeguarding linguistic minorities is a binding constitutional obligation of the Italian Republic. By taking advantage of the regional and decentralized nature of the State, protection is applied through an asymmetrical and differentiated approach which is consistent with the equality principle (Article 3 of the Italian Constitution). According to the area of settlement, “historical” (with a traditional presence in the territory) linguistic groups are subject to different protection and promotional measures, although within a common general framework of principles defined by law.

Only minorities which are explicitly recognized by the State can benefit from protection under Article 6 of the Constitution (Art. 2, Law no. 482). This means that the State must formally recognize a linguistic group as a minority within a given region and accordingly implement specific legislative measures to protect that minority (Art. 2). The Law itself recalls those languages and cultures which are formally recognized by the State – Albanian, Catalan, German, Greek, Slovenian and Croatian populations –, and individuals who speak French, Friulian, Ladin, Provençal-Occitan and Sardinian.

The concrete implementation of promotional measures provided by Law no. 482 is attributed to local authorities, thus each minority is entitled to a different level of

protection, and to differentiated measures aimed at promoting its language and culture. This system, based on asymmetry and differentiation, has led to the categorization of Italian linguistic minorities into three general types.

- The first is “recognized, super-protected” minorities, which includes groups that are settled in regions with special autonomous powers, such as Aosta Valley (French-speaking), Trentino-Alto Adige/South Tyrol (mainly German-speaking, but also Ladins<sup>10</sup> and, in Trentino, also Cimbrians<sup>11</sup> and Mocheni<sup>12</sup>), and Friuli Venezia Giulia (Slovene minority). These groups enjoy a high degree of protection, with the highest level accorded to the German-speaking group in South Tyrol.
- The second category is “recognized minorities with possible protection”: these are groups that, while recognized under Law 482/1999, might be but are not necessarily protected. This is linked to legislation stipulating that different levels of protection depend on the implementation of legislative measures at the local level.
- The third category is “non-recognized minorities,” which are not recognized by the state as linguistic minorities; notably Roma and migrants. These last groups are only guaranteed protection against discrimination but do not enjoy special protection under Law no 482.

The Italian system of protection for linguistic minorities is also relevant because the implementation of the principle of territoriality, according to which special protection applies exclusively in fixed geographical areas where a minority group has historically settled (i.e., in specific territories within the same Region, such as occurs with Slovenians in Friuli Venezia Giulia), produces different levels of protection for the same minority groups when the latter settle in different areas of the State.

The analysis of differentiation within the same linguistic minority may become very relevant in understanding how exactly the Law of Diversity works, and whether – and under which conditions – it is consistent with the principle of equality and non-discrimination on the grounds of language or culture.

This arrangement can be demonstrated by the case of the Ladin language. Ladin-speaking people are distributed across three different Provinces (South Tyrol, Trentino, and Belluno), which belong to two different Regions (respectively, Trentino-Alto Adige/South Tyrol, and Veneto). Depending on the location, three different legal regimes thus apply to Ladins:

- They are a “super-protected” minority in South Tyrol;
- An “almost” super-protected minority in Trentino;
- And simply a “recognized minority with possible protection” in Veneto.

This is not merely a formal classification but influences the concrete measures that are implemented.

As an example, if we consider the political representation of the former in the representative local bodies (Provincial or Regional Councils), the following arrangements are in place.

- Ladins are entitled only in South Tyrol to a guaranteed seat on the South Tyrol Council of Province, thus at least one minority representative will be a member of the Council.
- In Trentino the electoral law also provides for promotional measures but does not guarantee a reserved seat in the Council of Province: instead of the establishment of a reserved seat, representation is favoured by reserving one seat within the Council for the territory of those municipalities where Ladins are historically settled (Article 48, Statute).
- Differently, the Regional Statute of Veneto does not provide any special guarantee in terms of political representation for the Ladins which live in the Province of Belluno, which belongs to Veneto.

The same phenomenon occurs in the field of education and the right to learn a minority language in schools.

In Trentino-Alto Adige/South Tyrol, the protection and promotion of minority languages through education is guaranteed at the Autonomous Statute level, thus gaining constitutional relevance. Notwithstanding this, protection in the educational context encounters differentiated implementation according to the specific minority (German speakers, Ladins, Cimbrians and Mocheni) and territory (Province of South Tyrol, Province of Trentino, specific areas of the two Provinces, according to the territoriality principle). With specific regard to Ladins, in the field of education this group also receive differentiated legal status. In South Tyrol, the Ladin language is used in nursery schools and is taught in primary schools only within Ladins' traditional areas of settlement, which historically coincide with the Badia and Gardena Valleys (Article 19 Autonomous Regional Statute). Within the same areas, the teaching of the Ladin language is guaranteed in schools of all levels. Interestingly enough, the teaching of the Ladin language must be provided both in Italian and German according to a principle of equivalence in terms of teaching hours and final outcomes. Moreover, Ladin schools are separated, including in organizational terms, from Italian and German schools, and are autonomously managed by the Ladin linguistic group.

The arrangement is different in term of the Ladins who inhabit the Province of Trento. While in South Tyrol a model of "equal school" (*"paritaria"*) is enforced, whereby teaching is equally shared between languages (Italian and German), neither of which is the students' mother tongue (Ladin), in Trentino a different educational system is implemented. This can be classified as being among the majority schools which provide promotional and asymmetrical mechanisms for teaching the minority language. This approach is designed to meet the educational needs of small numbers of students living in the limited areas of a territory, such as is the case of the Ladin minority in Trentino.

The teaching of minority language and culture is guaranteed only in their traditional settlement areas (Article 102, Autonomous Statute). Statutory Law at the Provincial level guarantees the vehicular use of the Ladin language at schools and provides, with specific reference to Ladin schools, special mechanisms of organizational and administrative autonomy (Fassa Valley Ladin School; Law no. 5/2006).

Within Trentino Province, a further level of asymmetry and differentiation in the educational context can be detected due to the differentiation between Ladins, on the one hand, and Cimbrians and Mocheni, on the other. Even if the three linguistic groups receive the same protection at the Regional Autonomous Statute level (Article 102), Provincial Law no. 5/2006, in the light of implementing the general principle of favoring the teaching of minority languages and cultures, provides that within the schools located within municipalities where the latter minorities are settled (Cimbrians and Mocheni) the teaching of minority languages – together with German – shall be guaranteed, according to the concrete availability of competent teachers (Art. 95, Law no. 5/2006). Thus, the effective implementation of the promotional measure is predicated on the availability of human resources capable of teaching the minority language: this condition is not present within the regulation of Ladin schools, thus introducing a further element of differentiation, which can be justified in the light of the small numbers of scholars and teachers.

Analysis of the Provincial system of educational promotion for linguistic minorities in Trentino is also useful for understanding the relationship between the international standards set forth by the international treaties referred to in this paper,<sup>13</sup> and concrete measures implemented at the national level. If we consider the Framework Convention Article 14 states that “The Parties undertake to recognise that every person belonging to a national minority has the right to learn his or her minority language” (FNCM 1995).

However, the concrete implementation of the acknowledged right to learn is conditioned on a set of conditions and requirements which are strictly linked to the specific circumstances and characteristics of each minority in a given territory: the right may be guaranteed “in *areas inhabited* by persons belonging to national minorities” (territoriality principle); “traditionally or *in substantial numbers*” (quantitative criteria); “if there is *sufficient demand*” (subjective criterion); “*as far as possible* and within the framework of their education system” (contextual/organizational criteria); or based on “*adequate opportunities* for being taught the minority language”. If we consider all the conditionality clauses contained in Article 14, the acknowledgement that States Parties have a broad margin of appreciation in effectively implementing international standards is clear (Toniatti 1995).

This is also plainly affirmed in the Explanatory Report to the FCNM, where it is stated that “[i]n recognition of the possible financial, administrative and technical difficulties associated with instruction of or in minority languages, this provision has been worded

very flexibly, leaving Parties a wide measure of discretion". Thus, "[t]he obligation to endeavour to ensure instruction of or in minority languages is subject to several conditions; in particular, there must be 'sufficient demand' from persons belonging to the relevant national minorities" (FNCM 1995, 21, Article 14, Paragraph 2). The wording "as far as possible" indicates that such instruction is dependent on the available resources of the Party concerned.

Comparative analysis has highlighted a further characteristic of the Law of Diversity: it is not only asymmetrical in its content and plural in its regulatory and political tools, but also negotiated. The institutional and regulatory environment shall provide adequate procedural and substantive tools capable of favouring the active and direct participation of minority groups in law-making, law-enforcement and monitoring. The case study also reveals one of the most challenging deficiencies which can arise in the protection of linguistic minorities, and which the Law of Diversity approach tries to avoid: the lack of effectiveness of policies and regulations due to a number of factors intrinsically linked to the characteristics of the particular national and regional context. The disconnection between intended goals and concrete means and achievements is due to the difficulty of tailoring both institutional and functional assets to the concrete size and resources of minority groups living in the particular area. It is thus crucial to provide for mechanisms to monitor and assess the impact of promotional policies in order to regularly bring them into line with the principles of adequateness and empowerment of communities.

In conclusion, comparison within the Italian legal system of protection for linguistic minorities is able to paradigmatically reveal the pros and cons of a Law of Diversity approach. It also highlights the potential impact that international standards can produce in orienting national policies, although the margin of appreciation acknowledged to States is usually very broad. Finally, it also expresses the different steps that minority protection has historically involved by constructing a climax: guaranteeing the mere physical existence of individuals belonging to linguistic minorities; guaranteeing legal recognition on the part of States; assuring respect of the right not to be discriminated against; and developing ad hoc positive activities that overcome factual and legal gaps.

Once these goals are reached, the Law of Diversity approach aims to achieve two further objectives: the self-empowerment of minorities and increasing the effectiveness of promotional policies.

#### 4 Glossary of terms

Minority (stimulating definitions):

*“Even though I may not have a definition of what constitutes a minority, I would dare to say that I know a minority when I see one”.*<sup>14</sup>

*“Minorities as such do not exist. Rather, there exist large and small, numerous and otherwise, social groups. In abstract, all groups, each endowed with its own identity, equally represent the natural and cultural diversity of the human species”* (Toniatti 1995, 200).

National minority: minority groups within a State, which individuals belonging to national minority are citizens of, having a historical connection with a kin-state.

Linguistic rights: special rights which are acknowledged to individuals belonging to a linguistic minority which aim at guaranteeing and promoting the freedom to know, use and disseminate minority language and culture. These can be comprised of the right to use minority language in private and in public, such as in front of public administration, social and political life and in the media; and the right to learn and to be taught in a minority language at school (see the catalogue of rights provided by the Framework Convention for the Protection of National Minorities).

Framework Convention for the Protection of National Minorities: International treaty within the framework of the Council of Europe which represents one of the most comprehensive treaties designed to protect the rights of persons belonging to national minorities (FNCM 1998).

European Charter for Regional or Minority Languages: International treaty which aims to provide a set of principles and standards for the protection and promotion of languages used by traditional minorities within the Council of Europe (ECRML 1992).

#### Notes:

<sup>1</sup> Eurobarometer is a series of public opinion surveys conducted regularly in the Member States of the European Union on behalf of the European Commission.

<sup>2</sup> The Council of Europe is an international organization of 47 states. Its stated aim is to uphold human rights, democracy and the rule of law in Europe.

<sup>3</sup> The Race Equality Directive (Directive 2000/43/EC) prohibits discrimination on grounds of race and ethnic origin.

<sup>4</sup> The European Court of Justice (ECJ), officially just the Court of Justice, is the supreme court of the European Union in matters of European Union law.

<sup>5</sup> Art. 27; Available at:

<https://www.ohchr.org/EN/Issues/Minorities/SRMinorities/Pages/standards.aspx> (15 March, 2019).

<sup>6</sup> UN Human Rights Committee, for further information see:

<https://www.ohchr.org/EN/HRBodies/CCPR/Pages/CCPRIndex.aspx> (15 March, 2019).

<sup>7</sup> The rights of minorities, Art. 27.

<sup>8</sup> Case law refers to a set of past rulings by a tribunal, if these rulings can be cited later as precedents.

<sup>9</sup> See the classification of approaches of constitutional protection, as provided under “Conceptual framework and theories” at the beginning of this paper.

<sup>10</sup> Ladin is a Romance language consisting of a group of dialects, mainly spoken in Northern Italy.

<sup>11</sup> Cimbrian language: several local Upper-German language varieties, mainly spoken in north-eastern Italy.

<sup>12</sup> The Möcheno language is an Upper-German language variety, closely related to Bavarian, mainly spoken in north-eastern Italy.

<sup>13</sup> See in this paper under the heading “International declarations, legislation and treaties”.

<sup>14</sup> Keynote address of Mr Max van der Stahl, CSCE High Commissioner on National Minorities at the CSCE Human Dimensions Seminar on “Case Studies on National Minority Issues: Positive Results”, Warsaw, 24 May 1993.

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## The Role of Contracts, Standards and Certification in Protecting Fundamental Rights

MATTEO FERRARI

**Abstract** This paper deals with the role that contracts, standards and certification can play in guaranteeing the protection of fundamental rights in international supply chains. Recourse to standards and certification can be conceived of as a way to create uniformity in protecting fundamental rights when economic players of different nationalities are involved. A contract is an additional legal mechanism designed to make standards and certification binding for such actors. This paper demonstrates the role of these private legal instruments in rural development, human rights, safety at work, environment protection, and food safety by elaborating and comparing three case studies. The case studies are devoted to describing standards and certification systems in the coffee sector that implement norms and principles and thereby facilitate network-building among various stakeholders. Compliance with these collections of norms is enforced by private contracts, as a rule, and enables co-operation between multinationals and their suppliers.

**Keywords:** • private contracts • international • human rights • environment protection • food and work safety • rural development

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## 1 Introduction

One of the pillars of rural development is represented by the protection of human rights, since the latter are instrumental in fostering the quality of life and well-being of farmers. In this context, by rural development I mean “an ongoing and essentially interventionist process of qualitative, quantitative and/or distributional change leading to some degree of betterment for groups of people” (Buller and Wright 1990). However, in an age of globalization it is crucial for farmers to have access to markets, and in particular to international markets, if they are to have a chance to prosper. Thus, the protection of human rights must be pursued while considering the international dynamics within which rural development takes place. In particular, it is necessary to balance the protection of the interests of economic players who, as mentioned, nowadays operate on a global level, and the need to protect and promote farmers’ fundamental rights, an issue that appears to concern the local level.

A clash between the global and the local appears to exist: the protection of human rights at the local level seems to be capable of negatively affecting the smooth operation of international food supply chains. The problem is exacerbated by the fact that while economic exchanges are usually thought of as the domain of private parties, the protection of human rights is traditionally conceived of as the province of public action. It is seemingly difficult to reconcile the public dimension of human rights with the strong private flavour that international supply chains have: how can a public goal (i.e. the advancement of human rights) become part of a private exchange?

As the following pages attempt to show, the clash between the local and global, as well as between the private and the public, is more theoretical than practical: these different dimensions can, and often do, co-exist. Indeed, the emergence of international food supply chains and the use of tools pertaining to the domain of private law can revitalize the protection of human rights. The goal of this chapter is thus to introduce readers to the interplay between the protection of human rights, on the one hand, and the role that private standards, certification and contracts can play in international food supply chains, on the other.

## 2 Conceptual framework

The first part of the paper offers a short description of some terms and concepts that will play a crucial role in the following analysis. In addition, it illustrates the starting problem; namely, how to protect human rights in international food supply chains via recourse to tools of private law.

Starting from the latter point, protecting human rights in the international context faces several challenges, ranging from the definition of what human rights are to the policy options that can better guarantee their effectiveness worldwide. One of the most pressing

issues is represented by the lack of a supranational authority with the power to police the application of the norms that provide for the protection of such rights. Of course, national states have this kind of power, but they are not always effective at promoting human rights and prosecuting their violation, either because they lack the will and/or infrastructure to pursue this task or because their power stops at the nation's borders. The latter point is particularly important in the context of international food supply chains, which, as we will see, operate in different countries and involve parties from different nations (including, often, multinational corporations). Moreover, as mentioned at the outset, the protection of human rights is traditionally conceived of as the province of public intervention, while international food supply chains are typically governed through instruments that belong to private law. Thus, there seems to exist a gap between the regulatory contexts related to human rights and international food supply chains: the first are regulated by public law, and the second by private law. How may these two different environments be reconciled? Before showing how scholarship has dealt with this problem, it is apt to define a few terms crucial for our analysis.

The first term to be defined is that of 'human right', an expression frequently employed in different national and international texts. A key point of reference in understanding what I mean by human right is offered by the Universal Declaration of Human Rights, proclaimed by the United Nations General Assembly in Paris on 10 December 1948. According to Art. 2, human rights are all the rights and freedoms established in the Declaration and belonging to every human being "without distinction of any kind, such as race, colour, sex, language, religion, political or other opinion, national or social origin, property, birth or other status". In other terms, human rights are those rights that every human being has for the simple reason of being a member of the human family.<sup>1</sup>

The second term to be defined concerns the notion of private standards (Brunsson and Jacobsson 2000). These are rules that are created by private actors, rather than by public ones, and that, as such, are voluntary in nature. Indeed, private standards do not rely on the power states have to impose conduct and sanction those who do not adopt such conduct. Thus, as a matter of principle, operators are free to decide whether to follow standards. Nowadays, the use of private standards is widespread, especially in the international context. The reason is the fact that, since there is no such a thing as 'global law' – i.e. norms that can be imposed regardless of national borders –, private standards create a sort of common set of rules that can be applied worldwide (on a voluntary basis). Why should professional operators adhere to standards voluntarily? The answer is connected to the incentives associated with adopting such private standards: the greater such incentives are, the higher the probability that the private standard will be applied by the parties. In other terms, the adoption of private standards, being voluntary, depends on the benefits parties will obtain by complying with them: for example, if farmers comply with a private standard they might obtain access to a lucrative market; a processor might adopt a private standard in order to improve the quality of the goods it purchases; or a

retailing chain might use private standards to attract consumers (Giovannucci and Ponte 2005, 287; Poncibò 2007).

In the context of international supply chains, there are three sets of incentives that are more relevant in explaining the success of private standards.

- The first concerns the drive for legal homogeneity. Especially in the case of long supply chains involving players acting in different legal systems, it becomes crucial to have a set of rules that are homogeneous and can overcome differences in national regulation.
- The second set is represented by the drive for interoperability. In the case of integrated supply chains, in which different operators are involved at different stages of production and marketing processes, it is very important that such operators are able to interact on the basis of some common features.
- The third type of incentive is related to the need to provide more detailed specifications in the case of activities involving complex technical factors: in many cases public norms do not achieve the level of detail that is needed by private operators and/or they leave some room for discretionary choices. Private standards are thus aimed at restricting such space for discretion and offering a more detailed operational guide to private actors.

Within the broad province of private standards, I focus on one specific type; namely, the so-called ‘suppliers’ codes’ (Frynas and Blowfield 2005; Jenkins *et al.* 2004). These are codes enacted by large business operators (e.g. multinational corporations active in the processing or marketing of foodstuffs), with the scope of providing a set of rules that suppliers must comply with if they want to enter (or continue) a business relationship with such operators. In other words, these corporations create their own rules in order to better manage their production and/or distribution processes, and they ask their business partners to also follow them. The rules I am referring to here are private standards that are established by so-called chain leaders (i.e. the business operators who control the supply chain) (Cafaggi 2016, 230). The way through which these standards are created can differ, as the case study will show. The relationship between the chain leader and suppliers is hierarchical, while it becomes more cooperative in the phases of monitoring compliance with the content of codes (Cafaggi 2016, 223–224). The reason why private standards and suppliers’ codes are relevant for our analysis is that suppliers’ codes increasingly incorporate provisions concerning the protection of human rights. In particular, the codes impose on suppliers the duty to protect human rights in their business activities and are integrated by more detailed documents offering guidance about how to guarantee such protection (Cafaggi 2016, 231–232).

Suppliers’ codes contain private norms that can be applied worldwide since they are not dependent on a particular, national legal system. Nonetheless, one might wonder how this is possible. In other terms, how can these codes be binding and, more specifically, binding regardless of national borders? There are two possible mechanisms.

- The first revolves around the idea that compliance with codes is a prerequisite for entering into a business relationship with a chain leader: since the latter is usually a meaningful economic player, suppliers have a strong incentive to do business with this actor and therefore to comply with the codes. Lack of compliance with the private standards could amount to the impossibility of commencing negotiations with the chain leader.
- The second mechanism is represented by a specific private legal tool that can be employed to make the codes binding, namely, a 'contract'. More specifically, international contracts allow the chain leader to impose their own private standards on suppliers who operate in different states. While the first mechanism temporally operates prior to the birth of a business relationship between the chain leader and the supplier (such a relationship will not even arise if suppliers do not comply with the code), a contract aims at regulating the business relationship once it has arisen, making codes binding for the duration of the relationship itself.

But what is a contract and what is an international contract? The common idea behind the term 'contract' is that of an agreement binding two or more parties who must perform defined activities on behalf of the counter-parts. These activities are specified in the contract itself and give rise to legal obligations (i.e. to duties that the contractual parties have to perform). Of course, how a contract is regulated varies depending on the legal system in operation: nonetheless, the core idea that a contract represents a binding agreement is shared almost universally.

Another common way of looking at contracts is to conceive of them as the legal vessel through which economic exchanges take place in a market. If a farmer wants to sell his produce to a processor or a retail chain, he will have to define a contract regulating that sale. In the context of rural development, contracts are the mechanisms by which farmers can obtain access to the market; if farmers want to access an international market, they will have to underwrite an international contract. The latter is an agreement in which the two or more parties have different nationalities and/or operate under different legal systems. In such cases, the problem that can arise is deciding which national law should be applied. If one contractual party is South African and another French, should South African or French contract law be applied? These kinds of conflict are solved either via rules that form part of a special branch of the law called private international law,<sup>2</sup> or through international conventions that define common rules that apply in different countries in a uniform way.<sup>3</sup> In the first case, there is a national law that prevails, while in the second, no national law prevails since what are applied are norms that go beyond national borders (i.e. are international). In any event, the concept of contract is almost universally recognized and contractual agreements are enforced, even if through different modalities, in almost all legal systems.

Another set of problems concerns the monitoring of compliance with suppliers' codes. Suppliers might have an incentive to declare that they are following a code, while in real

terms they are not. How is it possible to control suppliers' behaviour? A tool often employed in these cases is certification. Certification is a mechanism that the law provides to supply and validate information that the market considers valuable. In the case of suppliers' codes, for market players and in particular for the chain leader it is important to know if suppliers are complying (e.g. whether they are protecting and promoting workers' rights in the workplace): the fulfillment of these conditions can determine important consequences such as the willingness of the chain leader to conclude supply contracts, the price to be paid to the suppliers, reputational damage suffered by the chain leader if, for example, it becomes known to the public that the chain leader is employing suppliers who violate workers' rights, etc. The monitoring of compliance with suppliers' codes is complex: the chain leader does not always have access to objective criteria – such as, for example, chemical parameters – to monitor suppliers' compliance, since the protection of human rights is somewhat immaterial; moreover, the chain leader cannot rely on what suppliers state, since they might have an incentive to cheat provided that the chain leader has no objective criteria for examining the truthfulness of what suppliers declare. Of course, the chain leader might send their own inspectors to a supplier to check if they are complying with a code, but this might be costly for the chain leader and, moreover, might give rise to the duplication of costs in cases in which there is one supplier code common to different chain leaders whose compliance can be monitored once on behalf of all the leaders. Thus, chain leaders usually make recourse to so-called certification bodies which are professional enterprises that operate in a third-party, independent way and which check whether suppliers are actually implementing what is provided for in suppliers' codes. The cost of this monitoring is borne by the suppliers who obtain a certificate if the inspection is positive; i.e. if the certification body finds that the suppliers' code has been complied with.

Finally, the expression 'international food supply chain' refers to an arrangement in which a chain leader is supplied with goods and/or services by other subjects (the suppliers) operating in different parts of the world (for example, a coffee processor operating in Germany might buy coffee beans from farmers and cooperatives located in Ethiopia or Colombia). Being a *food* chain, this arrangement concerns the supply of raw agricultural commodities, processed foodstuffs and beverages, and takes the form of contracts (e.g. for the sale of goods) that link the chain leader with suppliers and that specify the rights and duties contractual parties have with respect to each other. Private standards, suppliers' codes and certification contribute to integrating the contents of contracts.



### 3 The state of the art

The role that private standards, certification and contracts have in international food supply chains can be tackled from different perspectives. Scholars have focused their attention on the following main issues.

1) *The regulatory function of contracts.* Law scholars have underlined that contracts are increasingly applied to pursue goals usually pertaining to the realm of public law. Traditionally, it is within the realm of public law to establish rules concerning health, safety, environmental, labour conditions and the like. But things are changing. Private law, and contract law in particular, is able to create norms that define the conditions mentioned before by including contractual terms and/or by making reference to private standards that identify the conduct parties must follow in order to protect the environment, the health and well-being of their employees, the safety of consumers, and so on. In other terms, contract law is able to create the same types of rules traditionally provided by public law through a system of self-regulation and self-governance implemented by the contractors themselves (Brownsword *et al.* 2017). This use of contracts is especially evident in the international context, since it is there, we face the lack of a unitary body of public rules; contract law can thus create the common regulatory ground among different geographical areas that allows business to flourish (Cafaggi 2013; Park and Berger-Walliser 2015). The regulatory use of contract law also has a 'dark side'. The most obvious sign of this concerns the fact that a contractor who is in a dominant position *vis-à-vis* their counterpart can unilaterally shape the regulatory content of a contract in a way that favors his own interests. In other terms, the asymmetries that often characterize the bargaining force of contractual parties can also translate into regulatory asymmetries, thus deepening preexisting disparities between contractors. Going beyond the interests of single contractors, the regulatory implications of contract law pose a challenge both in terms of democratic accountability and wealth distribution for society at large.

2) *Suppliers' codes and Corporate Social Responsibility (CSR).*<sup>4</sup> The emergence of codes of conduct and suppliers' codes may be located within the larger phenomenon of Corporate Social Responsibility (CSR). This process is driven by large corporations who use such codes to (try to) govern social and environmental issues, such as labour conditions, fair prices, pollution, etc. Scholars have pointed to the fact that CSR in general, and codes of conduct/suppliers' codes in particular, can be appraised in two different ways (Mundlak and Rosen-Zvi 2011, 604). On the one hand, they should be conceived of as a substitute for public intervention and an effort to fix some of the problems and limits of public rules. On the other hand, they may represent a rhetorical device for masking the profit-driven nature of global economic activities. Lund-Thomsen (2008) provides a general global critique of the effectiveness and benefits of codes of conduct, also offering some advice about how to improve them. In both cases, the efficacy of such codes depends on the ability of corporations to communicate information about

their codes and practices to different types of agents and intermediaries, such as consumers, financial institutions, and public bodies (Mundlak and Rosen-Zvi 2011, 605–606).

3) *The public-private divide.* As mentioned, one possible way to think of suppliers' codes is to consider them an alternative to public regulation. This idea raises the issue of the relationship between private standards and public regulation. The interconnections between the two are copious, mutual and complex. On the one hand, the two are complementary, since private standards fill those gaps that are left open by public regulation. For example, private standards are more flexible and less prone to obsolescence than public rules; they can in some cases be used as a benchmark for enacting future, public legislation; private standards cannot substitute public regulation since they pose obligations that go beyond and are additional with respect to those posed by public law; private standards are more effective than public norms in regulating global supply chains (Saadoun 2013; Lytton 2019). On the other hand, scholars have underlined the fact that private standards can be somewhat antagonistic in relation to public norms since they pose additional costs to economic actors who not only have to comply with public legislation, but also with private orders (Saadoun 2013). As underlined in the previous section, the growing importance of private standards is re-shaping administrative law (Lytton 2019) and leading us to also critically reconsider the public-private divide that has traditionally been a feature of continental European legal systems.

4) *Private standards as a barrier to, or trigger of, rural development.* Scholars debate whether private standards and global supply chains represent factors capable of promoting rural development or, on the contrary, they are an obstacle to the achievement of such a goal (Lee *et al.* 2012). Some authors fear that food standards create additional burdens for smallholders and thus pose a barrier to entry for them with respect to international markets. As mentioned above, food chain leaders (e.g. retailers and supermarkets) are able to unilaterally dictate their own conditions to small producers, thanks also to the creation and use of private standards (Henson and Humphrey 2009). Other authors think that codes of conduct, suppliers' codes and private standards in general have a positive impact on smallholders and farmers since they allow them to upgrade their productive infrastructure, increase product quality and improve existing farming techniques, in this way fostering access to global supply chains and international markets (van Beuningen and Knorringa 2009). It is probably impossible to solve this dilemma: depending on the sociocultural context, market conditions, infrastructure, specific features of the product and the supply chain concerned, etc. private standards and suppliers' codes can either advance or retard rural development. In other words, only a case-by-case analysis can provide answers about the relationship between private standards and rural development.

5) *The importance of monitoring performance and sanctioning non-compliance.* It can be difficult to ascertain whether suppliers are really complying with codes of conduct.

This might be due to difficulties in getting access to the information important for assessing compliance (e.g. since this information is controlled only by the firm which should comply with the code); to reluctance to reveal cases of code violation because of the fear of retaliation (e.g. employees' fear of being fired or marginalized if they reveal a violation in the code of conduct by their employer); to the geographical distance between the chain leader and its suppliers (e.g. costs of organizing inspections); or to a lack of a specific expertise with measuring compliance (e.g. a lack of staff who have been trained in the areas covered by the codes of conduct). Therefore, it is crucial that the contracts between chain leaders and suppliers not only provide for the obligation to comply with the codes of conduct/suppliers' codes, but also establish monitoring procedures for monitoring the actual implementation of these acts by suppliers. These monitoring procedures should be effective: in order to be so, they have to be structured in a way that guarantees that they are impartial, independent, sufficiently funded, and adequately staffed. A further corollary of the need to provide for monitoring mechanisms is represented by the necessity of sanctioning those suppliers who do not comply with codes of conduct/suppliers' codes (Cafaggi 2016). Again, the sanctioning system should be effective. This requires that sanctions are sufficient to discourage parties from breaching the codes and that their application is rigorous.

6) *The influence of private standards and certification on contractual remedies.* The logic behind private standards and certification regimes differs from that which characterizes traditional contract law. On the one hand, as noted before, contracts can include terms that make private standards, suppliers' codes, codes of conduct and certification binding for the contractual parties. On the other hand, these standards and certification are capable of influencing and changing the contractual structure within which they are included. This phenomenon becomes clear if one looks to contractual remedies (Cafaggi and Iamiceli 2014). Traditional contractual remedies are centered around the idea of terminating the contractual relationship and compensating the aggrieved party for any losses suffered due to breaches of the contract; in contrast, in the case that a contract makes reference to private standards and certification, remedies tend to be more cooperative in character and aimed at keeping the contractual relationship alive (e.g. by correcting the causes of the breach of contract) and renegotiating terms already agreed upon (Cafaggi and Iamiceli 2015).

#### **4 Case studies from the coffee sector**

The coffee sector offers an interesting case study in which to both demonstrate many of the dynamics described above and to develop a few comparative remarks about the strengths and pitfalls of codes of conduct, suppliers' codes, private standards and certification (Slob and Oldenziel 2003; Giovannucci and Ponte 2005; Muradian and Pelupessy 2005; Reynolds *et al.* 2007; Macdonald 2007; Neilson 2008).

The coffee industry has experienced major changes since the late 1980s. Until 1989, the International Coffee Agreement (ICA) was in place; this instrument created a highly regulated market under which coffee prices were largely determined at a central level, as well as the quotas of coffee that each producer could export (Ponte 2004, 3). After the collapse of the Soviet Union and the rise of neoliberalism, many of the reasons for supporting the Agreement disappeared, thus the ICA was supplanted by a free-market regime with the coffee roasters acting as chain leaders and producers of so-called green coffee (raw coffee) as suppliers (Haight 2011, 75–76; Ponte 2004, 3–4; Muradian and Pelupossy 2005, 2029–2030). The regulatory power both of the ICA and of national states have now largely vanished, since relations are now determined mostly by buyers; i.e. coffee roasters and international traders (Ponte 2004, 4). The changes that occurred in the 1990s had a major negative effect, especially on small farmers, since between the latter and the roasters there are huge differences in terms of bargaining power. The risk is of a race to the bottom, with farmers forced to accept unequal contractual terms simply because they do not have the force to oppose them. However, consumers and NGOs have become more aware of the imbalances that the end of the old coffee governance regime may have created. Thus, the public became (and still is) increasingly interested in the dynamics of the coffee supply chain and how these dynamics can affect not only the quality of what they drink, but also the social, economic and environmental context in which the coffee is produced.

In the new context, chain leaders have increasingly made recourse to private standards in the forms of codes of conduct and suppliers' codes, both in order to meet consumer demand for sustainable products and to manage their supply chains through the establishment of quality- and ethical parameters that suppliers must comply with. Of course, lacking the authority/power to formally impose their conditions – differently from national states – chain leaders have increasingly made recourse to contracts that include terms that transform private standards/codes of conduct into contractual obligations. This is a clear example of what was described before as the regulatory function that contracts are capable of fulfilling.

In particular, sustainability has become a key term for the coffee sector (Ponte 2004, 9 ff). The notion of sustainability is a broad one: it encompasses environmental preservation, workers' protection, the economic and financial viability of the supply chain with particular regard to the defence of weak parties such as small farmers; and public and ethical issues concerning the impact of the supply chain on society generally. There are different private standards, certification and codes of conduct aimed at fostering sustainability in the coffee sector; simultaneously, chain leaders have followed different paths to (try to) promote sustainability. Comparative analysis of these different elements can help to shed some light on the inner structure of these different tools and to better understand the operational relevance of the theoretical issues we have analysed in the previous sections.

We will compare three different cases where private standards, certification and codes of conduct have been used to govern the coffee supply chain. These cases show the different strategies that chain leaders can employ, as well as the different roles that public, international and non-profit bodies can play.

*The Baseline Common Code of the Global Coffee Platform*

The first case study concerns the Baseline Common Code (BCC)<sup>5</sup> operated by the Global Coffee Platform (GCP),<sup>6</sup> a network of different stakeholders operating in the coffee sector (Neilson and Pritchard 2007). The application of the BCC is ensured by Coffee Assurance Services (CAS).<sup>7</sup> GCP's general goal is to create a common baseline for coffee production around the world with regard to social, environmental and economic sustainability. The BCC is one of the tools through which such a result may be achieved, and the ambition is for it to become the benchmark for the coffee sector globally. Any entity operating in the coffee supply chain and in a producing country can be subject to the Code: this includes roasters, mills, cooperatives, estates, etc. BCC's main features are that it focuses only on one specific sector, is it applied to different operators working in multiple contexts and legal systems, and it is built around detailed principles and unacceptable practices. These principles and practices are grouped under the umbrella of the three different types of sustainability mentioned before (social, environmental, economic). Under each principle is listed three possible scenarios (marked, respectively, in green, yellow and red) with a few indicators for each scenario.

For example, within the social sustainability category one principle concerns 'Discrimination'. Three different scenarios are described. In the first scenario (green) is listed 'Positive action programmes to secure equal rights are implemented'; in the second (yellow), 'Awareness to secure equal rights is raised and concrete steps to develop positive action programmes are evident'; under the third scenario (red), 'No positive action to either raise awareness or secure equal rights is evident'. In order to assess if a scenario really exists, a few indicators can be used. Thus, with regard to the green scenario one, one indicator is 'The policy and procedures are being implemented, i.e. potentially vulnerable groups are identified, and efforts have been made in order to explain in further detail the procedures to them, in particular the grievance mechanisms. There is evidence that this and other actions to remove the obstacles that foster discrimination are being developed'; for the yellow scenario, "In case incidents of discrimination, harassment or abusive treatment have occurred, these are being addressed"; in the case of the red one, "Incidents of discrimination, harassment or abusive treatment have occurred".<sup>8</sup>

The BCC is designed to be applied on a voluntary basis since it is the by-product of a private initiative bought into being by the GCP. In this sense, it is an example of a private standard originating from a third party (the GCP), managed by an independent entity (the CAS) that acts as a certification body, and is designed to be applied by multiple users.

*The Supplier Code of Conduct of Starbucks Corporation*

The second case study concerns the Starbucks Supplier Code of Conduct (SCC).<sup>9</sup> There are two texts that are relevant in this regard: the Supplier Code of Conduct and the supplemental Starbucks Supplier Social Responsibility Standards (SSRS).<sup>10</sup> Both determine the social obligations that Starbucks' suppliers agree to fulfill; they are both quoted in the Supplier Guidance Global Requirements (GGR),<sup>11</sup> thereby defining the standards that are applied to suppliers concerning not only socio-ethical sustainability, but also coffee quality, business processes, use of logos and trademarks, and packing and shipping requirements.

This latter document is relevant since it provides that all the standards established in the GGR (including, therefore, the SCC and the SSRS) are requirements "supported by our Standard Terms and Conditions and/or additional contract (including purchasing documents). Failure to meet the requirements outlined here may result in the collection of damages and eventual termination of the relationship". The language employed is rather clear. The standards Starbucks requires suppliers to follow are part of the contractual relationship that exists between Starbucks and its suppliers: if the latter fail to comply with these standards, this gives rise to breach of contract (and the possibility that Starbucks will ask for compensation for damages and terminate the contractual relationship).

Going back to the SCC and the SSRS, we note that they are very concise documents. SCC is only one page long, is dated June 2004, and lists five principles suppliers are required to comply with.<sup>12</sup> These principles are more fully specified in the SSRS. What it is worth noting again is the idea that the SCC and SSRS are binding since they are part of a contract suppliers are required to sign. In order to reinforce such provisions, the SCC states that "Failure to comply, or failure to work with Starbucks or a third party to correct non-complying situations, are grounds for cancellation of open orders, discontinued use of non-complying production sites, or termination of our business relationship".<sup>13</sup> The SSRS is four pages long, is dated November 2006, and is built around six sections: Transparency, Worker Health and Safety, Worker Treatment and Rights, Worker Hours and Compensation, Environmental Protection, Compliance and Corrective Action. The standards established in the six sections are supplemental with regard to the minimum requirement specified in the introduction of the SSRS itself, according to which suppliers have "to comply with all applicable laws, codes and regulations, including health codes, employment and discrimination laws, environmental regulations, safety codes and building ordinances for each location in which they do business".

It is clear that these private standards are integrating, not supplanting, public norms. Two other points deserve to be highlighted. First, most of the SSRS is focused on workers' conditions; only one section is devoted to the protection of the environment and no specific section focuses on other stakeholders' interests. Starbucks' primary interest seems thus to be in labour conditions and workers' rights, while other economic, social

and environmental issues play a minor role. Second, the first section in the SSRS establishes a transparency principle which appears to represent a prerequisite with respect to the implementation of the other principles listed in the document. The transparency principle requires suppliers to disclose conditions that might clash with the principles and values encapsulated in the standard; moreover, they are required to give Starbucks, or third parties designated by Starbucks, access "... to their operations, policies, processes, and relevant records" and to allow for "unannounced inspections of their records and facilities".

The SCC and SSRS represent another example of private standards that Starbucks uses to vertically coordinate its supply chain. The use of private standards to control suppliers is evident if we consider that Starbucks has unilaterally elaborated its own standards, differently from in the case of BCC where the standards were the output of a joint effort by different stakeholders. Starbucks' control over the standardization process is probably motivated by the need to have standards that are more in line with Starbucks' necessities and concerns.

*The Responsible Supply Chain Process applied by Illycaffè S.p.A.*

The third case study concerns the Responsible Supply Chain Process standard (RSCP)<sup>14</sup> employed by the coffee roasting and espresso producing company Illy.<sup>15</sup> This standard was developed by *Det Norske Veritas* (DNV),<sup>16</sup> one of the leading standard-setters and certification bodies worldwide. Initially, the RSCP standard was elaborated with reference to the coffee sector and later expanded to other production areas.<sup>17</sup> The standard is not available online and therefore cannot be analysed in detail. Nonetheless, DNV describes it as a system tailored to the "company's own strategic decisions and core products," which therefore implies a thorough analysis of the congruence of the company's processes and products with its goals. The final aim is to create an effective management system "of all major risks associated with environmental performance and pollution reduction; product quality & consumer issues; product safety; labor & fair operating practices; local community engagement; risks to human resources and human rights".<sup>18</sup> Thus, the RSCP is a management standard used to help companies to structure and then operate their sustainability policies. It is the company that provides the content of these policies, while the standard is conducive to maintaining them. Illy was the first company worldwide to apply this standard and to be certified as compliant with it. Indeed, it seems that Illy was a sort of pilot project in terms of developing the standard itself, and thus, in a circular way, contributed to shaping the standard's contents.

Even if the RSCP standard is not available, we can analyse the Sustainability Policy published by Illy.<sup>19</sup> This document is one of the most important outputs of the process described above through which the standard was employed to help the company (Illy) to build (and then make effective) their sustainability policies. The Sustainability Policy employs a long-term time horizon since the document covers the period until 2030. There are two sections of the text that are worth mentioning. First, the methodological approach.

The first step involves analysing seventeen sustainable development goals, then identifying nine macro-objectives, including targets in relation to each macro-objective, and finally creating a sustainability action plan spanning from 2017 to 2021. The second part of the text concerns sustainability commitments for 2030. These cover three macro-areas: responsible supply chain and sustainable agriculture; happiness and quality of life; circular economy,<sup>20</sup> and innovation.

In Illy's Sustainability Policy document, we cannot find any references to the protection of human rights: the focus seems to be more on environmental and economic sustainability than on social sustainability. However, this does not mean that the protection of human rights is not a part of Illy's policies. In a related webpage devoted to sustainability there is a section specifically concerning human rights.<sup>21</sup> There are references both to international agreements and guidelines<sup>22</sup> Illy complies with, and to the RSCP standard.<sup>23</sup> In addition, it is expressly provided that Illy will include "explicit reference to the Code of Ethics in all contracts, though a clause on respect for human rights in procurement and along the supply chain". Thus, all the standards, internal policies and international guidelines created and/or applied by Illy become contractual obligations that suppliers must comply with.

The DNV standard offers another example of a private standard incorporated into a contract. Differently from the other two case studies, it involves a third-way solution by which the standard setter does not establish the sustainability standards companies must comply with, but rather the methodology through which each single company can create its own sustainability policies.

#### 4 Comparative remarks

The comparison of the three case studies leads to the following conclusions.

1. In all case studies, references to human rights have been included in private standards. In other terms, the protection of human rights provided for in international conventions and agreements has been "translated" into private norms and principles. The reasons why such "translation" has taken place is never clearly specified. Sometimes it appears to be part of a marketing strategy, especially when private corporations are directly involved (e.g. Starbucks and Illy): developing standards (Starbucks) or adhering to standards (Illy) concerning CSR is a way to signal to the market that corporations are not only profit-driven but also care about values other than money. In particular, it is a way to attract those consumers who are most interested in the protection of such values (Giovannucci and Ponte 2005, 287; Poncibò 2007). Even if references are to values other than money, it should be borne in mind that compliance with these standards is in any case market-oriented and thus it is impossible to avoid a profit-driven logic. In other cases, the reasons why private standards have been developed are more mixed. In the case of BCC (Case Study 1), some of the subjects who partake of this initiative are enterprises



and are most likely market-driven in their choices, much as in the cases of Starbucks (Case Study 2) and Illy (Case Study 3). However, in Case Study 1 we can identify other, non-profit-oriented stakeholders who participate in the BCC initiative, such as civil society organizations, trade unions and public institutions. Here, a market logic probably does not reflect all the interests involved in the choice to take part in the BCC.

2. The BCC evaluation system (Case Study 1) classifies three possible variations in terms of compliance with the specified norms: the optimal situation (green colour), an acceptable situation (yellow colour) and an unacceptable one (red colour). The classification system is not binary (achievement of a goal/lack of achievement of a goal), but more nuanced thanks to the introduction of the yellow scenario. This adds flexibility in terms of pursuing sustainability goals.
3. Some standards (for example, Starbucks' SSRS in Case Study 2) focus more on social issues (labour conditions and workers' rights) than on other ones (environmental protection, community interests, etc.). Other standards like the BCC (Case Study 1), are broader in their focus, taking into account social, environmental and economic variables and giving them balanced consideration. The DNV standard represents a third possible way (Case Study 3), with more of a focus on the methodology that chain leaders should follow in building their sustainability policies.
4. In the BCC case (Case Study 1), the production of the standard is centralized through the operation of an international professional association for the sector: the Global Coffee Platform (GCP), which has specific expertise and is directly involved in the sector in connection with which the standards are established. In Starbucks' case, the standards are created directly by the chain leader and are thus internal and unilateral. In the case of Illy, the standard that is employed is created by a third party and is not sector-specific. The case of Illy (Case Study 2) is an interesting one since the RSCP standard does not directly define the sustainability policies the company has to implement, but rather provides for procedures and methods for building such policies and managing them. Thus in the case of Illy we find a sort of third-way solution with respect to the two alternative solutions represented by BCC (Case Study 1) and SCC (Case Study 1). Indeed, sustainability policies in these two cases are neither written at a centralized level (as in the BCC case) nor unilaterally at the company level (as in the Starbucks case). Rather, in Case Study 3 the resulting policies are the output of cooperation between, on the one hand, the company which sets the standard, verifies compliance and issues the respective certification (DNV) and, on the other hand, the company that implements it (Illy).
5. The level of detail of the standards can differ. Sometimes they are quite detailed and specific, as in the case of BCC (Case Study 1), while sometimes they are represented in the form of short principles, as in the example of Starbucks' SCC (Case Study 2). Finally, sometimes the standards are generic, meaning that they are not specifically tailored to the coffee sector, as in the case of Illy (Case Study 3).

6. With regard to verification of compliance with the standards, the systems described in the above case studies explicitly include some kind of monitoring mechanisms, even if the strategies for verifying them differ. In the case of Illy (Case Study 3), there is a private certification body (DNV) which is internationally recognized, operates in many sectors, and applies different types of standards. In the BCC case (Case Study 1), CAS, a dedicated certification body, has been established, which is again a private entity with very specific expertise and a focus only on the verification of the BCC. In the Starbucks case (Case Study 2), the company refers to two possible ways of verifying compliance: audits conducted by Starbucks itself, or by a third party designated by the company.

It should be added that the use of private standards to promote CSR and the protection of human rights is not a panacea. This approach has its problems and limits. For example, with reference to the coffee supply chain and in particular to Fair Trade certified coffee<sup>24</sup> – a type of certification in which the protection of human rights and social responsibility in general plays a pivotal role – Haight (2011, 76) points to at least four such limitations.

- First, market conditions (e.g. the price for premium quality coffee) can have a huge impact on the effectiveness of these social sustainability schemes: there are cases in which coffee farmers' cooperatives "are choosing to default on their Fair Trade contracts" due to the higher prices they can get on the open market.
- Second, the main focus of Fair Trade standards is small farmers, meant as small landowners, since these standards are addressed at cooperatives and a prerequisite of becoming a member of the cooperative is being a small landowner. This implies that the interests of the migrant laborers who represent the poorest segment of the coffee community and are not part of the cooperatives are marginalized.
- Third, there is a lack of transparency in business dealings due to several factors, such as – for example – the fact that documents are not translated into a language that farmers can understand. This implies that farmers cannot control how the extra money the cooperative gets because of the Fair Trade scheme is spent. Thus, "records kept by cooperatives have shown that premiums paid for Fair Trade coffee are often used not for schools or organic farming but to build nicer facilities for cooperatives or to pay for extra office staff".
- Finally, Fair Trade "provides incentives for some farmers to remain in the coffee business even though the market signals that they will not be successful. If a coffee farmer's cost of production is higher than he is able to obtain for his product, he will go out of business. By offering a higher price, Fair Trade keeps him in a business for which his land may not be suitable".

In general, Reynolds *et al.* (2007, 159) note that some of the certification initiatives in the coffee sector lack a robust democratic basis since in some cases NGOs and certification systems are being used to legitimize the control of processors and distributors over the coffee supply chain. The point is reinforced by considering that "certifications reflect Northern-based standards and procedures and may raise barriers to

entry for producers". Macdonald (2007, 809) stresses the fact that while codes of conduct have contributed to the empowerment of marginalized groups, there is still a lack of cooperation between public and private actors whose decisions can affect the conditions of such groups. Neilson (2008, 1619) highlights the issue of cost. Namely, the implementation of the standards defined in the codes of conduct requires financial investment that might be unavailable to farmers: "Corporate self regulation imposes requirements without necessarily offering developmental support". Finally, Neilson and Pritchard (2007, 328) note that private standards, CSR and codes of conduct run the risk of being perceived as vehicles of a neo-imperialist agenda due to "allegations of regulatory capture by corporate interests" and to the imposition of the "audit-culture mentality of Western corporate models".

## 5 Conclusions

The paper introduces readers to a complex and rapidly evolving area in which the law interacts with rural development in order to promote the latter. But rather than using the traditional tools of public law (taxation, direct payments, the building of infrastructure, etc.), the chapter seeks to show how rural development can be promoted through the use of the tools of private law, namely private standards, certification and contracts. The angle from which the phenomenon has been analysed is quite specific: the relationship between private law, rural development and the protection of fundamental rights. Such a relationship does exist and is becoming more important in a context in which consumers are increasingly interested in social sustainability, borders are becoming porous, and supply chains more global, yet there are still major differences in the level of protection of human rights in different countries. Even if the subject matter touched upon here seems quite narrow, it represents a first introduction into the complexities that characterize rural development and international supply chains.

### Notes:

<sup>1</sup> See the Preamble of the Declaration: '... recognition of the inherent dignity and of the equal and inalienable rights of all members of the human family is the foundation of freedom, justice and peace in the world'. See also Art. 1 of the European Convention on Human Rights, 4 November 1950: 'The High Contracting Parties shall secure to everyone within their jurisdiction the rights and freedoms defined in Section I of this Convention'.

<sup>2</sup> These rules employ specific indexes to determine which national law should be applied: for example, the place where the activity provided for in the contract must be conducted; the presence of contractual clauses specifying which national law prevails, etc.

<sup>3</sup> An example in the field of contract law is represented by the United Nations Convention on Contracts for the International Sale of Goods, signed in Vienna in 1980.

<sup>4</sup> Corporate Social Responsibility (CSR) is a type of self-regulation by international private business aimed at ensuring the implementation of certain ethical principles in the operation of businesses.

<sup>5</sup> BCC = Baseline Common Code, a document which forms the basis of the voluntary self-regulation of the companies in the coffee sector. The document is a collection of economic, social, environmental and food safety rules and principles.

<sup>6</sup> GCP = Global Coffee Platform: an international professional association of the coffee sector. Available at: <https://www.globalcoffeeplatform.org/> (15 March, 2019).

<sup>7</sup> CAS = Coffee Assurance Services is a private company which owns and operates the so-called "4C coffee certification system".

<sup>8</sup> See p. 16 of the BCC.

<sup>9</sup> Starbucks Corporation is an American coffee company and coffeehouse chain. As of 2018, the company was operating in 28,218 locations worldwide. For its Supplier Code of Conduct see: <https://www.starbucks.com/business/suppliers>; see also: <https://www.starbucks.com/about-us/company-information/business-ethics-and-compliance> (15 March, 2019).

<sup>10</sup> SSRS = Starbucks Supplier Social Responsibility Standards: a set of social criteria for becoming a supplier of the Starbucks Company.

<sup>11</sup> GGR= Supplier Guidance Global Requirements: a set of criteria for becoming a supplier of Starbucks Company.

<sup>12</sup> The principles are: "Demonstrating commitment to the welfare, economic improvement and sustainability of the people and places that produce our products and services; Adherence to local laws and international standards regarding human rights, workplace safety, and worker compensation and treatment; Meeting or exceeding national laws and international standards for environmental protection, and minimizing negative environmental impacts of suppliers' operations; Commitment to measuring, monitoring, reporting and verification of compliance to this code; Pursuing continuous improvement of these social and environmental principles".

<sup>13</sup> The final section of the SSRS contains a similar provision, although more detailed: "Failure to meet a corrective action plan commitment will be considered a material breach of our agreement and may result in cancellation of current orders and/or termination of our contractual relationship. Gross violations or illegal activities will be cause for outright and immediate termination of our contractual and business relationship" (bold in original).

<sup>14</sup> RSCP = Responsible Supply Chain Process standard; a certification system. Initially applied to the green coffee supply chain, it has since become a model for use with any kind of product line. See <https://www.dnvgl.com/services/responsible-supply-chain-process-certification-11193> (15 March, 2019).

<sup>15</sup> Illycaffè S.p.A. (branded as illy) is an Italian coffee roasting company that specializes in the production of espresso.

<sup>16</sup> DNV GL = Det Norske Veritas - Germanischer Lloyd, an internationally accredited certification society headquartered in Norway. The company provides services for several industries including maritime, renewable energy, oil & gas, electrification, food & beverage and health-care. It was created in 2013 as a result of a merger between two leading organizations in the field, Det Norske Veritas (Norway) and Germanischer Lloyd (Germany).

<sup>17</sup> See <https://www.dnvgl.com/services/responsible-supply-chain-process-certification-11193> (15 March, 2019).

<sup>18</sup> See <https://www.dnvgl.com/services/responsible-supply-chain-process-certification-11193> (15 March, 2019).

<sup>19</sup> See: [http://valuereport.illy.com/pdf/Sustainability\\_Policy\\_2030\\_ENG.pdf](http://valuereport.illy.com/pdf/Sustainability_Policy_2030_ENG.pdf) (15 March, 2019).

<sup>20</sup> Circular economy: a sustainable system of technologies and supply chains in which resource input and waste, emissions and energy leakages are minimized. The linear economy is the opposite, where production is based on a so-called "take, make, dispose" model.

<sup>21</sup> See: <http://valuereport.illy.com/> (15 March, 2019).

<sup>22</sup> “Adherence to the principles of the ILO - International Labor Organization; [...] Adherence to the Global Compact of the United Nations since 2012”.

<sup>23</sup> “Adherence to Responsible Supply Chain Process; Setting out of a Sustainability Policy to represent illycaffè’s values, objectives, commitments and governance in the area of sustainability”.

<sup>24</sup> Fair Trade, as applied to coffee, is one of the standards in the coffee sector with the most stringent social justice standards (Raynolds *et al.* 2007, 159).

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## Environmental Protection and Sustainable Local Development in the United States of America

DON ELLIOTT

**Abstract** Federal, state/provincial/district and local environmental protection regulations form some of the key frameworks within which sustainable local development must occur. Not only does that framework govern the locations and impacts of physical land development, but they also impact the types of new economic activities that can be targeted, the locations where they can locate, and the costs of developing those economic generators. In some countries, there is a strong top-down framework of laws in which local actions are largely constrained by norms and standards established by higher levels of government. In the United States, however, federal environmental controls are largely limited to protection of clean air, clean water, and endangered species and prevention of soil erosion and flooding. Local governments retain much flexibility to adopt additional environmental standards and requirements, and there are significant lessons in how they choose to exercise those authorities. This chapter will review the legal framework of environmental regulation in the United States and the seven types of local environmental regulations that are regularly chosen to supplement higher level controls. Key topics reviewed include regulations to address greenhouse gas emissions, renewable energy/energy conservation, water conservation, urban agriculture/local food production, connectivity/walkability/ public health, waste recycling, and resilience to the impacts of climate change.

**Keywords:** • environmental regulations • greenhouse gas emission • renewable energy conservation • water conservation • urban agriculture • public health • waste recycling • climate change • resilience • United States

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## 1 Background

The United States' federal system of government provides very wide latitude for local city and county governments to regulate land use and development. There are very few federal governmental laws that restrict local initiatives in this area. One significant exception to this general approach is environmental regulation, where both the federal government and many state governments have enacted laws that are binding on local governments and the land development projects that they approve.

Key areas of regulation where the federal government restricts local city and county development activities include:

- The Clean Water Act (CWA), 33 U.S.C. §1251 *et seq.* (1972), which prohibits pollution into the “navigable waters of the United States”, which has been interpreted by the courts to include smaller upstream tributaries whose waters flow into the “navigable waters”. This Act requires the creation of city and county stormwater management systems to ensure that rainfall onto developed areas does not flush pollutants into navigable waters. A very substantial amount of local government time and money is spent complying with the Clean Water Act, and it imposes significant expenses on many development and redevelopment activities.
- The Clean Air Act (CAA), 42 U.S.C. §7401 *et seq.* (1970), which regulates acceptable levels of air pollution. Over time, the private sector has responded to this Act by developing newer and cleaner technologies and equipment that can perform commercial and industrial activities in compliance with the Act. At this point, the major impact of the Clean Air Act is to pressure city governments to restrict or discourage automobile commuting in order to reduce related greenhouse gas emissions.
- The National Environmental Protection Act (NEPA), 42 U.S.C. §§ 4321 *et seq.*, which requires that any project using federal government money perform an Environmental Impact Assessment that evaluates the environmental and social impacts of a proposed project against alternatives (including the impacts of not doing the project at all). There is no requirement that the local government choose the alternative with the least impacts; simply that they take a “hard look” at those impacts through a public process before making a decision. Since many expensive infrastructure projects in the United States rely on federal grants or loans, the preparation of Environmental Impact Assessments has become a consulting industry, and substantial time and expense is required to comply with the Act. Some local governments respond to the Act by trying to avoid the use of federal funds, but some of the 50 states have adopted state-level versions of NEPA that apply whenever state government monies are involved.
- The Endangered Species Act (ESA), 16 U.S.C. Sections 1531–1544, which prevents development projects that would “take” species of animals that have been listed as “endangered” by the federal government. In practice, the prohibition of “taking” a species means that the project cannot damage or reduce the habitat for that species



(with some exceptions) unless there is adequate mitigation through enhancement or creation of additional habitat. The ESA affects land use in rural areas of the United States more than urban areas.

All local governments must comply with these four federal Acts. In addition, some of the 50 states (notably the most developed and populated states on the East and West coasts of the U.S.) have adopted additional environmental regulations that are binding on local governments. Other states have adopted no additional regulations.

### **1.1 Local regulations to promote environmental sustainability**

With few exceptions, U.S. cities and counties do not adopt additional restrictions to protect clean water or endangered species; they consider compliance with the federal and state acts in these areas to be adequate. Instead, local regulations for environmental sustainability focus on the following key areas where local zoning and land use regulations can make a significant difference:

- a. Greenhouse gas emissions;
- b. Renewable energy and energy conservation;
- c. Water conservation;
- d. Urban agriculture and local food production;
- e. Connectivity, walkability, and public health;
- f. Waste recycling; and
- g. Resilience to risks created by climate change.

#### *Reduction of greenhouse gas emissions*

Although the federal Clean Air Act imposes national standards for air quality, many citizens want their local governments to do what they can to reduce emissions of greenhouse gasses that contribute to climate change even if their community already complies with Clean Air Act standards. This is one area where local land use zoning can make a significant contribution to sustainable development in three different ways. First, many local zoning ordinances are being revised to allow more mixed-use development – development that allows a mix of residential and commercial uses. Allowing a mix of “living” and “working” uses in medium and high intensity development areas allows citizens to choose to live closer to where they work, and an increasing number choose to do so. Second, many zoning ordinances are being revised to allow a wider range of home-based business activities, which can significantly reduce the need for commuting to work. Finally, local land development regulations are being revised to require more connectivity within and between neighborhoods (discussed in more detail below).

#### *Renewable energy and energy conservation*

The United States is in the middle of a change to reduce the use of fossil fuels for the generation of electricity, and many newer zoning regulations are being drafted to encourage that change. Some regulations are being revised to require compliance with

the U.S. Leadership in Energy and Environmental Design (LEED) standards for energy efficiency, while others offer development incentives that allow larger buildings or higher lot coverage for projects that comply with LEED standards. Still other local zoning regulations are being revised to require or encourage east-west orientation of blocks and buildings to increase solar access or pre-wiring homes and businesses for future installation of solar energy devices. Many local codes are also being revised to authorize the installation of (1) geothermal energy facilities in any required open yard area, (2) solar energy panels in rear or side yards or on rooftops, and (3) wind energy facilities in side or rear yards of multi-family and non-residential development (but generally not low-density residential areas because of the significant equipment heights required for efficient electricity production). In addition, many newer regulations are broadening the definition of allowed automobile fueling stations to include alternative fuels, and others are encouraging or requiring the installation of electric vehicle charging facilities in larger development projects.

#### *Conserving water*

While some parts of the United States have ample water supplies, others – particularly in the West – have arid or semi-desert climates and too little water to support anticipated future populations. In dry areas of the country, water utilities are increasingly requiring the installation of water efficient appliances and fixtures. In addition, local governments are increasingly adopting zoning regulations that restrict the amount of irrigated landscape areas in order to conserve available water supplies for drinking purposes. Other local codes establish a “water budget” for different types of development and charge significantly higher water rates for developments that exceed those budgets. Finally, a few zoning and development codes are being revised to encourage the installation of grey water recycling systems that allow the reuse of once-used water for purposes other than human consumption. Progress towards implementation of gray water systems in private development has been slow because of the significant additional costs of installing a “two-pipe” system, but some larger public projects have absorbed those costs in order to demonstrate the feasibility and water savings that can result.

#### *Promoting urban agriculture and local food production*

A fourth area where local zoning and development regulations are encouraging sustainable development is in the promotion of local food production in urban areas. While backyard gardening has always been allowed as a secondary use of land, new zoning codes often now recognize community gardens and urban agriculture as a primary use of land. Often, urban agriculture uses are allowed in almost all zone districts, the size of the activity is limited to about the size of a city block, and the amount of the site that can be covered by structures (greenhouses and storage areas) is limited. Increasingly, these regulations allow for the sale of vegetables and crops grown on site, and a slowly growing number allow for minor food processing activities to occur on the same site. In many communities, interest in local food production is so strong that these food processing and sale activities are permitted even in residential zone districts, where the

conduct of commercial activities is (in theory) supposed to be strictly limited. In addition, many newer zoning regulations allow permanent or temporary farmer's markets in a wider variety of locations in order to encourage the wider distribution of locally grown foods.

*Strengthening connectivity, walkability, and public health*

As noted above, many cities and counties are revising their zoning ordinances to allow for a mix of uses that will allow their citizens to live closer to where they work. In addition, many local regulations are being revised to require that development and redevelopment be designed with smaller blocks, or with mid-block pedestrian passages, or increased connectivity both within the development and from the new project to existing surrounding development. The primary goal of these regulations is to shorten the potential walking, bicycling, and driving distance between two points in nearby areas so that more citizens decide to walk or bicycle between those destinations, and so those who choose to drive a vehicle will have a shorter drive (with fewer related greenhouse gas emissions). In mature urban areas, some of these regulations require that new projects extend and connect with the street and block structure of the surrounding area. In developing areas they sometimes require the use of a "connectivity index," which counts the number of street sections and intersections (points of connection) in a proposed development and requires at least a minimum number of connection points that can offer alternative routes and shorten travel times. A second goal of these regulations is to promote public health by making it easier to walk or bicycle between neighborhood destinations. As a corollary, many local regulations are being revised to eliminate exceptions to a general requirement to install sidewalks each time a new development or redevelopment project occurs. Still others regulations now require that convenient pedestrian-friendly walkways and bicycle-friendly routes be provided through or around larger parking lots so that those lots do not discourage those who would otherwise walk or bike to the establishment from doing so.

*Recycling waste*

In order to encourage recycling – rather than disposal – of waste a growing number of new zoning ordinances are requiring that multi-family, commercial, institutional, and industrial sites be designed to include a location for waste recycling containers that are easily accessible by service vehicles while also minimizing impacts on surrounding development. Because construction waste makes up a high percentage of waste deposited in landfills, a slowly growing number of local regulations are encouraging or requiring that a percentage of construction waste be transported to a construction waste recycling facility if one is located within a stated distance of the site. While many areas do not have such a facility nearby, regulations such as these may help create a market that will make construction waste recycling facilities more economically feasible in the future.

*Resilience to risks created by climate change*

Finally, a growing number of local zoning and land development regulations are being revised to encourage or require development to be located or designed to minimize the risks related to climate change. Along the East and West coasts of the United States, and in Hawaii, these regulations focus primarily on sea level rise. In the arid Western U.S., they often focus on increased risks of wildfire on the vast areas of public lands located near major population centers. Throughout the country, they are also beginning to address the likelihood of increased flooding from rivers and streams as trends toward more frequent and more intense storms combine with increasing populations in flood-prone areas. An increasing number of regulations are based on available (but admittedly imperfect) modeling and mapping of areas affected by sea level rise, wildfires, and flooding, although arguments about the accuracy of the models and maps are common. A second type of regulations requires buildings to be designed so that humans and equipment are located higher in the building (and further from potential tides and floodwaters). A third type of regulation requires that buildings with human occupancy be located further from wildfire risk areas than they were in the past. Some jurisdictions are also revising their approach to development in flood prone area to require not only the raising of structures higher above anticipated flood levels, but to require that any construction in those areas not result in upstream or downstream impacts on other properties.

**2 New York City's responses to super Storm Sandy**

In 2012, New York City was battered by one of the most intense storms in its history. Fifty-three people lost their lives and an estimated \$19 billion of property damage was sustained. Rebuilding of the South Ferry subway station by itself cost \$369 million, making it one of the most expensive subway station projects ever undertaken by the city. One positive outcome of the Super Storm Sandy tragedy was that New York City invested heavily in research to determine what could be done to avoid similar damage in the future. Much of this research was aimed at understanding and promoting “resilience” – a community’s ability to rebound quickly from shocks while reducing the risk of future similar events.<sup>1</sup>

Among the basic strategy discussions in all projects to improve the resilience of urban areas is the question of “retreat” versus “harden”. Strategies to harden urban areas include investments in seawalls or other constructed barriers to keep tide and floodwaters and other environmental hazards away from people and important buildings, and they tend to be very expensive. Strategies to retreat from risks include regulations to increase setbacks from waterfront, riverfront, and high fire risk areas over time, and sometimes also include programs to relocate people away from at-risk areas. Retreat strategies also tend to be very expensive, but sometimes less expensive than hardening strategies. Many communities that have this policy discussion decide that a combination of retreat and hardening strategies need to be considered, and that hardening strategies can only be

afforded when the value of existing buildings and improvements and the number of people living and working in at risk from climate change is very high. Because of the very high population density and property values in Manhattan and other areas, New York decided that hardening approaches were justified in some cases.<sup>2</sup>

In addition, however, research revealed that there were a number of strategies that could have limited property damage and risks to human life without investing in expensive public infrastructure to harden the city. Potential strategies to minimize and mitigate damage from predicted serious storms in the future include:

- Increasing the “freeboard” – i.e. the elevation of the building ground floor above the water levels indicated by flood modeling – above the current federal standard of one foot to two or three feet.
- Requiring “compensatory storage” – i.e. requiring that for each one cubic foot of floodwater that will no longer rest on your land because you raised the elevation of the land or created new improvements, you must buy and donate one cubic foot of floodwater storage capacity somewhere else in or adjacent to the floodplain.
- Designing public parks and required open spaces so they can act as water storage facilities (“flood parks”) during severe storm events, as the City of New Orleans has begun designing after the damage from Hurricane Katrina.
- Designing ground floors of structures in or near floodplains so that they do not contain key electric, water, or sewer equipment and so that water can flow into (and out of) them during severe storms without weakening the structure supporting higher floors of the building or interfering with the use of those higher floors.
- Ensuring that all key building system equipment for hospitals, nursing homes, and other facilities with sensitive or less mobile residents are located on upper floors of the building, so that inundation of the ground floor does not affect light, electricity, water, sewer, or communications services to the rest of the building.
- Designing integrated flood protection systems along coastlines with “tiers” of flood defenses so that areas generally usable by the public (i.e. walkways or landscaped areas) only get inundated with water during the most severe floods.

Obviously, all of these solutions cost money, but the incremental cost of implementing many of these changes as individual buildings are built or rebuilt, and as public improvements are constructed, can help reduce the need for even more expensive hardening structures or retreat strategies, or can delay the dates on which some of those more expensive strategies will need to be implemented.

### 3 Conclusion

Within the United States system of land development regulation, local governments retain much autonomy to regulate the environmental and sustainability impacts of land development. There is no national building construction code, land use zoning ordinance, or land subdivision law. Federal law does establish and enforce minimum standards for clean air, clean water, protection of endangered species, and environmental analysis of projects that use federal funds. Some state governments have parallel systems or additional controls, but many do not.

While only a few local city and county governments have duplicated these federal and state controls, a number have gone beyond the topics covered by federal law to promote more economically and environmentally sustainable development. More specifically, U.S. local governments are increasingly using their land use zoning and regulatory powers to promote:

- Reductions in greenhouse gasses, primarily through allowing more mixed use development;
- The use of renewable energy, and conservation of energy in general;
- Water conservation;
- Connectivity between developments, and walkability/bikeability in general;
- Local food production;
- Waste recycling; and
- Improved resilience to risks created by climate change.

While innovations in each of these areas is occurring throughout the country, the vast volume of research conducted by New York City following the extensive damage of Super Storm Sandy has been particularly helpful in understanding how cities and counties can act to respond to the anticipated impacts of climate change.

#### Notes:

<sup>1</sup> See, for example, *Lessons from Sandy: Federal Policies to Build Climate-Resilient Coastal Regions*.

<sup>2</sup> See, for example, *Vision 2020: New York Comprehensive Waterfront Plan*, New York City Department of City Planning, March 2011.

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## Land Use Planning and Zoning as Key Tools in Sustainable Local Development in the United States of America

DON ELLIOTT

**Abstract** The pattern of local land use and development has a large influence on both the economic and environmental sustainability of future development. Patterns of land use that require separation of employment opportunities from housing require longer commutes to work that create greenhouse gasses, or as an alternative require higher and more expensive investments in public transit to reduce those greenhouse gas emissions. They also limit housing choices for those who could and would live closer to their places of work and increase the total cost of housing and commuting costs, which tends to drive up labor costs and make local economies less competitive. As an alternative to creating these types of barriers, local planning and zoning controls can offer incentives such as increased development density, height, or land coverage, to new projects that incorporate mixed residential and non-residential use, particularly if those developments attract or incorporate new businesses in areas where the community has a natural competitive advantage. The United States' decentralized system of land use regulation has both advantages and disadvantages in achieving more sustainable development. Advantages include wide latitude for its hundreds of thousands of local governments to innovate in the design and implementation of land use controls; disadvantages include the relatively weak power of the federal government to mandate preferred sustainable development patterns. This chapter reviews the use of land use controls to achieve sustainable development goals in a decentralized system, and the impacts that trends toward global economic integration, greater public sector efficiency, and increased public participation in land use decisions have on those local efforts.

**Keywords:** • land use • zoning • local planning • sustainable local development

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## 1 The U.S. governmental framework for sustainable local development

In the United States, sustainable local development is primarily a function of local government initiatives. While the federal government offers grants and loans to city and county governments to implement policies it favors, there are never enough federal funds to meet local demands, and those funds are declining over time. In addition, the federal government does not have general powers to regulate the use and development of land in the states or cities. Federal protections for civil rights (such as the Civil Rights Act of 1964, Pub.L. 88-352, 78 Stat. 241 (1964)) and for the environment (such as the Clean Air Act, 42 U.S.C. §7401 et seq. (1970) or Clean Water Act, 33 U.S.C. §1251 et seq. (1972)) limit some land use and development activities, but in general the government in Washington only tells states and cities what they cannot do in these areas – it does not tell them what they can or must do on or with the land in their communities. In short, there is no national system of land use planning or regulation that ensures that local cities and counties manage and develop their land to help achieve national economic or social priorities. The power to regulate private land in the U.S. is almost exclusively held by state and local governments.

While some of the 50 state governments in the U.S. have a state-mandated system of planning and zoning (i.e. one in which cities and counties must plan and regulate use and development to implement state priorities), many other states do not have such a system. Statewide planning systems typically (1) establish several statewide planning goals (for example, to allow for the provision of housing for all citizens reasonably expected to live in the community), (2) require that cities and counties prepare periodic land use plans that reflect those goals, and (3) require that cities and counties then adjust their land use regulations to be consistent with those local plans. In some states, the state government reviews all local plans to ensure that they are consistent with state goals, but in other states the local plans and regulations are presumed to be consistent with statewide goals unless someone complains and asks for a state-level review. In both cases, however, there is usually wide latitude for cities and counties to decide how and to what degree they want to implement state priorities; only those plans that clearly ignore or are clearly inconsistent with state goals are required to be revised.

In the majority of U.S. states, however, there is no statewide planning system or regulatory review procedures, and most powers to plan and regulate land development are given to local governments. In “Dillon’s Rule” states, cities and counties only have those powers that are explicitly granted to them by the state government, while in “Home Rule” states cities and counties have all power to regulate land use and development except in specific cases where the state government retains control.

Like the federal government, many state governments offer grants and loans to support cities and counties that want to implement programs that benefit state priorities, but money is always in short supply, and grants often come with conditions that make them



less attractive to local governments. While the United States federal system of government provides some of the explanation for why land is controlled at the local level, there is another key factor. There is a strong belief that neither the federal nor the state government has the detailed knowledge of local economic and political realities or opportunities to make the nuanced choices necessary to make local economic development successful. For all of these reasons, in the U.S. almost all decisions about how a city or county regulates private land are made at the local level.

## **2 The role of zoning and land use regulations in sustainable local development**

Local land use controls are a critical element in promoting sustainable local economic development. If local regulations prohibit a land use for which there is market demand, or impose too many conditions and restrictions on that type of use or development, or allow development to be completed with unsustainable materials and technologies, they inhibit the very type of economic development they probably want to promote.

Most local land use regulations are contained in zoning controls adopted at the local level. Zoning controls what can be built, and what activities can occur, on land in each “zoning district”. A local government can adopt as many zoning districts as it likes, but the zoning regulations are supposed to treat all similar properties in a specific zoning district similarly. For example, all office buildings in a particular zoning district are intended to be controlled by generally similar regulations for the height and size of the building, its location on the lot, and the allowed uses of the property.

U.S. cities and counties that want to promote environmentally and economically sustainable development need to review their zoning regulations to identify:

- Barriers to development that can be removed;
- Incentives to sustainable development that can be offered; and
- New regulations that may be needed to ensure that future development is sustainable.

Barriers to sustainable development can include:

- Minimum land parcel sizes that are too large to be economic, and that are not needed to preserve intended character;
- Maximum building intensities or heights that prevent economic development, and that are not needed to preserve character;
- Automobile parking requirements that are higher than needed to prevent traffic congestion – particularly for new and creative forms of development;
- Required building design features that increase the cost of development more than they contribute to the positive image of the surrounding area; and
- Requiring renewable energy features (such as solar or wind facilities) to be set back from property lines at least as far as the primary building.

Most local governments have the ability to offer incentives to encourage types of building and land use that are more supportive of local planning goals. Incentives can include:

- Allowing taller buildings for projects that include affordable housing, or mixed use development, or that provide more space for community meetings, training events, or preferred land uses (such as child care);
- Allowing the builder to provide less automobile parking if the builder agrees to implement Transportation Demand Management (TDM) tools to reduce auto and truck traffic to and from the development; or
- Allowing buildings to have a lower level of architectural detailing or material quality in return for commitments that the space will remain occupied by priority commercial or economic activities.

If these types of incentives are offered, it is important to “test” them for economic reality – to ensure that the costs of providing the required benefit to the city or county does not exceed the value of the incentive to the builder. Investors will not apply for or use incentives that do not pass this test.

Even after removing barriers and providing incentives, however, it is sometimes necessary to adopt new regulations to ensure that new development and redevelopment are both economically and environmentally sustainable. Examples of new regulations that can promote sustainability include:

- Requiring that new development be oriented on an east-west axis to the maximum extent practicable in order to maximize solar orientation;
- Limiting the number of automobile spaces provided on-site in order to avoid creation of large expanses of parking that will seldom be used, will create stormwater runoff, and will make it more difficult to walk or bicycle between uses;
- Requiring the preservation of all large mature trees to the maximum extent practicable, in order to preserve the site’s ability to absorb carbon dioxide emissions;
- Allowing expedited review and approval procedures for projects that will create or preserve desired economic activity; and
- Requiring that all landscaping installed on the site be water-conserving.

These three categories of action overlap. For example, some goals that can be achieved by adopting new regulations can also be achieved by offering economically realistic incentives. The choice of which approaches to use, and in what combination, is almost always up to the local city or county government. Carefully evaluating the land use, development, and redevelopment needs in target economic sectors, and then revising zoning regulations to make it easier to build and operate facilities in those sectors, is a key element of sustainable local development. In fact, the failure to use these tools and to align them with the community’s sustainable development goals is generally one of the first items mentioned by the private sector when questioned as to why desired economic development is not happening.

### 3 Three cross-cutting challenges

As the United States' local governments strive to align their existing zoning tools with their sustainable development goals, they face three complicating factors:

- Global economic competition;
- Pressures for efficient public administration; and
- Desire for more, and more effective, citizen participation.

Global economic competition affects local government efforts at zoning reform because many types of jobs and economic activities can now be conducted over the internet, and tend to be performed wherever the skills necessary to perform the job are available at lowest cost. Even when large companies are subject to reviews or penalties that discourage or prohibit them from “outsourcing” work to other cities or countries, those regulations rarely apply to the type of small businesses and entrepreneurial start-ups that most cities and counties want to encourage. Regulations that add to the costs of developing or redeveloping land or buildings run the risk of encouraging “portable” economic activities to be moved elsewhere. To avoid this result, cities and counties tend to focus on the creation of local economic activities that:

- Rely on resources that are only available in their area; or
- Take advantage of a local concentration of businesses that can serve as suppliers to, or customers for, that specific good or service; or
- Do not involve the types of general information or data management skills that can easily be relocated to another community.

These constraints significantly narrow the types of sustainable economic development pursued by local governments.

A second trend (not just in the United States but globally) is the pressure for local governments to perform their functions more efficiently. Local governmental employees are supported primarily by local taxes, and the costs of public employees and their related pensions and benefits are by far the largest expense of city and county governments. As a result, there is continuing pressure on U.S. local governments to (1) replace workers with technology or equipment, (2) not replace workers who retire, and (3) not hire additional workers if their work can be performed through investments in technology or equipment. This also limits the types of sustainable local development that cities and counties can consider, because most new programs or approaches to sustainability that require additional staff will be disfavored. Two examples are listed below:

- In many cases, stormwater water pollution from streets can be significantly reduced by having that water flow into bio-swales or vegetated areas, or by using “pervious pavers” that allow water with road pollutants to enter the soil rather than streams and rivers. However, these techniques require periodic mowing and cleaning of the small areas of pervious surface to keep them functioning well, and many local

governments do not want to hire the additional employees needed to perform that new function.

- Since most economic growth in the U.S. is created by small businesses<sup>1</sup> (even though many small businesses fail), some communities have created “incubators” or “startup spaces” to encourage local entrepreneurs to form new businesses. Incubators are most effective, however, when there are professional staff available to advise those starting new businesses about how to form, grow, market, or finance those ventures. Because of the high rate of small business failures, however, local governments are often reluctant to hire the new employees needed to make incubators effective.

A trend (also global) complicating sustainable local development is the desire to incorporate more meaningful, citizen involvement into local government decision-making. Because the U.S. system of land use regulation operates primarily at the local level, and with relatively few constraints from the state or federal level, citizens often expect to have a large role in local decisions – and that desire appears to be growing. Over time, most local governments have become fairly skilled at conducting effective public involvement in both site-specific and community-wide land use decisions, and citizens have become used to a system in which their input is solicited and respected, but their suggestions are not always accepted. However, the process requires significant time and effort; time to organize meetings, notify nearby residents and stakeholders in a variety of ways, provide background documents, conduct the meetings, and then review public input to determine which parts of that feedback do not conflict with the community’s long-term development goals. One side effect of conducting significant, effective public involvement is that many decisions of city- or county-wide importance (for example, identifying a site for a new targeted economic use that will produce significant traffic) become local. While acknowledging the importance of the effort, citizens near the proposed site object to that specific location – and the same would probably be true in most proposed locations where the new use could operate. So at the same time that local governments are under pressure to operate more efficiently, they are often under pressure to allow more time for wider notice and more public input events before making a decision, even though the results of that public involvement is likely to make the decision more difficult.

#### **4 Denver's efforts to align planning and zoning with sustainable development goals**

Denver, Colorado, is a city of almost 700,000 people within a metropolitan area of 2.2 million. Located where the U.S. Great Plains meets the Rocky Mountains, Denver is well-located to serve as a center of trade and is the largest metropolitan area between Chicago and California. Although Denver's airport was already one of the busiest airports in the nation in the 1980s, the city undertook a very ambitious project to build a newer and much larger Denver International Airport, which opened in 1995. Although the Denver metropolitan area is the 16th largest in the U.S., the airport is the 6th busiest in the nation and (unlike many other airports) has lots of land available to expand as air travel and trade continues to rise. Since the United States recovery from the recession of 2008, the Denver metropolitan area has been one of the fastest growing – both in terms of population growth and job growth. By 2018, housing vacancy rates and unemployment rates were at historically low levels (both below 5%). Because of favorable weather and a variety of outdoor recreation and entertainment activities, Denver has been able to attract many young and relatively high-skilled workers, which in turn make the city more attractive for more job creation and relocation from other cities.

Denver's experience tends to reinforce one of the key messages in Richard Florida's influential book *The Rise of the Creative Class*<sup>2</sup>; that investments to make a more attractive and interesting city tend to attract the "creative class" – which in turn attracts other types of economic growth. In order to promote economically and environmentally sustainable growth, Denver and its suburbs (either alone or collectively) have taken the following steps:

- A. Invest in Public Transit. Although the western United States is generally very "auto-oriented" – most residents use private automobiles for most or all of their trips – it has proven impossible to expand road infrastructure as fast as population growth requires. To provide an alternative, Denver and its neighbors created a Regional Transportation District (RTD) that provides bus and rail transportation services in a seven county area. Although it only operated busses for several decades, in 1992 RTD began to build a light rail system and the voters have approved an additional \$5 billion to expand that system quickly over time. In 2016 RTD also began operating heavy rail transportation services to Denver International Airport, and the heavy rail system is also expanding. Since 2010, the city has also expanded its investment in protected bicycle lanes, even though the city's bicycle commuting rates are still lower than the national average. While necessary for general population mobility (and to reduce the frequency and length of automobile trips and related greenhouse gas pollution), the expanding menu of transportation services offered by RTD helps Denver attract the growing number of young, high skilled workers who do not want to own a car or want to use their car as little as possible.
- B. Grow the Housing Stock Near Transit Lines and Stations. In 2010, Denver adopted a new citywide land use zoning ordinance that exerts more control over the types of

buildings constructed in different areas of the city but allows significant flexibility in how those buildings are used. As part of that change, the map that accompanies the new ordinance tends to promote development and redevelopment in areas that are close to public transportation routes and stations by allowing larger and taller buildings in those areas. The new ordinance also allows for many of those areas to include a mix of housing and business uses, which allows households more opportunities to live closer to their workplaces if they want.

- C. **Strengthen Neighborhoods.** Businesses form and expand where they think they can find good employees, and employees with higher skill levels want to live in strong, vibrant neighborhoods. While Denver has long had a program to plan for neighborhood improvements, that program did not cover all of the city's neighborhoods. So the city recently initiated a Neighborhood Planning Initiative that aims to produce an effective improvement plan for every residential area of the city over the next 15 years.
- D. **Promote Affordable Housing.** Although private companies have moved to use the new zoning ordinance to build more housing very quickly, they have not been able to keep up with the influx of new Denver residents. As a result, housing prices and rents have risen quickly, which has displaced lower-income households and made it difficult for many companies to hire the employees they need because there is no housing available nearby at their income levels. As a result, Denver has begun to offer development incentives (allowing taller buildings) in return for legal commitments by builders to keep prices and rents down in a percentage of the units they build. In addition, the city recently moved to repeal a law requiring all multifamily housing builders to build a percentage of affordable units and replaced that law with new fees on new development and a new tax that will raise \$150 million for affordable housing investment and subsidies over the next 10 years.
- E. **Encourage Tourism.** Like all other large (and most small) cities, Denver wants more tourism – because tourists take money earned elsewhere and spend in the cities where they choose to be tourists. To ensure that it can host all but the very biggest conventions, Denver replaced its old convention center with a bigger one in 1990, and then expanded that new center twice over the next 25 years. A third expansion is currently being planned. In addition, Denver's land use regulations make it easy to convert existing downtown buildings into hotels to serve the rapidly growing tourist market.
- F. **Invest in Art and Culture.** Area political and business leaders have supported the creation of a Scientific and Cultural Facilities District (SCFD), which imposes a small additional sales tax on an area that includes 53 cities and seven counties to fund arts and culture. The majority of the funds go to major institutions (such as the largest zoo, art museum, and science museum), but a second tier of funding goes to medium-sized institutions, and a third tier of funding goes to small, innovative, entrepreneurial artists and venues.
- G. **Focus on Small Business Formation and Retention.** Despite international perception that the United States is dominated by "big business," the vast majority of U.S. jobs

– and the vast majority of new jobs created each year – are in organizations that have less than 50 employees (or even less than 20 employees). While small businesses are formed at a rapid rate, they also fail at a rapid rate, so Denver and other cities interested in job growth need to provide continual support to assist small businesses to survive and grow. The new Denver zoning ordinance takes a flexible approach towards business, institutional, and commercial land uses – it groups them into broad categories so that fewer permits or approvals are needed when a business property changes from one use to another. In addition, the new ordinance includes many “mixed-use” districts that allow both residential and non-residential uses to occur near one another. Those who want a quieter and more predictable housing environment may choose not to live in those areas, but a growing share of the population finds such areas attractive places to live. While the media focuses on new “start-up” ventures, the city needs to provide equal or greater attention to help existing small businesses find new products, markets, and ideas so they can continue to growth. To do that, Denver funds a Business Assistance Center, provides a clearinghouse where small businesses can learn about grants, loans, and support programs, and helps small businesses recruit qualified employees through the website [www.Denverhelpwanted.com](http://www.Denverhelpwanted.com).

- H. Cooperate Regionally. In addition, Denver cooperates with 22 other surrounding cities and towns in the Greater Denver Chamber of Commerce to jointly market the economic benefits of the Denver metropolitan area throughout the U.S. After a business has been persuaded to locate or expand in the Denver area then individual members of the Chamber may compete among themselves to offer the best site or situation. Denver believes that its fairly flexible approach to land uses will allow it to compete well at this stage, even though some of its building quality controls are stricter than some of its neighbors.
- I. Clean Up Polluted Properties. In many cases, well-located commercial properties have been polluted and cannot be reused until the pollution has been removed or remediated. Denver and its neighbors operate a “brownfields cleanup fund” to assist new users in making these sites clean and safe to occupy. Again, a flexible zoning approach to business, commercial, and industrial uses tends to open up more opportunities for investors to find an innovative use for these properties.
- J. Offer Employment Services. In addition to working with business owners, Denver and its neighbors offer services to raise and tailor the skill levels of the workforce to match available job openings. They offer free job training services, job placement services, job training tax credits, and Denver operates five workforce centers. Flexible land use controls allows these types of facilities to be located in a wide range of locations in the city without the need for individual approvals. In many cases these services are offered in partnership with local businesses or non-profit enterprises, rather than by city employees.

## 5 Conclusion

The U.S. system includes very little federal regulation over land use – except for environmental regulations. Most cities and counties are given substantial authority to regulate the division, development, and redevelopment of land as they see fit – subject only to constitutional protections of property rights and fair procedures. Local governments are very active in using those land use powers, but have to do so in a world in which (1) global economic pressures, (2) domestic pressures for efficient government, and (3) growing desires for citizen participation in land use decisions constrain both the tools they use and the outcomes they can achieve. The Denver, Colorado, metropolitan area provides a good example of how local governments try to innovate and collaborate to encourage local development in ways that are both environmentally and economically sustainable over time.

### Notes:

<sup>1</sup> See, for example: Neumark, David, Brandon Wall and Junfu Zhang. 2011. "Do Small Businesses Create More Jobs? New Evidence for the United States from the National Establishment Time Series." *The Review of Economics and Statistics* 93 (1): 16–29.

<sup>2</sup> Florida, Richard. 2011. *The Rise of the Creative Class*. New York: Basic Books.

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## A Model of Centralizing Local Government Finances

ISTVÁN TÓZSA

**Abstract** This paper explains how the Hungarian Government tried to overcome and manage the economic problems and deficits of local governments (LGs) which accumulated between 1990 and 2010. The model has been used as a case study for teaching about the fiscal reform of local governance; i.e., measures of decentralization and centralization. The aim of the model was to reform the management of local finances to help solve some real financial problems of LGs while preserving the principles of local democracy and satisfying the requirements the Hungarian Act on Local Governments. The model can be applied in other countries where the operation of local public services is beset by financial difficulties and the central government possesses sufficient resources to intervene. The paper presents a model of the consolidation of local governance involving the parallel and harmonized reform of the institutional arrangements of local finances, the economy, public services, elections and administration. The paper also contains observations about the near future of Hungarian local governments and gives some recommendations.

**Keywords:** • centralization • local governments • reforms • Hungary

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## 1 The financial position of local governments by 2011

The system of local governance, with its freely elected local representatives, was introduced in post-communist Hungary in 1990. By 2011, the total debt of Hungarian local governments amounted to 4.3 billion USD, an amount which could no longer be adequately handled. The accumulation of the debts of LGs was due to a lack of financial expertise and inexperience in dealing with economic activities. Most of the loans given to local governments, which were disbursed in order to finance the development of settlements, were instead spent on financing the ongoing operation of local public services. Local governments were no longer creditworthy for banks. Also, the system did not motivate elected local representatives to support the development of the local economy. Therefore, the reform and transformation of the local governance system could no longer be delayed.

## 2 The legal and financial transformation of local governance

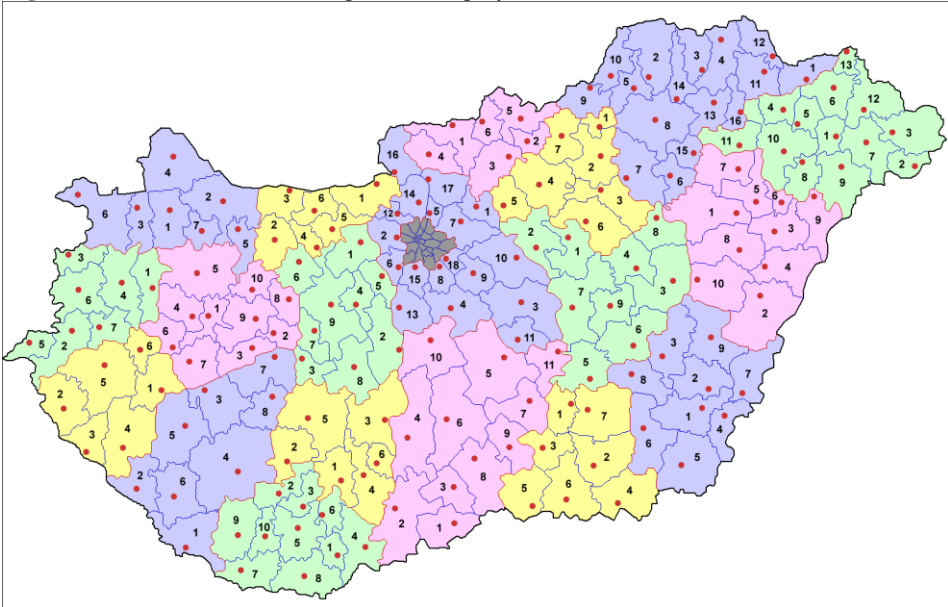
The transformation of local governance according to new principles began in 2010. First, the legal status of the local governments was modified in the Constitution, according to which loan applications of local governments could be approved only for local or regional development investment projects with a clearly defined financial basis. Local governments were prohibited from taking up loans for the purpose of financing the ongoing operations of their institutions. Also, the law on national property was changed and a kind of nationalization was introduced: a wide range of properties formerly owned and operated by local governments became state-owned properties.

The new *Law 189/2011 on Local Governments*<sup>1</sup> restructured the administrative tasks of local governments: some 40% of these tasks were transferred to the central government. These local tasks included the maintenance of official inventories, registries, public education, personal document management and, with the exception of social care, all kinds of duties that authorities performed. The central government was able to manage these tasks through the reintroduction of the so-called borough system of territorial administration. By force of the above-mentioned Law, 175 boroughs were established around the country in 2013, preserving the preexisting system of 19 counties and 7 regions.

To understand the change that was bought about by the reintroduction of the borough system, let us revisit the history of Hungarian public administration. Boroughs existed from the early days of governance; each royal county was divided into four or eight boroughs depending on the size of the county. A borough (in some cases named a “riding”) spanned the distance that citizens could cover on foot from their places of habitation to the administrative centre of the borough and back within one day. In the years 1972–1975 the borough system was replaced by a system in which the administrative centers were concentrated in large and medium-sized towns. In 1990, when local governments were established to replace the previous system of local

councils, each of the local governments was permitted to maintain an administrative office, providing they could afford it. At that time, from the 3188 Hungarian local governments 1514 had to share administrative units with neighbouring settlements, since they could not afford to perform administrative services on their own.

**Figure 1:** Counties and boroughs of Hungary



\* Note: New Law 189/2011 on Local Governments  
Boroughs (175) reintroduced from 2013  
Source: Wikipedia (2019).<sup>2</sup>

Due to the bankruptcy of the majority of local governments, it became necessary to undertake economic consolidation. This took place in four phases between 2012 and 2014 according to the following schedule:

- In 2012 the government spent 700 million USD on consolidating those LGs in which problems were the most urgent.
- In 2013 the government disbursed 300 million USD to cover the full debt of settlements with a population of less than 5000.
- In 2014 the government spent 3300 million USD on supporting the capital Budapest and its districts<sup>3</sup> and several major towns in Hungary by financing their debts to a level of 40–100%, the level of debt financing depending on the particular LG.

The new concept behind the legislation was that the eligibility for the economic support of local governments had changed. Previously, support was given on a so-called normative basis, i.e., it was proportional to the size of the population. However, according

to the new principle, LGs received support according to so-called duty-based, service-based, or task-based calculations. In other words, the amount of support depended on the local income capacity rate, on the amount of locally collected tax, and on the number and volume of services operated or managed by the local government.

### **3 A new concept for reshaping local services**

As mentioned above, the idea of the reform was to put a stop to mere institution-financing (i.e. normative support) by replacing it with service, duty or task-based support. The new aim is thus to develop towns as a whole, together with all their functions, but the provision of – for example – good urban transportation or health care should not be narrowed down to support for the operation of a transport company, or a hospital; i.e., of individual institutions.

Hospitals and schools were especially sensitive and problematic institutions because LGs lacked sufficient expertise to run them, and there were insufficient resources to finance them. As a rule, the smaller the town, the more difficult it was to afford the maintenance of educational and health services. Accordingly, hospitals and special health care units were taken over by the central government, as were schools. In the case of towns with a population of over 3000, a mixed system of school management was introduced, whereby both the central and local governments contributed to their maintenance. This implied a complicated bureaucracy which has faced difficulties with operating educational institutions and has occasionally turned teachers and pupils against the political leadership. Moreover, analogous processes unfortunately took place in the field of health care, where the operation of hospitals faced difficulties, including a lack of doctors and nurses.

The operation of the social care sector has remained in the hands of local governments. Previously, local governments distributed social benefits according to norms which were defined under 52 so-called “pretences” (titles). The complexity of the system led to administrative difficulties and slow working processes. According to the new regulation, citizens may now apply for social benefits from local social care administration using only one of eight different pretences.

Other services, such as waste management, a chimney sweeping service, water supply, and distance heating were provided by many contributors, some of them owned by the LGs, others by private enterprises. It was found difficult to engage these actors in fruitful discussion and to agree with the representatives of these stakeholders. Therefore, the reshaping of these services and markets and the amendment of the respective regulations were deferred to a later date.

#### **4 New principles for financing local governments**

As mentioned earlier, the former normative financing of local governments was replaced by task-based financial support from the central government. Instead of the size of the population remaining the basis for financing local public service tasks, the new financial system stimulates LGs to provide the services required by the respective regulations according to economic data supplied by the local governments themselves, who take into consideration the amount of local tax and duty revenues. Thus, the new financing system is based on the financial capacity of the governments, while their professional expertise in providing the related services is also taken into consideration. The financing system encourages LGs to develop their professional expertise and decision-making capacity in order to improve public services.

There are, however, some service fields that are closely monitored by the central government and financed according to specific principles. This approach affects the provision of school meals, the provision of kindergarten services, the enlargement of local kindergartens, and the management of public transportation. Some 2.3 billion USD in annual support is awarded for the development and operation of these services.

As mentioned earlier, local governments can no longer apply for loans to finance ongoing public service operations, but there are opportunities for loans for development and investment. In parallel, the repayment conditions for loans have been tightened up. In the case of emergencies, the respective law permits the disbursement of operational loans, but only within a one-year repayment deadline.

The government agency responsible for local governments is a state secretariat located in the Ministry of the Interior (Home Office). This agency encourages local governments to apply for development loans, especially those devoted to developing public sport service infrastructure such as swimming pools and football fields. Likewise, preferential credit is offered for improving public transportation. European Union subsidies are available for improving environmental quality, especially the development of waste water treatment and waste management; such support schemes encourage LGs to apply for complementary loans and grants.

#### **5 Reforming the administration of local governments**

Reform of local governance included the rationalization of administration, too. Only settlements with a population exceeding 2000 are entitled to run their own local government offices. In 2015, for example, from the approximately 3200 Hungarian local governments, some 1400 operated their offices on their own, while 1800 local communities had to share offices with neighbouring settlements. Before 2010 the number of LGs sharing offices with neighbouring settlements was only some 500, which means that rationalization raised the number of joint local government offices

by a factor of 3.6. On average, eight settlements share common offices and 17 civil servants work for a single office. The staff of such joint offices totals 25,000 clerks.

## **6 The economics of the self-reliance of local governments**

The 198/2011 Law<sup>4</sup> focused on the most important features of the institutional arrangement of LGs. However, for reshaping the economic environment of LGs, new reforms were needed. The main focus of interest of the government shifted to the responsibility of local bodies in attracting working capital, investment, and jobs to their territory. The implementation of these tasks required better urban marketing, an enhanced local identity, image building and urban branding.

Another law of 2011 legally underpinned the institution of public employment. This enabled LGs and other organizations such as NGOs and churches to apply for government funds to employ workers to carry out local public tasks in a non-profit arrangement. This has led to a considerable decrease in local unemployment. The mainly unskilled labour force hired in this way has been used not only for cleaning public spaces, but also as the staff of local establishments, among them new investments. Also, so-called social cooperatives were introduced to create new jobs in agriculture, predominantly in the area of growing fruit and vegetables, and in manufacturing, predominantly in the creation of alimentary products. Local governments were encouraged to open local marketplaces: i.e., premises for marketing and selling the products of local social cooperatives and mobilizing private agricultural producers, thereby serving the needs of traditional, licensed small-scale producers of agricultural goods and food. These products help to sustain traditional agricultural activities and contribute to preserving the identity of local consumers and producers, and even of the whole population.

## **7 Reforming local elections and institutional arrangements**

According to new regulation, the date and frequency of local elections is defined differently to the date and frequency of general elections. Previously, these two types of elections coincided, as both were held on the same day every fourth year in the springtime. Under the new regime, elections for local governments are held every fifth year in the fall. Additionally, members of the national parliament are not allowed to run for mayoral posts at the local level because this practice previously resulted in some conflicts of interest.

Under the new regime, elected representatives of local government bodies are required to take part in a life-long learning process. Civil officers and clerks must attend post-graduate training courses offered by the National University of Public Service. Every third year the clerks employed in public administration are obliged to collect a defined sum of credits from these post-graduate courses, some of which are based on e-learning.

Law 198/2011<sup>5</sup> establishes a platform whereby associations representing local governments can cooperate with the representatives of the central government by mutually sharing and exchanging their views. Also, a Local Government Research Institute has been established as part of the national University of Public Services.

A Government Decree of 2015 provides that those ministries which have jurisprudence or competence in terms of influencing local governments are obliged to establish the division of labour between their respective ministerial departments and the affected local governments.

## **8 The future of local governance**

The government is prepared to centralize the administration of certain public services in the centers of the seven regions. Significant steps towards regional centralization have already taken place in the administration of public health care and education. Another example is chimney sweeping, which in the future will be administered at the regional level in order to meet the challenges of fire protection, security, environmental protection, and energy management.

LGs in Hungary must have compatible information systems. A nationwide application service that supports an ASP (application service provider) system must be introduced to local government offices in order to decrease their risks and financial burdens. This will facilitate the introduction of uniform practices of book keeping and the regular provision of statistical data from every local government office.

As for the financing of local governments in the future, it is important that an inventory of debts and loans that are disbursed to them is constructed. Regulating loan conditions, together with compiling an inventory of local tax levies, will increase the transparency of the financial arrangements of local governments.

Public transportation is also a crucial function. Further steps are needed to harmonize railway and road transportation timetables around the country.

The incentives for the development of local economies require an inclusive type of local government decision-making that incorporates the active part of the local population.

It is additionally necessary to spread know-how about urban and regional marketing among LGs. Awareness must be raised of the fact that urban marketing involves the accomplishment of certain tasks that are additional to those of tourism marketing.

The establishment of inventories of local tax levies, loans and debts will enable stronger legal control over the financing and economies of local governments in the future.

**Notes:**

<sup>1</sup> Available at (in Hungarian): <https://net.jogtar.hu/jogszabaly?docid=A1100189.TV> (15 March, 2019).

<sup>2</sup> Available at: [https://commons.wikimedia.org/wiki/File:Townships\\_\(districts\)\\_of\\_Hungary.png](https://commons.wikimedia.org/wiki/File:Townships_(districts)_of_Hungary.png) (15 March, 2019).

<sup>3</sup> The 23 districts of Budapest are governed by autonomous local governments.

<sup>4</sup> Available at (in Hungarian): <https://net.jogtar.hu/jogszabaly?docid=99700081.TV&celpara=> (15 March, 2019).

<sup>5</sup> Available at (in Hungarian): <https://net.jogtar.hu/jogszabaly?docid=99700081.TV&celpara=> (15 March, 2019).

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## Local Democracy in Comparative Perspective

SIMONA KUKOVIČ, COLIN COPUS & DAVID SWEETING

**Abstract** Of all the issues that democracies face, maintaining legitimacy and democratic accountability rank among the most important; a fact that has been reflected in a burgeoning literature that addresses what is commonly referred to as the democratic deficit. This debate extends to the local level, where conceptually and practically there is a need for greater transparency and accountability in the decision-making process as a means of responding to declining voter turnout and the necessity of having appropriate structures that are able to tackle the evermore complex and interlinked problems that face local decision-makers. It is a debate which espouses different interpretations of political concepts, such as the political legitimacy to act locally, the visibility and profile of local leaders, the transparency of the local political decision-making process, the most effective mechanism for political accountability, the role of citizens in local democracy, and the role of political parties and partisanship in local government. These discussions shed light on the similarities and differences between countries regarding the role of local government and local democracy, as well as providing templates and case studies about how these responses may best be able to transfer across national boundaries. The chapter seeks to contribute to this discussion by providing a comparative analysis of three countries (England, Spain and Slovenia), which are of different territorial and functional types (Northern European, Southern European, and Central and Eastern European) according to the categorizations of local government systems in Europe. The authors analyse issues of local democracy, with particular emphasis on elected mayors and local council size, and review the debates around those issues in all three selected countries. Moreover, they describe the systems of local government, and arguments within countries concerning aspects of local government and democracy.

**Keywords:** • local democracy • mayor • local council • England • Spain • Slovenia

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## 1 Introduction

The point of departure for this chapter is the assumption that democracy is built at the grass-roots level, where claims for personal recognition can be made. This means that local politics must be based on community, and related values of openness, tolerance and inclusion. Furthermore, they must be based on democratic practices like elections, organized group activities, and other ways for citizens to influence the collective actions that tie people together and underpin local democratic infrastructure (Ostrowski and Teune 1993). To qualify as a democracy, a local political system has to allow its citizens' effective control of its political agenda and the decisions thereby rendered. Even if a local political system effectively and efficiently provides public services and facilities in perfect agreement with the needs of its citizens, such a system is not authentically democratic if its citizens are not included into decision-making processes (Denters *et al.* 2014). Local democracy is the idea of promoting a common good under circumstances where there is no strong preexisting agreement about what the common good is, what it entails, and how it can be promoted. It is thus subject to public justification (Barber 1984; Haus and Sweeting 2006).

Weir and Beetham (1999) claim that a system of collective decision-making can be called democratic to the extent that it is subject to control by all members of the relevant association considered as equal. The principle of citizen control is applicable to both direct (participatory) and indirect (representative) democracy. Furthermore, Weir and Beetham (1999) argue that the realization of the principle of control is dependent upon three intermediate principles. First, the *principle of authorization* involves what are largely constitutional provisions that provide public officials with the formal democratic legitimacy to exercise authority on behalf of a population (for example, laws that regulate the electoral procedures by which officials are elected and can be removed from the office). Second, the *principle of accountability* refers to the accountability of public officials to the public (in a representative democracy the main mechanism securing this principle is that of free, competitive elections, where all adult citizens can exercise control over the political fate of political officeholders). Third, the *principle of responsiveness* requires that the government systematically takes note of the full range of public opinion in the formulation and implementation of law and policy. This principle requires a well-functioning system of political representation in which elected representatives are open and accessible to public demands, and are also prepared to act upon them (Beetham and Stoker 1996).

The local level of government is critical to the development of democracy because it is the primary channel between the people and authority. In a unitary system, power is devolved by a central government to a local government, but these devolved powers can be revoked by the centre and cannot be used in conflict with central policy direction. In a federal system, power is shared among federal, state and local governments; in practice, the relationship is largely between the state or regional government on one side and local government on the other, because (constitutionally) local government is normally created

within the constitutional mandates of state or regional governments. In any political system, local government is created to “decongest” the functions of central governments and to supply services that are local in nature but which also provide a degree of local self-government and control. This is why local government requires political leaders and citizens that can tolerate legal conflict, accept group differences, and endorse political equality, as relationships in localities are diffuse and the environment is diverse. Complex interests and a wide spectrum of local services create the perfect space for problems to arise that demand flexibility, quick adaptation and responses from local leaders. Therefore, local government is a very significant and specific form of power organization which is accepted in almost every country in the world. Of course, it should be emphasized that local government in different parts of the world have their own specific characteristics and differ considerably. These differences are due to many factors, such as path dependency, tradition, historical circumstances, organizational structure, functioning, scope of responsibilities, type and number of service delivery, activities, normative and financial independence, level of economic development, the size of territory, population, and the like.

Furthermore, while vast differences exist globally in relation to local government (Hambleton and Gross 2007), even within Europe there is rich variety in local government systems organizations and, above all, in different forms of local democracy. To meet the needs of our chapter, we apply a typology of local government systems created by Page and Goldsmith (1987), later updated by John (2001), to draw a distinction between *Northern* and *Southern* European countries.<sup>1</sup> This typology is based on three indicators: first, the proportion (both numerical and type) of functions assigned to the sub-national authority; second, the legal discretion available to local policy-makers; and third, the access of local politicians to the central authority (John 2001, 26). The main idea behind this typology is that there is an inter-relationship between these indicators. It is clear that policies that are enacted, as well as the corresponding leadership roles – which are fulfilled by mayors – vary greatly depending on the pattern of this interaction. The typology presupposes that Northern European systems are marked by a strong decentralization of functions, a high degree of discretion, and the low access of local politicians to the central government, while in Southern European systems local politicians can have a strong influence on the central level of authority, but represent politically weak municipalities.

Moreover, Northern democracies, based on the independent power of the local level to decide about important issues, have developed a system of local government which has become known as a “small political system” (John 2001, 30). Local politicians have to achieve results, typically through the use of local resources and with an emphasis on providing local public services. Since the early 1950s, many municipalities have merged in an attempt to increase efficiency and provide better public services. In Northern European systems there are only a few levels of authority. On the other hand, local politicians of southern democracies are forced to act within a given framework of territorial representation and political localism, and to use different networks to access

national and regional centers of political power in order to represent local affairs (Page 1991; John 2001). The size of local communities is still small, because, within a given context, community identity has been more important than the effectiveness of public services. Southern European countries therefore have many levels of authority – partly as a means of increasing the potential of territorial representation (Heinelt and Hlepas 2006, 23–24; Kukovič 2015, 35–36).

The typology of Northern and Southern Europe has clear advantages as it is simple and avoids the old institutionalism that has long prevailed in comparative analyses of governments, including the analysis of local authorities. Of course, on the other hand, there are also some disadvantages; for example, only a limited number of countries were included in the original analysis. Furthermore, at the time when Page and Goldsmith's (1987) typologies were originally developed, the new democracies of Central and Eastern Europe did not yet exist as autonomous countries with their own local government structure and development. However, a few years later Swianiewicz (2014) provided an Eastern European typology of twenty countries based on: (i) territorial organization and tiers of elected local government, (ii) scope of functions provided (functional decentralization), (iii) financial autonomy, and (iv) horizontal power relations within local government institutions (election systems and relationships between mayors and councils): this typology adds to our developing understanding of the nature of the relationship between the centre and localities.

The main purpose of this chapter is to present three examples of different structures and patterns of local democracy in three European countries which have different territorial and functional types of local government. We analyse and compare English local government as representative of the Northern type, Spanish local government as representative of the Southern type, and Slovenian local government as representative of new Central and Eastern European type. We analyse issues related to local democracy, with particular emphasis on elected mayors and local council size.

In looking at these issues in more detail, this chapter proceeds as follows. First, we examine the different historical roots of local government in England, Spain and Slovenia. The next section describes the contextual settings and puts an emphasis on local leadership – the mayor; the third section sets out to analyse the role of the local council in selected countries, while the final section discusses and draws out the lessons from the three selected cases.

## **2 The context of local government in England, Spain and Slovenia**

The current territorial organization of the 28 EU member states is very diverse, both at the state- and the sub-national level. At the state level, the 28 member states can be classified into three main categories: three countries are federal States (Austria, Belgium and Germany), two are regionalized States with a quasi-federal structure (Italy and Spain), and the remaining countries are unitary States, although some have asymmetrical

forms of organization (Portugal, the UK). Despite their different territorial organization, all three countries have formed local governments which are organized into one, two or three tiers, depending on the country.

**English** local government is organizationally diverse and, for traditional and political reasons, either exists in a two-tier structure in parts of England – i.e. county and district councils; a unitary system – where all services and functions are provided by a single council, a structure which exists in both semi-rural and urban areas; or in the form of parishes – the smaller units of local government, very distinct from the counties, districts and unitary councils.

Some elements of this structure can be traced back to arrangements in place before the Norman Conquest which developed from Anglo-Saxon hundreds, burghs and shires. Modern democratic local government in England began to develop with the 1835 Municipal Corporations Act with further democratization taking place in the 1880s. In the late 1960s a plan was to drawn up for a pattern of 60 single-tier councils throughout the country, but the incoming Conservative government replaced that proposal with the implementation of a two-tier structure of county and district arrangements. The current shape of local government in England was introduced by the Local Government Act 1972, which reduced the number of county councils in England from 58 to 47 and the number of district councils from 1,249 to 333. Subsequent legislation has further reduced the number of county councils to 34 and the number of district councils to 238. The Act also created six metropolitan counties with 36 metropolitan districts among them to cover the major conurbations of the country; these metropolitan counties, along with the Greater London Council although not the metropolitan districts, were abolished by the Local Government Act in 1985. Since then, these large metropolitan areas of the country have been represented by single tier (Copus 2010, 8).

The Greater London Council was replaced by the 25-member London Assembly and the directly elected mayor of London by the Greater London Act 1999. These new bodies exist alongside 32 London boroughs, created in 1965 at the same time as the Greater London Council. In addition to the two-tier structure of local government which covers most of England (after the abolition of the metropolitan counties and Greater London Council the metropolitan and London Boroughs became de facto unitary councils) there are 55 unitary authorities, created under the Local Government Act 1992. Unitary councils can be created by a statutory instrument: that is, by the Secretary of State and without the employment of the full process of parliamentary legislation – they are, however, powerful councils, providing a full range of local services (Copus 2010, 8).

Following the death of Franco in 1975, **Spanish** society was confronted with the question of how to establish a constitution which could transform a unitary and centralized state into a politically decentralized and modern democratic one. The 1978 Constitution has since guided the formation of the Spanish state and the asymmetrical devolution with which it is associated.

In the first phase of development (1979 to 1981), the Statutes of Autonomy were granted to the historical communities the Basque Country and Catalonia (1979); Galicia (1981); and Andalusia (1981). During this phase the autonomous agreements of 1981 were signed, establishing the map of autonomous communities and the route to autonomy for each of them, and the organizational structure, uniform to all Autonomous Communities (Legislative Assembly, Government Council and President) with an end date for the process set as 1 February, 1983. In the second phase (1981 to 1992), the map of autonomous communities was gradually completed with 17 separate autonomous communities, being constituted through the different processes and methods established by the Constitution. In the third phase (1992 to 1996), the Autonomous Agreements of 1992 were signed, which equally granted powers and responsibilities to certain Autonomous Communities through the reform of their Statutes of Autonomy. In this phase the reform of the Spanish Senate took place in order to increase its territorial representation. Finally, in 1994, the General Commission for the Autonomous Communities was created which integrated senators and representatives from the national and autonomous community governments who may intervene in its sessions and request the calling of a meeting. In 1995, once Ceuta and Melilla became autonomous cities, the autonomous process was completed in terms of the map of autonomous communities (Nivero de Jaime 2009, 67).

The Spanish Constitution established a model of a state with three levels of government and administration: central, regional and local. The completed constitution is composed of 17 autonomous communities and two autonomous cities. The local model, which is divided into municipal and provincial subdivisions, is comprised of more than 8,100 municipalities and 50 provinces (Nivero de Jaime 2009, 67).

**Slovenia** – by far the youngest of the selected countries – has only one tier of local government. On the territory of what is now Slovenia, local government had already been introduced in the mid-1800s by the Austrian act on municipalities, signed by the then Kaiser in 1849. The first municipal representative bodies in Carniola were elected in 1850. Sixteen years later an act on municipalities was adopted, and from then on legislative regulation of local government was performed continually until 1955, when a socialist communal system was introduced, de facto abolishing local government. In the communal system, the municipality was a so-called socio-political community that primarily acted in the name of the state, whereas local government proper existed in part only in local communities at the sub-municipal level (Haček *et al.* 2017, 113).

After Slovenia gained independence in 1991, the introduction of local government was one of the most important and difficult tasks, as this represented radical change in the then-self-governing communal organization in the direction of the "classical local government" of the European type. The first steps were preparations for creating the technical groundwork to support the project of local government which had already been prepared in 1989, the adoption of the new Slovenian Constitution with a significant emphasis on local government at the end of 1991, and the adoption of the basic law on

local government in December 1993. Foundations for the implementation of the reform of local government were laid with the adoption of the Act of Referendum for the establishment of municipalities in 1994, when 147 municipalities were established. In Slovenia, local-self-government has been in operation since January 1995, when the old system was finally replaced and territorially modified municipalities, having new substance and new representative bodies, became operational.

At every local election since 1998 new municipalities have been established (the latest municipality was established in autumn 2014), bringing the current number of municipalities to 212.

This brief review shows that local government development has significantly different historical roots in the three selected countries. However, the lowest local government unit is the municipality, which ensures the delivery of community services to the population. Municipalities, which are very diverse both in terms of localization, size, organization and resources, manage basic local public services such as distribution networks (water, waste, public transport, public lighting, etc.), leisure and living environment services (urban planning, protection of the environment, etc.), and are also in charge of primary education and social services (Hermenier 2009). For the effective and efficient performance of public services, municipalities require leadership, which is confronted with the everyday challenges of a troubled environment. With this contextual setting in mind, we move on to explore the mayoral office in all three selected cases.

### **3 Who puts the mayor into office?: The role of, and elections for mayor**

There are several reasons why local political leaders and leadership should be subject to extensive research that uses a comparative perspective (Paige 1977; Nixon 1982; Wiatr 1988). One of the most important reasons for a comparative approach relates to the fact that the local government settings in which local leaders work differ considerably. Thus, by comparing local leaders and their activities, we can discover much about local leadership and reveal important information about the local government system and local democracy of a particular country (Farrell 1970).

Different structures of governance imply different roles for local actors and for local political elites, including local political leaders. Within the context of local governance, these are crucial for the development of local democracy. Mayors have to deal with economic and social conflicts that arise in the community. They are also accountable for successes (or failures) in resolving these problems and for the development of a civil culture of democracy (Linder and Heierli 1999, 2) that embraces values of inclusion, tolerance and openness. In democracies, mayors are meant to be responsive to their electorate – they listen to their wishes, are open to participation, to propositions and advice from different actors and they try to seek or negotiate compromises. In most settings, the behaviour of mayors is of important symbolic as well as instrumental

significance and is, at least to some extent, affected by their beliefs about local democracy.

In recent decades ensuring the satisfaction of citizens through service delivery has become an important task for local leaders (Haus and Sweeting 2006, 155; Sweeting and Copus 2012), entailing the increasing presence of the marketization of political relationships and the stimulation of competition within the public sector. Additionally, as local leaders act as mediators seeking compromise between different interest groups and other local actors, they are seen as conflict dealers in situations where none of the different actors or groups is strong enough to enforce a solution against the will of the others (Haus and Sweeting 2006).

We start our analysis of local leaders with evidence from **English** local government. The Local Government Act from 2000 radically transformed the structure of political decision-making in local government, and Part II of the Act required all councils with populations above 85,000 to introduce one of three new-style executive political decision-making arrangements. The three executive options available under the Act were: (1) a directly elected executive mayor and cabinet, (2) a mayor and council manager (an option removed by the Local Government and Public Involvement in Health Act 2007), and (3) an indirectly elected executive leader and cabinet (Copus 2018, 500).

The indirectly elected leader and cabinet option was preferred by the overwhelming majority of councils, which is not surprising as this option represents the least change to existing practices and structures and maintains the right of councillors to choose local leaders. Here, the council, but in reality the ruling party group, selects one of its members to be leader. A cabinet of up to nine councillors (plus the leader of the council) is formed, again, normally from the majority party group, unless the council has no overall control. The leader and cabinet form the council's political executive. The system is not dissimilar to that which existed prior to the 2000 Act when the ruling group would ensure that the council appointed its leader as council leader and went on to elect a number of committee chairs and vice-chairs from among its number. The main difference is that, since the 2000 Act, individual councillors can have decision-making delegated directly to them – much like government ministers.

The directly elected mayor is the executive political head of the council, but, unlike a council leader, all the voters in a council area elect him or her. There are two ways in which an elected mayor can be introduced through the council's executive arrangements: (1) a referendum is held after the collection of a petition signed by 5% of local people which delivers a "yes" vote, following which an election for a mayor must be held within six months, or (2) a council meeting can vote to introduce an elected mayor – without a referendum. Much debate has centred on the issue of a directly elected mayor, a political office very different from the current ceremonial mayor that chairs council meetings. Despite many councillors complaining that the mayoral office should see that the concentration of power is in the hands of a single individual, the reality is different from



that which is often claimed (Copus 2006). The directly elected mayor has broadly similar powers to those of the indirectly elected leader. The elected mayor is elected by all the voters in a council area, not just by councillors, and thus has a direct electoral mandate that is far more powerful and legitimate than the indirect one granted to a council leader by fellow councillors. The directly elected mayor is elected through a supplementary vote system, where voters place a cross in a first- and second-preference column against their preferred two candidates (Copus and Dadd 2014). After the first count, if no single candidate receives fifty percent of the votes cast, all but the top two candidates are eliminated and the second-preference votes are redistributed to the remaining candidates.

The introduction of directly elected mayors has brought into existence a highly visible local political head of the council with responsibility for providing political leadership, proposing a policy framework for the council, preparing the council's budget and taking executive decisions. Directly elected mayors on the surface appear to be a radical change for local government, but the mayors and councils on which they serve were given no new powers that would clearly distinguish them and their councils from any non-mayoral councils of the same type. It is thus not so much the power of the mayor that is different, but rather how they get the job, and here it is the voters that decide instead of a handful of councillors from the ruling group on the council (Copus 2018, 500).

Between 2000 and October 2016, 53 mayoral referendums were held across England, of which only 16 delivered a "yes" vote. This figure includes the ten referendums in English cities in May 2012 required by the government under the Localism Act 2011. Two councils – Stoke and Hartlepool – subsequently eliminated the office of directly elected mayor and returned to a system with an indirectly elected council leader. However, two councils – Liverpool and Leicester – resolved to introduce an elected mayor under powers granted by the 2007 Local Government and Public Involvement in Health Act, which allowed councils, following a two-thirds majority decision by councillors, to adopt an elected mayor without a local referendum. What was clear after the initial round of mayoral elections in 2002 was that voters in at least half the mayoral contests had taken the opportunity the new arrangements had given them to reject candidates from political parties, and often from the party that had long controlled the council. Political parties have since regained territory in mayoral elections, and in 2016 only two mayors were independents. Taken as a whole, out of 352 English councils, only 16, excluding London, are headed by a directly elected mayor (Copus 2011; Fenwick and Elcock 2014; Copus 2018).

On the other hand, **Spanish** mayors (*alcaldes*) have had an effective leadership role for decades and are strong and visible local leaders; some authors (Magre and Bertrana 2005; 2007) even talk about the presidentialism of Spanish mayors (Wollmann 2012). Comparative studies rank them as among the strongest mayors in Europe, and one study has categorized them as "directly elected mayors" (Heinelt and Hlepas 2006). Spanish mayors are, however, indirectly elected by councillors, and only those candidates that are at the head of their party lists can become mayors.<sup>2</sup> While coalitions between smaller

parties that support a mayor are possible, the mayor is usually the head of the largest party group of elected councillors, and that party will in most cases have either a majority of votes, or will have been the most-voted-for party (Navarro and Sweeting 2014).<sup>3</sup> Local elections appear as contests between candidates for mayor, rather than between lists of candidates for local council. The campaigns are very personalized and focused on the heads of the list – i.e. only on those candidates who can become mayor. Although the formal election of the mayor is in the hands of the councillors (of the political parties in reality), the fact that only the head of the list can occupy the mayor's office gives voters a controlling influence over the election of the mayor. The legitimacy required to occupy the mayoral position is also reinforced by the fact that electoral participation in Spain is high in comparative terms.

Legal provisions identify the mayor as the head of the municipal corporation, and in a context when the powers and influence of appointed council officers are relatively weak, is in overall political and administrative control of council bureaucracy. The mayor has the formal power of appointing deputy mayors and members of the governing board and sets the full council agenda. The clearly defined hierarchy in the municipality facilitates the effectiveness of the decision-making process and the implementation of policy priorities. The mayor has the general power of direction and the support of the government team to make decisions, more so than many other European mayors. In the Spanish case, the concentration of power is seen (rather dangerously) as an advantage, enabling the mayor to implement the party's electoral program (Navarro and Sweeting 2014). Beyond the internal activity of the municipality, the mayor represents the community to the outside world. Local media usually generously cover the activities of the town hall, often focusing on mayoral activities (Navarro and Sweeting 2014).

Since the transformation to democracy, Spanish mayors have been the central figures in local government and politics in their areas, despite the fact that they lead municipalities with limited powers. As city leaders they have full legitimacy and their indirectly elected status does not prevent them from wielding considerable influence in local governance. In addition to the formal prerogatives granted by law, a very personalized leadership culture and loyalty to the party on behalf of councillors adds to their potency (Sweeting 2009). These informal rules are essential for maintaining the strong position of the mayor. The visibility of the mayor's office is a clear feature of the Spanish system, and the mayor is undoubtedly the political leader of the municipality.

In **Slovenia** voters elect mayors directly for a four-year term of office. The right to vote is conferred upon voters who have permanent residence in the municipality (The Local Self-Government Act 2007, Article 42). The right to vote and to be elected as mayor is conferred upon every citizen who has the right to vote in elections to the municipal council. The Slovenian system of local government features a fairly simple candidacy procedure, since mayoral candidates can be proposed by political parties or groups of voters. If the latter is the case, the candidacy must be supported by a number of signatures equal to at least two percent of all voters who have cast their votes in the first round of

the most recent mayoral election, yet this number must not be less than fifteen, and need not be more than 2,500. Mayoral elections use a double-round absolute majority vote system; in other words, the candidate who receives the absolute majority of the votes that are cast is elected as the mayor. If none of the candidates receive the majority of the votes that are cast, a second round of elections is held between the two candidates who received the greatest number of votes in the preceding round. If two or more candidates receive the same highest number of votes, or if two or more candidates receive the same second highest number of votes, the choice of candidates that will enter the second round, which has to be held no later than 21 days after the first round, is determined by lot.

As mentioned, mayoral candidates can be determined by political parties and groups of voters. Non-partisan candidates can submit their candidacies if they are supported by groups of voters; the size of any such group is ultimately determined by the size of the municipality in which such candidate is proposed. In this way, non-partisan candidates have a relatively simple way of asserting their passive suffrage, a claim which is also confirmed by empirical data about local elections since the 1990s. These reveal that non-partisan candidates have been increasingly successful, as the proportion of elected candidates relative to the number of candidacies submitted is significant. Haček (2010, 43) concludes that the absolute number of mayors who, at least formally, have not run for the office as members of political parties has been constantly increasing; ever since the 1998 local elections, the greatest number of municipalities that have had mayors who have not been proposed by any political party has increased (43 at the 1998 local elections, 59 in 2002, 66 in 2006, 70 in 2010 and 115 in 2014).

In accordance with the organization of the work of the municipality and the distribution of competences within the municipality's tasks across municipal bodies, the function of the mayor is at the same time both executive and coordinative. In addition, the mayor has various functions in relation to the municipal council as well as varying influence on its operation. On the one hand, the mayor's responsibility is to take care of the implementation of decisions adopted by the municipal council; on the other, he or she has an important function in proposing an array of decisions to the municipal council, and finally overseeing the lawfulness of the latter's operation (Kaučič and Grad 2008, 369–370).

The mayor is the “master” of the municipality. Namely, by signing different contracts, inviting public tenders, through rational and economical implementation of the budget, and consistent adherence to the principle of good diligence, and all of this on a daily basis, the mayor takes care of the municipality's assets and increases its value and quality. Their task is also to summon citizens' assemblies and (when people's lives and/or property are compromised) to adopt urgent measures (Prašnikar 2000, 46). However, the mayor's most important function is to be the head of the municipal administration. Mayors are sovereign and practically “untouchable” throughout their entire term of office. Together with the municipal administration that they head, mayors can pursue a very independent policy in the municipality, regardless of that pursued by the municipal

council. However, this can be problematic in cases when the elected mayor does not come from one of the political parties that control a majority in the municipal council. The Slovenian mayor is thus the central figure in the Slovenian local government system and, being an individual, one-person body, is the most recognized political figure among the citizenry (Kukovič 2018).

In this section we have put emphasis on the characteristics of mayors in three different countries. We analysed who is responsible for putting mayors into office and what the role of these mayors is once they occupy office. In this regard, each country uses different mechanisms. In England, executive mayors can be elected directly by voters or indirectly among local councillors; in Spain, the plenary assembly elects the mayor, with a legal clause providing for the candidate of the best-supported party to be automatically elected mayor when the full council cannot agree, which in fact means that voters have considerable influence on the election of the mayor. In Slovenia, direct elections of mayors are in use, whereby citizens themselves decide who will occupy the most recognizable position at the local level. In the next section we discuss the size of local councils and how the role of these representative bodies is perceived in each national setting.

#### **4 The local council: legislative body and meeting point of political interests**

Of all the issues that democracies face, legitimacy and democratic accountability rank among the most important (Norris 2011), a fact reflected in a burgeoning literature that addresses what is commonly referred to as the democratic deficit. The debate also extends to the local level, where it has been argued that there is a need for greater transparency and accountability in the decision-making process as a means of responding to declining voter turnout and the necessity of having appropriate structures for tackling the evermore complex and interlinked problems that local decision-makers face (Wollmann 2008; Kukovič *et al.* 2015, 694). Local government gains legitimacy through having representatives elected to it (Sharpe 1970, 168). Elections are crucial as they enable voters to choose between different representatives, hold decision-makers to account, and signal their views about election commitments. The representative form of local democracy enables a variety of interests – geographical, party, class, gender – to be represented in some sort of assembly which is the sovereign decision-making organ of government (Sweeting and Copus 2012, 22). According to Copus and Steyvers (2017), crucial to understanding how elected representatives operate and drawing lessons from their action is recognizing the implications of how these leaders are located within differing constitutional settlements.

**In England**, the local council is a dual-purpose body: it is a politically representative institution which operates as the foundation of any healthy, well-functioning democracy; it is also a vehicle through which the public services vital to modern industrial welfare states are organized, provided, commissioned or overseen. These two broad central purposes of local government mask, however, the complexity of local government as an

organization, but they also capture the two interrelated council worlds that the councillor must navigate. Being a councillor means running, or taking part in the running of, a large, complex, multifaceted organization which has its own separate administrative and managerial structure. The interaction councillors have with the managerial and administrative staff of the council is shaped by the type of councillor they are – leading member, majority group member, opposition member, for example; by the nature of the subject matter being explored – strategic policy issues, casework, ward-based concerns; and by the setting in which the interaction occurs – formal council meeting, informal discussion, or a forum which is external to the council. The council is a politically representative and elected body, and councillors and council meetings are the vehicle for the legitimate expression of the views, opinions and priorities of local citizens (Copus and Wall 2017).

Local government has a legitimate governing role within and across the community. Consequently, it is the setting for political interaction and decision making that reflects the ideological and policy preferences of councillors. Currently, some 92% of principal authority councillors in England are elected as candidates from either the Conservative and Labour Parties or the Liberal Democrats. Party politics looms large in the relationship councillors have with the council. What becomes clear very quickly however, is that parish and town councils are far from party politicized, yet even at the first tier of local government – the parish and town – national political party councillors are found working alongside councillors independent of party. National political parties do not, however, have the penetration into parish government that they do at the principal authority level (Copus and Wall 2017, 16–17).

In most of England, there are two tiers (county and district) with responsibility for services split between the two. County councils cover the entire county area and provide around eighty per cent of services. Within the county, there are several district councils which cover a smaller area and provide more local services. However, London, other metropolitan areas, and some parts of shire England operate under a single-tier council structure.

In total, there are five possible types of local authority in England. These are:

1. County councils – which cover the whole county and provide eighty percent of services in these areas, including children's services and adult social care.
2. District councils – which cover a smaller area within a county, providing more local services (such as housing, local planning, waste and leisure but not children's services or adult social care); these can be called district, borough or city councils.
3. Unitary authorities – referring to just one level of local government responsible for all local services, can also be called a council (e.g. Medway Council), a city council (e.g. Nottingham City Council) or borough council (e.g. Reading Borough Council).
4. London boroughs – where each of the 32 boroughs is a unitary authority.

5. Metropolitan districts – effectively unitary authorities, the name being a relic of past organizational arrangements. These can be called metropolitan boroughs or city councils (LGIU 2018).

There are 352 principal (unitary, upper and second tier) councils in England (27 county councils, 201 district councils, 32 London Boroughs, 36 Metropolitan Boroughs, 55 Unitary authorities; in addition there are two Sui Generis authorities – the City of London Corporation and the Isles of Scilly). Across England there are some 18,000 councillors (LGIU 2018) all elected using the first-past-the-post simple majority system of voting.

In **Spain**, the collective decision-making body (local council) for municipalities is the “*pleno*”. This is the plenary, the deliberative body of the Town Hall (the *ayuntamiento*) formed by elected councillors, and presided over by the “*alcalde*” (the mayor).

The members of the local council are directly elected by universal suffrage and according to proportional representation, using the D’Hondt method and a closed list of proportional representation, with a threshold of five percent of valid voters being applied in each local council. Parties not reaching the threshold are not taken into consideration for seat distribution. Councillors of municipalities with populations of less than 250 inhabitants are elected under an open list, with electors voting for individual candidates instead of parties. The council is elected every four years, and cannot be dissolved. There is no limit to the number of times councillors may be re-elected. If they die, resign, or are dismissed, the next person on the electoral list of their political party replaces them; therefore, there are no by-elections. The law requires that the council meet in full session at least every three months; either the mayor or one-quarter of all councillors can call extraordinary sessions.

The population of the municipality determines the number of council members; the latter are allocated to municipal councils based on the following scale:

- Less than 100 inhabitants: 3 councillors;
- 100–250: 5 councillors;
- 251–1,000: 7 councillors;
- 1,001–2,000: 9 councillors;
- 2,001–5,000: 11 councillors;
- 5,001–10,000: 13 councillors;
- 10,001–20,000: 17 councillors;
- 20,001–50,000: 21 councillors;
- 50,001–100,000: 25 councillors;
- Over 100,001: + 1 per 100,000 inhabitants or fraction thereof; + 1 if the total is an even number (Navarro and Sweeting 2013, 3)

The number of councillors and the population do not increase proportionately – the latter rise much more than the former. As the analysis from 2006 in Table 1 shows, about half

of the voting population of Spain live in authorities with more than 50,000 inhabitants each.

**Table 1:** Municipalities and councillors in Spain

Population size of municipality	Number of voters	Per cent of voters	Per cent municipalities	Number of councillors	Per cent of councillors
Up to 250 inhabitants	299,491	0.9	28.9	8,680	13.3
251–5000	5,075,436	15.1	57.0	37,348	57.2
5001–20,000	6,718,903	20.0	10.5	12,306	18.9
20,000–50,000	4,119,461	12.3	2.1	3,696	5.7
Above 50,000	17,372,666	51.7	1.5	3,235	5.0
Total	33,585,957	100.0	100.0	65,265	100.2

Source: see Delgado (2006, 166).

At the last local elections in 2015, Spanish voters elected 67,515 councillors in the country's 8,122 municipalities. The smallest have only a handful of residents, whereas the largest, Madrid, has well over three million. Municipalities are financed by grants from upper levels of government, local taxes, and fees and charges, though the weight of public spending is concentrated at regional and national levels (Sweeting 2012). Municipalities with more than 50,000 inhabitants provide a range of services including public transport, waste collection and disposal, street cleaning, leisure facilities, police and fire services – and many larger authorities provide many more services.

The central body of **Slovenian** local government is the municipal council, which is the highest authority for decision-making regarding all matters within the scope of the rights and obligations of the municipality. It is elected in direct, general and free elections, by secret ballot cast by the inhabitants of the municipality, for a term of office lasting four years. Municipal councils are elected at general elections by the citizens of each municipality every four years; both one-round relative majority and proportional electoral systems are in use, the first in smaller municipalities (of up to 3,000 inhabitants) and the latter in all other municipalities, where both the D'Hondt and Hare methods of seat allocation are used. There are 3,369 local councillors in 212 municipal councils across Slovenia.

A municipal council can have from 7 to 45 members, depending on the total number of residents in the municipality. Thus, a municipal council has the following number of members:

- 7–11 municipal councillors for up to 3,000 inhabitants;
- 12–15 municipal councillors for up to 5,000 inhabitants;
- 16–19 municipal councillors for up to 10,000 inhabitants;
- 20–23 municipal councillors for up to 15,000 inhabitants;

- 24–27 municipal councillors for up to 20,000 inhabitants;
- 28–31 municipal councillors for up to 30,000 inhabitants;
- 32–35 municipal councillors for more than 30,000 inhabitants;
- 36–45 municipal councillors for more than 100,000 inhabitants.

The competences of the municipal council include the following: adoption of the statute of the municipality, of municipal decrees and other municipal legal acts; adoption of spatial and other developmental plans of the municipality; the adoption of the municipal budget and its balance sheet; appointment and dismissal of the members of the supervisory committee and members of commissions and committees of the municipal council; appointment and dismissal of representatives of the municipality in the advisory committee of the head of the administrative unit; and, decision-making concerning the acquisition and alienation of real estate and control over the performance of duties by the mayor, deputy-mayor(s) and the municipal administration – with regard to the implementation of decisions adopted by the municipal council (The Local Self-Government Act 2007, Article 29).

The most important act of general application adopted by the municipal council is the statute that sets out the basic principles for the organization and functioning of the municipality, the creation and authorities of municipal bodies, the organization of the municipal administration and public services, the method of citizen participation in decision-making in the municipality and other issues of common concern in the municipality. The statute is adopted by the municipal council by a two-thirds majority of all members. In addition to the statute, the municipality governs matters within its competence, especially through decrees and ordinances, rules and instructions.

With this section of the chapter we have displayed the complexity and variety in the collective body known as the local council. The analysis shows that local councillors are, according to the concept of representative democracy, directly elected by citizens in all three national settings of local government and have very similar competencies and functions. However, the organization differs among the selected countries and it may be subject to consideration which national settlement ensures better representation of interests and greater legitimacy.

## 5 Conclusion

The chapter has illustrated the richness of local government systems, as exemplified through an exploration of our three case study countries: England, Spain and Slovenia. We selected these three countries to provide different examples of the issues we wished to explore and because they have emerged and developed from different local government traditions, with Northern and Southern typologies and historical traditions illuminated by England and Spain, and the Slovenian case used to provide a Central Eastern European example. Indeed, Slovenia as a nation did not exist when the Page and



Goldsmith typology (1987) was constructed, although it was part of Swianiewicz's (2014) typology.

We have described how local political systems are extremely country- and context-specific, as would be expected. But such a conclusion does not damage the comparison we have conducted, nor the need to understand and systematize our knowledge about local government systems. This is because there are three primary components of local political systems which cut across systems and national / historical settings. First, decision-making power is given to local elected officials to allow them to fulfil fundamental functions and represent the preferences of citizens in the decision-making process. Second, there is the existence of political, governing, economic, financial, social and technological incentives that encourage local political leaders to represent their constituents. Third, there are mechanisms that hold the local government and its elected and non-elected officials accountable for the appropriate use of their decision-making roles and powers (Boex and Simatupang 2015). The institutional context for the effectiveness of local political systems and local political leadership within which forces of discretion, incentives and accountability interact is provided by (1) the internal political organization of the local government, which means either the separation of powers between councillors and a local political executive and leadership, or a blurred system where the executive is drawn from and responsible to councillors; (2) the manner in which the local executive (mayor) and councillors are elected (including the representation of women and disadvantaged groups); (3) the nature of the political party system and the degree of national or local / regional party control of local government; (4) the vertical separation of powers between types of councils, tiers or other levels of sub-national government; (5) the effective control that the political leadership has over its management team and over local administration at large; and (6) non-electoral aspects of local political participation and accountability.

The idea behind this chapter was to provide insight into local government in different countries and to stimulate thinking about systems, local politics and leadership choices that result in systemic differences (and to explain why these differences emerge and what they mean), and about different conceptualizations of the role, purpose and value of local government within the overall system of government of any one nation. The power and beauty of local government involves its fundamentally different historical trajectories, different traditions and political cultures connected with specific local political development, combined with how broader national developments influence and shape local government and are in turn shaped by local government. Despite the different attitudes towards local democracy that exist among academics, national governments, and national and local politicians, we conclude that while local government is “only local,” and as a consequence may be seen by regional, state or central governments as a potential plaything to be reshaped, reorganized and remolded to suit the needs of other tiers of government, it is still an essential part of any modern democratic state. Moreover, we detect that local government is experiencing rehabilitation, rejuvenation and revival due to the fact that citizens in most countries are less than content with their level of

inclusion and ability to influence national and supra-national governmental organizations. They are therefore seeking refuge in local democracy as the most basic pillar of democratic representation as well as development in modern society.

#### Notes:

<sup>1</sup> The differences between the countries in Northern and Southern Europe have their roots in historical development. In the Northern European countries of the eighteenth and nineteenth centuries, the central (state) power did not develop a centralized bureaucracy but, along with local elites, implemented national policies (Page 1991). Education was decentralized – under the jurisdiction of local institutions – and in many countries the Protestant church remained part of the state. Strict and impartially enforced national legislation, as well as a professional and effective civil service, secured the unity of modern statehood. Later, when countries responded to demands for equality, legal entitlement and social security, a social protection system was established whereby local authorities became responsible for social public services. In Southern Europe, a model of the Napoleonic state spread across all modern national countries which led to the development of a unified administration throughout these territories, and education systems being managed directly from the country's capital. The central authority looked at local elites with mistrust and therefore built its own territorial organization with a directly established administrative body. In the twentieth century, social states began to appear in Southern Europe, giving central authorities new competencies (Heinelt and Hlepas 2006, 23–24).

<sup>2</sup> Voting for mayors involves an indirect election except in the “*concejo abierto*” system, where local residents vote for their mayor directly. However, this system operates in very small municipalities only (Ministerio de Administraciones Publicas 2018).

<sup>3</sup> A legal clause provides for the candidate of the most-voted-for party to be automatically elected to the post of mayor in the event that no other candidate gathers an absolute majority of councillor votes.

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## **Sector and Spatial Analysis**



## Local Development in Italian Districts “After the Deluge”

ITALO TREVISAN

**Abstract** Italian industrial structure is characterised by the importance of SMEs and their weighty contribution in terms of employment, sales and exports. The international competitiveness of Italian SMEs has been enhanced by another peculiarity of Italian industrial structure: the sectoral concentration of production in small, specific areas. The industrial districts in which industry has been concentrated were instrumental in the development of many areas of Italy and are distinct from the powerhouses of Italian industrialisation and development, meaning that they are not located within the large conurbations of the North-West. The additional distinctiveness of these districts has been their strong interaction with the local community, thus the related districts can be seen as an evolved form of the Marshallian industrial district.<sup>1</sup> This evolution has been characterised by the importance that the communities and the people of these areas have had in the establishment and successful development of these districts.

**Keywords:** • industrial districts • globalisation • economic crisis • adaptation • Italy

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## 1 Italian industrial districts according to statistics

The Italian economy is characterised by the still large role of the secondary sector. The proportion of employment in industry (28.3%) is the highest among large developed countries,<sup>1</sup> and the weight of industry in GDP (24%) is surpassed only by Germany and Japan (30.1% and 29.7%, respectively).<sup>2</sup> Another characteristic of the Italian economy is the great weight of small- and medium-sized firms (SMEs), which in 2015 made up 99.4% of all companies. In any country small firms make up a large proportion of the total (inevitably, the smaller the size, the larger the number), but the importance of SMEs in the Italian economy can be seen from other perspectives, too. SMEs employ 78% of the total workforce; they contribute 48.8% of total turnover, and (even more surprisingly) 50.8% of added value. If an assessment is made with exclusive reference to the manufacturing industry (where larger firms are more common), the weight of SMEs is still extremely high. They make up 90% of all manufacturing firms, employ 76.5% of the workforce employed in manufacturing, create 60% of turnover and 66% of added value.

Possibly the most characteristic element of the Italian industrial structure is the clustering of SMEs that belong to the same industry in a number of relatively small industrial districts. Indeed, in no other country is the weight of industrial districts as important for the economy as in Italy.

In 2001, a year when the consolidated success of the districts started to fade, just before the "deluge" (but when the effects of some "heavy rain" were already being felt), there were 181 manufacturing SME industrial districts, as identified by ISTAT (the Italian statistical service). In these areas were operating about one-quarter (24.3%) of all local units of Italian firms, and they were responsible for one-quarter (25.4%) of national employment and the production of 27% of national added value. More specifically, these districts were home to 38.8% of all local units engaged in manufacturing in Italy, employed 39.3% of all the people working in this sector, and produced 38% of value added in manufacturing. Their weight in Italian exports was even greater: 44% of exports of manufactured goods came from these areas, with peaks of 52% in exports of machinery and 60% in tiles and ornamental stones.

In 2011, after the deluge of Chinese exports and the additional hit of the recession that started at the end of 2008, there were 141 industrial districts still in operation. They accounted for 24.4% of all local units and 24.5% of total employment. Their importance for the manufacturing sector was still greater, as they accounted for 34.3% of manufacturing local units, and 37.9% of employment in manufacturing. Their weight in national exports had slightly increased to 48% of the total, again with a much higher concentration in the sectors represented by the so-called "4As" of the "Made in Italy".<sup>3</sup>

Industrial districts are one of the major success stories of the Italian economy. Their success is also shown by the growing international interest in this phenomenon that many consider to be a useful reference model for the promotion of local development.



Industrial districts, however, are not a novelty nor are they a peculiarity of Italy. The concept of the industrial district goes back to Alfred Marshall (Marshall 1920, paragraph 3). In *Principles of Economics*, he discusses the occurrence of the "concentration of specialised industries in particular localities" and explains that such a concentration "within the narrow boundaries of a manufacturing town or a thickly peopled industrial district" happens thanks to the external localization economies resulting from the concentration of many small firms of a similar nature in specific places. This concentration facilitates the finding and changing of jobs and the intra-district flexibility of labour. In these small areas owners and workers live together; therefore the solidity of the district is strengthened because "[s]ocial forces here co-operate with economic: there are often strong friendships between employers and employed". The circulation of workers and the relative ease of starting a new business spreads know-how about the industry of specialization. As Marshall puts it, "[t]he mysteries of the trade become no mysteries; but are as it were in the air, and children learn many of them unconsciously" (Marshall 1920, paragraph 3).

The district, then, is something more than a simple agglomeration of firms in a certain place; it is a stable community where production activity is enriched by a shared specialist technical expertise, and where a strong local cultural identity can develop.

Some peculiarities distinguish the Italian industrial district<sup>4</sup> from the archetype explained by Marshall. In the Italianate industrial districts too, there is a strong "industrial atmosphere" of a Marshallian type. The industrial district is a local community that specializes in manufacturing a certain type of product. More significantly, the emergence of some models of productions of excellence ends up reinforcing the spirit of identity of its inhabitants and their attachment to the territory in which they live. Local people are particularly proud of the success of their firms and of their territory, to which everyone is aware of having contributed. In a way, community and firms tend to blend. The district, then, is a socio-territorial entity characterized by active coexistence, in a geographically circumscribed and historically determined area, of a community of people and a population of industrial enterprises focused around one specific industry (Becattini 1990). Most firms are SMEs, but some larger, leading companies also often emerge. From these, new enterprises are frequently born through a process of "gemination," meaning that in periods of cyclical upswing of the characteristic industry workers from established firms resign in order to establish their own small firms. This process often implies some form of support being given to the leaving workers by the owner of the firm where they were employed. This hints at the presence of an attitude of cooperation between firms that is one of the peculiarities of the Italianate industrial district.<sup>5</sup> In fact, this peculiarity is a combination of competition and collaboration between companies. Internal competition is very strong and fosters selection of the best companies. However, the companies in the districts often collaborate with each other in relation to shared projects (marketing abroad, the management of environmental problems, etc.).

The interaction and integration of disparate elements make evident the systemic nature of the Italianate industrial district and its complexity. Moreover, this complexity is a specific indication of the evolution of the Italianate manufacturing districts from the traditional Marshallian industrial district to a more sophisticated entity called *Area Sistema* (AS). To sum up, according to the literature six essential elements should be present in the evolution of an Italianate industrial district into an *Area Sistema*.<sup>6</sup> These are:

- A small and clearly demarcated *territory*, with some definite characteristic that set it apart from neighbouring areas;
- The presence of a *community*, sharing a homogeneous system of values in terms of work ethic, family values, a sense of belonging;
- A large number of *small and medium-sized enterprises* specialized in one or few phases of the production process;
- The presence of *strong* and, as a rule, informal *links among firms*, creating an atypical system of relations, where co-operation and competition coexist;
- *Widespread competency and know-how*, mostly of a technical type, related to the dominant industry of the area, thus the specific level of competence of the local population is quite high;
- The involvement, not necessarily from the beginning, of *institutional players*; this involvement is the expression of the full participation of all the components of the local community in the working of the AS (Trevisan 2006).

The Italianate districts and their evolved forms, the *Area Sistema*, are a resourceful answer to the problems of local economic development in Italy. Localized in small areas – often eccentric to the main industrial centers of the country – they have played a determining role in the economic and social development of whole regions that had been left behind in the first stage of industrialization of the country. Although they started, similarly to any industrial district, as areas with an industrial monoculture (wherein the productive structure was based on a single industry), they have developed to incorporate a degree of complexity and interaction among firms that belong to different, albeit related, industries that make them a specific sub-type of industrial district.

From a structural point of view, it is possible to detect a certain trend towards increased complexity that marks the development of the Italianate industrial district. As with any industrial district, the former started as an area of industrial monoculture. In time, most districts acquired a higher degree of complexity and expanded their industrial focus to different, albeit related, industries.

Industrial districts can be classified according to the degree of their organizational and structural complexity (Garofoli 1983). This classification can be seen as an evolutionary sequence whereby some districts evolve, and by evolving become stronger and more successful, while those that do not evolve tend to falter and sometimes disappear.<sup>7</sup>

The first step, at the lowest level of complexity, is the *area monoculturale semplice* (simple monoculture area), which is the typical *industrial district*. This has a large concentration of mostly small and medium-sized firms that belong to one industry and which are quite often specialized in one phase of the production process. These firms are locked in tough competition and – as in Marshall's formulation – do not have any meaningful structured relationships. The few (relatively) large firms tend to have a guiding role that strongly limits the independence of the smaller ones. The essence of the *area monoculturale semplice* is the subdivision of labour and specialization in the production process.

The second step is the *sistema produttivo locale* (local production system). Here, too, SMEs mostly operate in the same industry and are specialized in one or a few phases of the production process. Strong horizontal competition characterizes this type of district but, as a consequence of specialization and strong community feelings, intra-industry relations are much more developed and are not limited to short-term transactions. Relationships and groupings of firms are changeable but tend to revolve around a core of firms that have developed long-term cooperation. Development in the area is fostered by the build-up of a critical mass of factors, leading to the increased formation of firms. Some leading companies appear in the ranks of local firms. These, however, tend to remain of middling dimensions; if greater production capacity becomes necessary, it is achieved through groups of SMEs, generally family run.

The last step is the Area Sistema (AS, integrated industrial system) which involves a higher degree of structural complexity. The main characteristics of a population of specialized SMEs operating in different phases of the dominant industry are still present. However, some of the most successful firms may reach a larger size (but seldom above 500 employees) and take a leading role in shaping the strategy of the area. Strategic collaboration among firms is widespread and is both intra-industry (without dampening strong local competition) and inter-industry, linking upstream and downstream activities. Therefore, the division of tasks and specialization of firms and activities also evolves beyond the original – still dominant – industry, involving related and supporting industries, such as a mechanical engineering industry producing specialized machinery for the main production activities, or specialized marketing services. The outcome of this evolution is an accumulation of differentiated capabilities due to the strong functional links between the dominant (manufacturing) industry and the set of activities that supply it with operational or strategic inputs. This combination creates greater resilience and stronger competitive advantages for the Area Sistema as a whole, and for its firms.

This is, for now, the last complete step in the evolution of Italianate industrial districts.<sup>8</sup> This is the distinguishing trait of the most successful of the Italian industrial districts, while many others remain at a simpler stage and can be considered Area Sistema *in fieri*.<sup>9</sup> This evolution has allowed many Italian industrial districts to meet the significant and disruptive changes occurring in the competitive structure of the world economy, and to

maintain or regain their competitiveness when facing the many challenges of the first decades of the twenty-first century.

## 2 The internationalization of Italian industrial districts

The industrial districts represent, in a way, a different form of economic development, and the Italianate districts are certainly an example of this diversity. The entrepreneurs in the districts' firms, often based on deeply rooted local traditions of craftsmanship, have taken an autonomous path of development, focusing on manufacturing niches in light industries, often in "traditional" sectors. In a country going through a rapid process of industrialization, with government policies focused on stimulating the development of southern regions through massive investment into heavy industry, district entrepreneurs became accustomed to working without protection or aid. Districts were the unplanned response of a peripheral economic system with good potential for development, but substantially ignored by an industrial policy biased firstly towards the "protected" sectors of state industry and, secondarily, the support (or rescue) of the large companies in the hands of the historical families of Italian capitalism.

Operating in a domestic market dominated by a few large companies, district firms had as an important and sometimes main reference the world market. Since the mid-1960s, foreign markets became the training ground where district firms and districts themselves strengthened their competitive capacity. In many industries, the districts soon become world leaders in their specialty sectors.

The start of the evolution of the districts and their internationalization can be dated to around the mid-1960s, after a short recession that brought to an end the Italian "economic miracle". During those years, the transformation of the many widespread artisanal businesses into proper industrial activities took place. This also created the conditions for the take-off of the districts and their internationalization. The slowing growth rate in the mid-1960s became insufficient for ensuring the growth of the districts' firms on the relatively small Italian home market. Therefore, entrepreneurs from the sectors where Italy had recognized skills – those sectors that later became identified by the sobriquet<sup>10</sup> *Made in Italy* – started looking at international markets. This period saw the large-scale launch of exports of footwear, furniture, jewellery, textiles and clothing, ceramic tiles, taps, etc. from Italian districts. The districts became a veritable manufacturing powerhouse, compensating for the contracting trend of the main industrial areas dominated by the large companies (state-owned and private). The district environment was advantageous to local firms in several ways, not least the avoidance of social tension. In the metropolitan areas where the large companies were, the 1970s were difficult years of exasperating trade union conflict, increasing unemployment and terrorism. In the districts, the locally embedded SMEs were lean and fast, and could adapt quickly to changes, unemployment was almost nonexistent, and social tensions were minimal. Thus, the second "economic miracle" of Italy, the miracle of "Made in Italy," largely built by

the districts, was born almost spontaneously and outside any pre-established industrial policy design.

Indeed, the industrial policy of the time focused on how state intervention was able to develop the southern part of the country through the expansion of heavy industry and subsidies to large companies. While this effort continued with dismal results, the large pool of entrepreneurs in the districts (and outside them) had moved ahead, leveraging their competence and the flexibility of their SMEs to move into the international market, specializing in those sectors of light industry (such as food, fashion, home-furniture, and light mechanical engineering that were their traditional strengths. This evolution also relied on the gradual sophistication and ripening of district types of organization of production, and allowed for the development of dynamic new regional areas of the country: the North East and the Adriatic coast.

The 1980s and especially the 1990s were the period of maximum development of the model of the district and of Made in Italy. Italy was ranked sixth in the world in terms of value of exports, and in 1996 Italy's trade balance was the third largest in the world after Germany and Japan. This success became the "Italian puzzle". Italy was one of the biggest economies in the world (for a short time ranked fifth in terms of GDP) but this appeared incompatible with the persistence of the "backward" characteristics of the production system. Italy was not only characterized by a large presence of SMEs, but also had fewer large enterprises than the other industrialized countries by far (very few Italian companies – 10 – ranked among the 500 biggest in the world). Among these countries, it had the highest proportion of self-employed people and the lowest proportion of female employment. It had a marginal presence in high-tech sectors (accounting for less than 10% of exports) and a very low level of R&D expenditure. The "country system," moreover, had a penalizing effect because of significant bureaucracy and structural and political inefficiency, leading to the insufficient development of crucial infrastructure, and the highest energy costs in Europe. However, this country of middle-sized and small firms, often struggling to access finance, was the sixth largest exporter in the world (and more than half of these exports were due to SMEs). Italy was (and is) a prosperous advanced industrial country but its strength on foreign markets has often been linked to "traditional," labour-intensive industries where the competitive advantage would normally have gone to low-wage developing countries.

The answer to this puzzle lies in the phenomenon of integrated industrial districts, the Areas Sistema. The latter were the factor driving Italian competitiveness on world markets.<sup>11</sup> They constituted the strength of the country, creating employment and a trade surplus despite the decline of many of the larger companies. The networked structure of the Area Sistema, which valorises the connection of the small to the small, transformed what were individual weaknesses into collective strength, making the districts a powerhouse of internationalization and innovation.

### 3 Industrial districts and globalization

In the 1990s, after a phase of tumultuous and uninterrupted growth, the districts were faced with a number of new problems. globalization did not simply mean new openings in new international markets; it started to mean increased competition from low-cost countries, particularly in sectors with lower added value, and most strongly in textiles and clothing. Asian competition began to be felt. Additional factors adding to the uncertainty included enhanced attention to environmental issues which required serious investment (particularly in districts specialized in activities such as tanning and the production of ceramic tiles) and additional costs, and a growing shortage of skilled labour (most local youths being less interested in taking up a factory job than in the previous generation). Moreover, with Italy's adoption of the euro, the practice of the periodic devaluation<sup>12</sup> of the lira had to cease, putting an end to this method of rebalancing the competitiveness of Italian exporters. In this new context, characterized by the intensification of globalization processes, it seemed that factors that once represented the strong points of the districts (the small size of firms, a preference for exports rather than investment in foreign facilities – FDI – and strong links to territory) could become structural weaknesses for both the districts and the whole Italian manufacturing sector.

The significant competitive capacity of the districts developed in a period when the competitive context allowed for processes of adaptive learning (reacting to market stimuli, imitating successful strategies, focusing on incremental innovation) to become the basis of the attainment of competitive advantage. For decades, the model of development of most districts was essentially one of the "extensive" type, based on the progressive enlargement of the production base in quantitative terms (growth in demand = growth in companies and employees). The transformations that begun to be clearly felt around the turn of the century created a more complex competitive environment, which had the power to undermine the stability of the districts on many fronts.

The increased tempo and changing character of technological innovation was an important factor. Since the last years of the twentieth century, innovation has been mostly associated with the new technological paradigm of information and communication technologies, but many industrial districts have lacked access to this know-how. In addition, the changes in values and social attitudes and the processes of homogenization that have affected most societies in the developed world have touched the districts as well. This has placed their social fabric under stress, already strained by the generational change in the ownership of local firms, which is more often than not a threat to business continuity, and the solidity of the district as a whole.

However, the main destabilizing factor has been globalization. From this period onwards Italian districts, as well as the Italian and European manufacturing sector as a whole, were, so to say, at the "receiving end" of globalization. Until then, they had been protagonists and beneficiaries of this process, but from that point they started feeling increasing competitive pressure from firms located in developing countries. This

competition became more troubling because these countries added to their well-established cost advantages by improving their technical and operational skills, leading to improvements in the quality of their products and their marketing. This hit the Italian industrial districts particularly hard, because they were (and are) specialized mainly in "traditional" and mature industries, which are the natural fields of expansion of companies from developing countries.

The need to adapt to this changing competitive environment and to adopt a new competitive approach better suited to the increasing and more threatening dynamism required significant changes in the firms of the districts, and of the districts as a competitive unit. This new situation, in fact, required a new, proactive approach that would anticipate the changes in the international competitive system. The competitiveness of Italian industrial districts could be maintained only by exploiting new, different levers of innovation and internationalization, and by readjusting the shape of the value chains of firms.

In order to tackle the growing competition from low-cost producers, many district companies decided to fully embrace globalization and adopt a delocalization strategy. At the beginning (in the years around the turn of the century) the delocalization strategy adopted by some of the more important firms in the districts did not involve disruptive dimensions: some firms started to source their supplies from abroad, or relocated some labour-intensive phases of the production process in low-cost countries. However, almost immediately it transpired that following this path might pose an existential risk to the district. These shifts started to cause a loss of business for the many smaller firms specialized in the simpler or more labour-intensive phases of the production process; a loss that risked the demise of the firms and the loss of local jobs. This also created the risk of a loss of cohesion in the district because of the weakening of links within the community. The shifting of activities outside the district moreover progressively increased the risk of dispersion and the loss of accumulated knowledge, which was one of the strong points of the districts. Cutting the local supply chains in many districts caused a structural crisis both for the main industries and for ancillary industries that had grown up to support them and which had originally shaped the development of the Area Sistema.

There was no doubt that the previous model of development of the district was not up to the new situation. It was based on locally embedded know-how, on successful access to foreign markets, and on exporting in a competitive environment where most competitors who could make products of a similar or slightly lower quality had higher costs, and those who produced at a (slightly) lower cost were creating products of much lower quality. In this situation, the districts grew "extensively" through the progressive enlargement of the production base in quantitative terms (i.e. growth of demand led to growth in number of companies and employees). In the new situation, characterized by requirements for new, ICT-based and less localised, know-how, and by a competitive environment in which

competitors had significantly lower costs and made improvements in the quality of their products,<sup>13</sup> a different model of development was necessary.

The districts already had a highly internationalized industrial structure in the sense that they were selling a large proportion of their finished products abroad. However, in the new situation they were not global enough in the sense that they did not have a production chain distributed across various countries, suitably selected to take advantage of the activities located there.

District firms woke to the realization that internationalization and exporting were no longer synonymous, even for them. Some district firms started exploring two different paths to internationalization.

- The first strategy option was delocalization: companies could foster the transnational distribution of the various activities of the value chain to be able to exploit to their advantage the national differentials specific to different countries. Firms can gain a decisive advantage by selecting the location of various activities according to the different characteristics of cost and productivity. Given the differences between countries, particularly considering emerging countries with low labour costs, the maximum value of each business may be attained by distributing the activities of the supply chain in such a way as to exploit the relative advantages.
- The second strategy option was active participation in international networks for the purpose of sharing tasks related to the production and use of knowledge. Firms may acquire a decisive advantage because they can use knowledge and specialization accessible on a global scale, rather than producing this on their own – or in the “closed” environment of the district – at high cost and risk. Being part of such a network allows firms to specialize in a specific form of know-how which can be exploited on a global scale, and to count for everything else on other firms in the network with whom a relationship of trust and fairly open communication has been developed. This, after all, would not be anything new for a district firm: it would “simply” involve the transposition at a global level of the patterns of relationship developed in the district.

As a consequence of the changes in the competitive environment, a new avenue to internationalization developed among the (bigger) firms in the districts – an approach that gave much more space to transnational exchanges of knowledge, instead of limiting external relations to the marketing of finished or intermediate products.

Delocalization and global networking heralded a new model of growth for the districts. Accordingly, the districts were to grow “*intensively*” by grounding their growth on progressive increases in the intrinsic quality of existing products, on product innovation, and on productivity gains. The application of this model did not involve an increase in the number of companies or employees, but rather implied some tendencies towards their general reduction.



#### 4      **The reorganization of industrial districts**

Moving from an export focus to the global organization of the production chain, however, is not easy. It is necessary to develop a strategy of networking and/or to implement correctly the process of the Delocalization of the "poorer" phases of the production process, and to try to get access to places where new technological development is taking place (without forgetting that, in terms of product differentiation and targeted process innovation, Italian districts have quite often been in the vanguard).

The path of Delocalization in search of lower costs, however, not only offers the possibility to decrease labour costs and to help compete with low-cost producers from emerging countries. It also leads to the emergence of leading companies whose connections, not only in terms of outlet markets but also of production capacity and innovative ideas, have shifted from a logic of territorial proximity to a widened logic of the global scale, which occurs essentially based on strategies of convenience and apparently without any territory-based restraint.

The relocation of phases of the production process to other countries inevitably brought with it a fall in employment in the districts. The parallel development of network technologies gradually reinforced and amplified the de-structuring of the districts. The expansion of the geographical boundaries within which the leading district firms connected, driven by economic advantages and technological support, loosened the links of territorial contiguity that characterized the Italian district and on which it based its strength. On the one hand, the interconnections and relationships that innervated<sup>14</sup> the district were modified, raising the spectre of their total disruption. On the other hand, the success of those leading firms whose action – aimed at preserving their competitive capacity, if not their self-preservation in a more threatening competitive environment – had the potential for disrupting the districts from which they had drawn their strength was not a foregone conclusion.

The interpersonal relationships that regulate the relationships within the individual districts, the different forms of aggregation outside the places of production, the informal communications that are based on collective experience, and a common culture of production are phenomena difficult to replicate across borders, let alone through the internet. A different situation, however, applies to business relationships outside the district. The requirement is to find a "common language" that allows local companies to network beyond the boundaries of the district and permits closer interaction with outside actors.

In this period, the district well-known as an area specialized in the production of Made in Italy quality goods started to undergo important changes. Alongside the usual interlocutors, new partners, already long used to dialogue with foreign markets in terms of export orientation, started joining these firms. The firms from the district faced a potentially deadly threat, and most of the attempts at surviving that threat and remaining

successfully present on global markets also increased the threat to the districts, which were still the basis of their strength.

This dilemma came to the fore in the period after the turn of the century. Increasingly tough price competition from low-cost producers (either from developing countries or from the companies of the developed world that had already delocalized to those countries) pushed many medium-sized district firms to delocalize.<sup>15</sup> In the first five years of the new century, the Italian economy started showing less dynamism in comparison to main European competitors.<sup>16</sup> Nevertheless, alongside the steep decline in big business, the industrial districts, considered as a whole, maintained in this period surprisingly strong capacity. Yet the picture has both light and shadow, and situations of growth were accompanied by obvious situations of difficulty and crisis.

Broadly speaking, the districts as a whole managed to maintain their importance as a manufacturing and exporting powerhouse. In the framework of increased exports (from 178 billion USD in 1992 to 236 billion USD in 2000 to 366 billion USD in 2005), the export propensity of the districts grew from 39% in 1992 to 48.3% in 2000 to 50.9% in 2005. The strong performance of the districts in foreign markets was still mainly due to exports, but was complemented by their more active presence through the establishment of commercial branches and franchising agreements. Most significant in these years was the internationalization of the production *filière*.<sup>17</sup> The setting up of international supply chains came about as a result both of agreements with small producers localised in lower-cost countries (such as the countries of Central and Eastern Europe), often as part of Outward Processing Traffic (OPT),<sup>18</sup> and of the direct establishment of production facilities, sometimes fully owned and sometimes joint ventures. In these years, the average proportion of exports in the turnover of firms increased, particularly for the district firms.

It appeared that, despite the slowing down of the Italian economy, the model of industrial development based on small- and medium-sized businesses embedded in the industrial districts and on manufacturing specialization and internationalization was still a vital and dynamic system, which played an important role in Europe and throughout the world thanks to its significant export capacity. However, the districts found it difficult to react rapidly to the profound transformations that were affecting the world economy. Thus, despite success apparently still characterizing their performance, the general situation of the districts had deteriorated. They found it increasingly difficult *to fend off international competitors and to maintain internal cohesion in the face of this competitive onslaught*.

## 5 The "Deluge"

The growing difficulty in international markets was clearly related to the emergence of Asian economies and, in particular, of China and (to a lesser extent) India. The scale of their economies is truly gigantic. The size of these economies makes their growth (and its effects) quite different from the case of the "four tigers" of East Asia in the 1980s and

1990s. Transformation in the world economy became a gigantic process of reallocation of wealth, with very significant processes of income redistribution between countries and between wages and profits in individual countries.

To assess the impact of this phenomenon it is worth taking China as an example,<sup>19</sup> although there were other countries that also competed on the international markets that the districts participated in, and the problems for the districts started before the explosion of Chinese exports. Between 1996 and 2005, there was an extraordinary deterioration in Italy's trade balance with China (from a deficit of € 930 million to more than € 9 billion). However, the problem concerned the traditional export markets more than the internal market. The German market has been for decades and still is the main reference market for Italian exports and, in particular, exports from industrial districts. The trade balance of Italy with Germany reached a positive peak (€ 4 billion) in 1996; by 2005 the balance was a deficit of more than € 12 billion. Italy had kept importing – in increasing measures – products from Germany (from chemicals to cars); the large retail chains and large German buying groups, on the other hand, were replacing Made in Italy products with cheap products from Asia.

The difficulty the districts had in maintaining their internal cohesion sprung, as already mentioned, from the attempt of the main companies in the districts to reshape their approach to international activity. The evolution of the districts tended to create growing asymmetry between its firms, with the strengthening of the leading firms and their networks that increasingly extended beyond the district. The leading companies consolidated their control of the supply chain by modifying their relationships with suppliers and developing networks of companies governed in a hierarchical way, and also through the formation of groups. While activities linked to design, technology and marketing became more important (and therefore more closely kept under control by the leading firms), basic manufacturing activities were increasingly subcontracted outside the district, especially abroad. Trying to improve their performance, the leading companies changed both inter-organizational relations and district boundaries. It was no longer possible to see the district as an area in which the production cycle was self-contained. The division of labour within the district changed because the leading firms, needing to adapt to new ways of transnationally producing value to remain competitive in a globalized market, opened up to external relations, jeopardizing the local interconnections that sustained the district. As a consequence, some of the "upstream" subcontractors also started looking (with mixed results) at markets other than those no longer comprised of local customers.

The relationships of internal complementarity, which gave strength to the district as a socio-economic unit and, consequently, to its firms, started crumbling. On the one hand, the leading downstream firms, by abandoning their local suppliers for suppliers outside the district, caused the demise of many of the former. On the other hand, upstream suppliers, in order to face the mortal threat of losing their local clients, looked outside too. Some of them did so by replicating the Delocalization strategy of their clients –

indeed, delocalising to keep them – while others followed different strategies. Some looked for new clients – outside the district and internationally – supplying them with the know-how developed in the district; some tried to integrate downstream and become competitors of their former clients. Not many of them were successful, but in one way or the other the "natural" complementarity of interests, on which the district's collective value chain rested, broke down when the interests and attitudes of the various firms diverged in the face of the new international challenges. Downstream firms (customers) started feeling the competition from external producers that was powered by technologies, skills, services that had accumulated in the district and that became available on the international market thanks to sales or cooperation agreements made by the district's upstream producers. Conversely, these upstream firms (suppliers) could no longer count on being the fixed points of reference for their local district customers. They felt the weight of competition from other potential suppliers who became accessible to their customers thanks to their new international locations. This created the potential for conflicts of interest that could have seriously undermined the foundations on which the "district atmosphere" of competitive collaboration and territorial unity rested.

Another development placed additional strain on these foundations. To complement the outgoing flow of FDI from the delocalising firms, an opposite flow of incoming investments appeared. These acquisitions of district firms by foreign ones (quite often large multinationals) resulted in the acquisition by foreign companies of technological skills and supply chain auxiliary firms that typically developed within the districts. In some circumstances, this helped other smaller district firms to become visible on international markets. More often, however, the bigger external firms tended to use the districts as specialized production centers, places for manufacturing skills, moving activities with strategic value for the company and the local system to the headquarters of the company. In such cases of "functional downgrading" local firms tended to lose control of their design, brands, and of their direct relationship with the market. Even when in the short term the performance and profitability of such acquired companies was positive, in the longer term they risked losing the ability to innovate and reach final markets. Consequently, the district as a whole became impoverished, and less able to internationally compete and maintain the level of local integration and job creation.

The financial crisis of 2008 heralded the so-called Great Recession which affected a large proportion of the world's economies (in the first quarter of 2009, 59 countries simultaneously saw a fall in their GDP), and Italy was particularly heavily and for a longer time (despite some quarters of recovery, Italy was still in recession in the fourth quarter of 2014) (Eurostat 2018).<sup>20</sup> The districts were obviously affected by the recession, which increased the pressure on them and their efforts to respond to the threats mentioned above. In fact, in these years the districts underperformed other areas of Italy where a more mixed composition of activities and the presence of larger firms resulted in a less steep fall in turnover and employment.

Looking at the census data for 2011 (i.e., after the first wave of the recession), it is possible to see its effects on the districts and on the Italian economy. The first noticeable fact is that the number of areas recognizable as districts<sup>21</sup> in 2011 was 141 compared to the 181 that were present in 2001. Moreover, 35 of these districts were "new" areas that ten years earlier did not have the characteristics of industrial districts. This has two implications. On the one hand, it means that 75 areas that were recognized as industrial districts in 2001 were no longer such areas in 2011: thus in ten years 41% of the districts had disappeared. This obviously does not mean that they had all become industrial deserts. However, it does mean that the surviving firms in those areas did not form the industry-specific critical mass that represents the nature of a district. In some cases, indeed, the district basically disappeared due to a precipitous fall in the number of active firms and people employed in the area. This was more often the case with districts specialized in the textile and clothing industry, as well as furniture and household goods, while the number of districts specialized in mechanical engineering and metal products increased significantly (Eurostat 2018).

This suggests another implication of the data about the changes in the number of districts from 2001 to 2011. The amount of people employed in the districts and the number of local units increased. However, this increase was due to a positive balance between the decrease of both employees and local units in the manufacturing sector (as narrowly defined) and the growth in the same districts of employees and local units in non-manufacturing activities (most noticeably in the services-to-industry category) (Magliocchi 2015a). The districts appeared to be in a phase of transformation that, albeit sometimes disruptive, allowed them (at least those that were successfully managing the transformation) to weather the dangerous storm of the Great Recession combined with the preexisting competitive challenges of globalization.

In addition, the numerical contraction of the districts over the decade and the simultaneous birth of new industrial districts created clear variation in the geographical distribution of districts in the various regions of Italy. The areas with the biggest decrease were North-West Italy (-30% in the number of districts and -24% in the number of employees in manufacturing) and North-East Italy (-27% and 19%, respectively).

The following few years were ones of renewed recession and difficulty for the districts, as well as for Italian industry as a whole. However, the year 2014, still recessionary, saw a recovery of Italian manufacturing and specifically of most industrial districts, led by an increase in exports. Turnover, orders, and employment showed positive trends, in particular in medium-high technology industries (mechanical engineering and electro-mechanics), but also in the more traditional Made in Italy industries (food and beverages, textiles and clothing, and furniture and home furnishings) (Mazzeo 2016). During this still weak recovery, the districts – after almost a decade when they underperformed the other industrial areas of Italy – returned to growing faster than the rest of the production system. It appeared that the "district factor," despite some curtailment of its strength, remained an important element in the competitiveness of Italian industry.

This return to growth of the districts, albeit hoped for, was rather unexpected. It was also the outcome of a structural transformation in the most successful districts, each reinterpreting its activity and functions and developing diverse organizational models. The crisis led to a revision of the market and the organizational strategies of the district firms, particularly in relation to the thick fabric of formal and informal networks. The consequence is ongoing change in the shape and substance of the districts, still rooted, however, in the solid practices that gave the districts their strength. New elements are influencing the paths of innovation (with the growing uptake of digitalization in production processes), the configuration of supply chains, and the strategies of internationalization, reshaping the relationship between the production systems of the territory and its social capital.

The reshaping of the district model and its fabric of networks is a consequence of the twin developments of globalization and digitalization. On the one hand, these factors have compelled the district firms to combine the traditional local dimensions of their networks with enlarged ones that include the foreign countries where they operate and sometimes try to recreate a “district atmosphere”. On the other hand, they have pushed the firms to blend their rather informal traditional ways of organising production with the transmission of capabilities and the more formalized organization of production and distribution processes, relying on automation and the remote control allowed (or rather, required) by digitalization. As the process of modernization of industry rests mainly on ever-closer integration between manufacturing and advanced services, in particular with those related to ICT, the (successful) districts appear to have taken a path whereby the impact of digitalization becomes transformative, leading perhaps to a new phase in their life cycle. Indeed, because of the twin developments mentioned above, knowledge networks are changing and the district model needs to change correspondingly, with its territorial structure possibly taking on new shape.

This appears particularly true in relation to the organization of supply chains and supply networks. In this period, the lengthening of supply networks became widespread with the strengthening and widening of relationships with firms located outside the district, and sometimes abroad. By 2015, more than one-third of the main suppliers of the district firms were from outside the district (but still within Italy).<sup>22</sup>

The widespread changes have also involved the downstream side of activity. The growth in exports from the districts in 2014 and 2015 was a result of their revitalized competitiveness, linked to the evolution of the approach to internationalization and the modification of the competitive strategies of the district firms. In the past, international competitiveness was based on the division of labour and specialization at the district level, which allowed the district firms to benefit from economies of scale that – accompanied by good quality products – gave them an advantage in price competition. When differences in inflation or costs made it difficult to compete successfully on price, the devaluation of the Italian currency restored the competitiveness of Italian firms. With the adoption of the euro, this strategy of recovering price competitiveness through

cadenced devaluation became impossible. Moreover, competing on price with producers from emerging markets would have been hopeless. The successful district firms were those that changed their competitive strategy from a strategy of cost leadership to "differentiated leadership".

Regaining competitiveness was strongly helped by the strength of the Made in Italy brand in most of the industries of district specialization. The positive "Country of Origin Effect" played (and plays) an important role in the international competitiveness of Italian products in the field of mechanical engineering as well as in more traditional areas such as food and clothing, where low-cost competitors would otherwise have a free run at obtaining market share. The strength of the Made in Italy brand, however, would not have been sufficient without product innovation, the personalization of products, diverse distribution strategies, and direct control of after-sales services, all of which increased the ability of companies to retain customers and to reinforce both the components of the Country of Origin Effect (Han 1989).<sup>23</sup> In the period following the 2008 crisis, an increasing number of district firms – and not only the leading or larger ones in the district – implemented multifaceted export strategies. Moreover, in the increasingly frequent cases of the localization of production lines abroad (Mariotti and Mutinelli 2017),<sup>24</sup> the main motivation ceased to be cost savings and became the possibility to operate in a more direct and immediate way in markets of high importance to the firm.

These developments were able to produce a change in the nature of the districts that now could become "bodiless" sorts of entities. They could transform into multi-localised entities in which the territory of origin of the "district" became the seat of design and development and of more sophisticated and non-transferable functions, while the structures located abroad increasingly became nodes of production and distribution networks focused on regional markets.

The most striking change in the system of relationships, however, is not that which affects the knowledge exchanges and the supply and production networks, but the one that modifies the social networks and the internal connections of the district. These connect the various actors that have given life to the district: smaller firms, industry associations, local banks, local foundations, chambers of commerce, and higher education institutions. The leading firms in the district, and smaller ones too, have in this period loosened their links with these subjects and organizations, preferring to make connections with outside networks that facilitate the process of internationalization and technological development. However, quite a few companies have found that some problems, such as the need for specialized vocational training or financial institutions that are connected with and knowledgeable about local situations, can be better addressed through the activities of local subjects rather than external ones.

The issue of the intensity of the links between the business players of the district and its territory, and the connections between the district as a productive unit and the social capital of the district as a community remains at the fore. Although the relational

framework in which the district firms operate is constantly and increasingly evolving, the elements that constitute the foundations of the district are always present. Certainly, the link with territory is changing and is apparently looser; collaboration networks are changing their shape and extent. However, the district is still a manifestation of the specificities and the values of its territory and its community. It is still the outcome of know-how that was accumulated over a period of time which is ingrained in its social capital. Not all districts have weathered the storm of the emergence of third-world (particularly Chinese) manufacturing and the Great Recession; many have sunk under its onslaught. Many others have survived, changing when necessary, and preserving what is useful. By 2015, the surviving districts were still vital and competitive elements of world markets and were still at the forefront of the development of the country.

In subsequent years, the districts again showed that they are the place where operations that foster innovation – be this technological, organizational or market-related – are more readily adopted and disseminated. District firms performed better than non-district ones. In the districts there is a higher proportion of exporting firms than in the country as a whole (38% vs. 28%), of firms with internationally registered trademarks (31% vs. 25%), of involvement in Foreign Direct Investment (29 firms invested in for every 100 district firms vs. 20 for every 100 firms nationally) (Intesa Sanpaolo – Direzione Studi e Ricerche 2017). The fact that district firms of every size are present on foreign markets is indicative of the permanence and intensification of informal and sometimes unintentional mechanisms for exchanging and sharing knowledge about the markets that have always been present in the districts. These mechanisms activate a process of imitation of commercial strategies adopted by the most active firms that permits many other smaller firms to compete internationally.

In the critical years after the financial crisis, another development also took place in Italian manufacturing structures. The impact of the often intangible factors of competitiveness that have always characterized these territories gradually strengthened and became more disseminated, and led to the concentration of entire sectors in the districts. As a result, many sectors, such as tanning, footwear, hosiery, jewellery and tiles, are now strongly if not exclusively concentrated in districts. It appears that the districts continue to generate positive externalities which support the global competitiveness of their firms. Moreover, this creates a context that favours investment in the ever more specialized districts by larger Italian firms, as well as foreign multinationals (De Michele 2017).

This rediscovery of the districts as a competitive home base, attracting FDI from foreign multinationals – either in the form of acquisitions of local firms or the establishment of new production units – has had an additional positive consequence. The leading district firms that kicked off the process of Delocalization from the districts in the 1990s have now started to bring back to the district their production (or at least a part of it). Indeed, the perception of quality linked to the Made in Italy brand and the distinctive and specialized competences of the districts are encouraging the phenomenon of “*reshoring*,”



the bringing back of production activities once delocalized to low-cost countries to the place from where they originate (Fratocchi *et al.* 2015). Numerous cases of reshoring have occurred in the fashion industry as well as in furniture and household goods and mechanical engineering. This has led to a revival of production in the districts, with a consequent increase in local employment. This has also required renewed focus on high-end segments of the market, which allows these firms to counterbalance the higher costs of production in a country such as Italy compared to emerging countries (such as Turkey and China).

The evolution of the last few years thus points to the resilience of the districts. Those that have weathered the storm have renewed their competitiveness by reinterpreting their traditional factors of strength, leveraging them to reestablish their centrality in the strategies of local firms, and by developing new ways to reinforce and extend the network of connections that helps circulates their vital “lymph”.<sup>25</sup>

In order to understand how some districts have weathered the storm, and some have not, a brief analysis of two districts is presented. The tannery district of Arzignano – Valle del Chiampo is a district that has managed to overcome difficulties, and whose firms are still successful players on world markets, while the chair-making district of Manzano is a district that has gone through a near-death experience over the last decade and, despite attempts at reviving it, is a shadow of its former self.

### 5.1 Case study: the Arzignano-Valle del Chiampo tannery district

This tannery district, located in the Valle del Chiampo (in the Venezia Province, about 90 km west of Venice), includes 15 communes extending over 130 Km<sup>2</sup> and has a population of 99,000 inhabitants. Economic activity in this area is heavily concentrated in the tannery industry, which employs 8,500 people in 458 local units (Unione Nazionale Industria Conciaria 2018). It is the biggest of the three areas in which most of the Italian tannery industry is located (see Table 1).

**Table 1:** Italian tannery industry, 2017

District	Number of firms	%	Number of employees	%	Value of production in EUR million	%
Valle del Chiampo	458	37.2	8,498	47.9	2,867	56.2

<b>S. Croce sull’Arno</b>	526	42.7	5,762	32.4	1,420	27.8
<b>Solofra</b>	157	12.7	1884	10.6	360	7.0
<b>ITALY</b>	1231	100.0	17,746	100.0	5,100	100.0

Source: Unione Nazionale Industria Conciaria (2018).

The tannery industry has always been one of the strong points of Italian manufacturing. In the last seventy years it has gained increasingly significant weight on international markets, becoming the largest producer and the largest exporter of leather in the world. It kept this position until the turn of the century, when it was overtaken, in terms of quantity produced, by China.<sup>26</sup> It still remains the leading producer in terms of value: in 2018, the value of Italian leather products amounted to 20% of the world total. Even more predominant is the position of Italy in international trade: the export of leather (finished hides) amounts to 27% of the world total (Unione Nazionale Industria Conciaria 2018, 18).<sup>27</sup> The industry employs 17,746 workers in 1,213 firms (if ancillary industries are included, the figures can be doubled). Almost 75% of the production of industry is exported, making it one of the most export-oriented activities in the country. In 2017, the value of exports was € 3.8 billion.

As in the case of many other industries in Italy, tanneries are also concentrated in specialized districts. Indeed, 1,141 firms (94%) and 16,144 workers (91%) creating products worth € 4.65 billion (91%) are localised in the three districts of Arzignano-Valle del Chiampo, S. Croce sull’Arno (near Pisa), and Solofra (in the province of Avellino, in the mountains 70 km east of Naples). Arzignano is the biggest of these, accounting for 38% of firms, 48% of workers and 56% of the turnover of the tannery industry in Italy. Moreover, the Arzignano district is one of the districts that evolved earlier under the Area Sistema structure. Therefore, the tanneries, many specialized in some phases of production or in certain types of skins or final products, are supported by a whole set of firms specialized in collateral activities. So-called "ancillary" industries here range from the mechanical engineering industry that creates the specialized machinery required by the tanning process to the chemical industry that makes specific products for the various phases of processing of hides, from marketing services to traders.

## 5.2 History of the Valle del Chiampo district

In the Valle del Chiampo tannery traditions are deeply rooted. The first modern record of the presence of a tannery industry in the Vicenza province dates back to 1366, and in documents from the first decades of the following century can be found the first references to tanneries in the Valle del Chiampo. In those years, the acquisition of the territory of Vicenza by the Most Serene Republic of Venice (AD 1404) — opening up the territory to the Venetian trade network — created the conditions for the expansion of

economic activities in the area. Among these were the tannery industry in valleys such as the Valle del Chiampo, rich in water and in trees from which tannin could be extracted.

For a couple of centuries this activity prospered for a couple of centuries, but the weakening of Venice also brought about an economic slump, which impacted on the tannery industry as well. From the middle of the seventeenth century, tanning activities declined, and by 1746 only four tanneries were left in the Valle del Chiampo (Zampiva 1997). The industrialization of the Province of Vicenza in the nineteenth century was based on the textile industry, and in particular, wool. In the Chiampo valley, towards the end of the century wool was superseded by the production of silk.<sup>28</sup> Tannery activities, although still a deeply rooted, by 1907 were undertaken by only three smallish firms (which were at the forefront of the revival of the industry in the valley in the following decades) (Fontana 2004). In subsequent years, the silk industry was challenged by a decline in demand during the two world wars and by strong Japanese competition. This crisis intensified in the 1950s and the last spinning mill was closed in 1968, when the leather industry was already booming.

The expansion of the tanning industry in the Chiampo valley can be rightly defined as a boom that started in the 1950s. The revival of this industry had a slow start during the years of the First World War and the interwar period. By 1927, seven tanneries were operating, employing 94 workers (see Table 2). As early as in the years immediately after the Second World War, tanneries opened up in the valley, trebling the number of firms that were present and workers employed.

**Table 2:** Evolution of the tannery industry in the Chiampo valley in the twentieth century

Year	1907	1927	1951	1961	1971	1981	1991
<b>Firms (Local units)*</b>	3	7	19	100	161	602	447
<b>Employees</b>	n.a.	94	361	1,929	3,209	6,358	7,2

\* Note: the figures refer to local units: a larger firm may have more than one local unit.

Source: Author's construction using data from Unioncamere (2016) and ISTAT (2019).

Initially, the birth of the district was due to the growth of a few historical firms that expanded their production and increased their dimensions. The real launch of the industry and the establishment of a proper industrial district happened in the 1950s when an increasing number of technicians and even workmen employed by those firms decided to become independent and set up their own small firms. By the end of the decade, the

number of tanneries in the valley as well as the people employed by them had increased fivefold. These processes of spin-off from existing firms continued in the following decades and were fostered by the growth of international demand that stimulated the establishment of new firms also specialized in trading (raw material inputs) and marketing sectors. The fact that the larger firms preferred to keep abreast of the growing demand not so much as by internal expansion as through growing recourse to subcontracting gave the district its specific structure based on the external division of tasks and deep specialization.

The 1980s saw the first period of contraction. In the first part of the decade, the tanning industry suffered the effects of the unfavourable economic situation that hit the Italian economy in those years. Then, when the Italian economy started recovering, the tanning operators realized that the problems of the sector were not cyclical but structural. Until then, the output of the industry was mainly absorbed by downstream industries in Italy: footwear, leather goods, furnishing, apparel, all highly successful industries with a strong position in world markets. However, in the early 1980s these downstream industries were in difficulty: the downsizing of the leather goods sector was followed by that of the main customer of the tanneries: the Italian footwear industry, which had become less competitive (mainly on price, but also because of fashion). In other downstream sectors, too, Italian products were losing market share. It appeared that national demand was going to remain stagnant, and that for products of medium-low quality was definitely contracting. This led to a structural surplus of supply that had the potential to cause the downfall of the Italian tanning industry and the demise of the Arzignano district.

By the middle of the decade, many operators were in serious difficulty: the drop in orders from downstream industries led to cash-flow problems for larger companies, which in turn stopped payments to suppliers and subcontractors. Firms started going out of business and unemployment became a problem for the first time in thirty years. This led to reactions from the whole district, from firms to local authorities (Panati *et al.* 1988). The firms made considerable effort – in technological innovation, in managerial modernization and in promotional activity – that required some time to bear fruit. There was a serious process of restructuring among the firms of the district following the closure and merging of several companies. While the less efficient firms dropped out of the market, the most solid ones were able to take over these failed activities and start a process of concentration. By 1991, the number of active firms was down by about one quarter, but efforts were showing some results and the number of people employed in tanneries was already picking up (+ 13% on 1981).

### 5.3 The evolution of the district and its internationalization

The local authorities favoured the establishment of support services that could be shared by all the firms. They helped the latter to cooperate in their approach to foreign markets and to develop a positive image of the production of the district rather than (or in addition to) that of single companies. The shift to higher quality, facilitated by technological

innovation, the improvement of the image of the products of the area, the push to find new uses for products, and the joint drive with downstream firms to regain leadership in fashion were the factors that allowed the district to overcome difficulties and reshape itself for a new period of successful growth.

The consolidation and the recovery of the district also stemmed from the activities of the supporting institutions and of related and supporting industries. The former concerned the training of workforce and the provision of infrastructure (in particular, the establishment of a purification plant to raise compliance with new anti-pollution rules), and the latter to the expansion in the district of firms in ancillary industries. This included suppliers of inputs, such as chemicals for the tanning process and specialized machinery or traders specialized in different types of hides, as well as suppliers of services and even some downstream industry. In particular, in those years a process of the establishment of small firms in the mechanical engineering industry took place in the western Vicenza area. It also involved the district, where a thriving industry for tanning machinery developed.

The 1990s saw the full transformation of the industrial district of the Valle del Chiampo into a fully-fledged Area Sistema (see Table 3). The development of new technologies for tanning machinery was undoubtedly a form of support for the development of the district. In little more than a decade, because of extremely demanding local customers, the local producers of specialized machinery for the tanning industry reached a high technological level that made them uncontested world leaders in their sector.<sup>29</sup>

**Table 3:** Evolution of the tannery Area Sistema of Chiampo valley (1991–2001)

Activity		1991	1996	2001
Tanneries	Firms (Local units)*	447	594	644
	Employees	7,2	9,341	10,111
Travel items, bags, saddlery	Firms (Local units)*	27	21	22
	Employees	135	83	258
Leather gloves and belts	Firms (Local units)*	7	13	9
	Employees	47	93	47

<b>Making, installing machines for the leather industry</b>	<b>Firms (Local units)*</b>	32	33	44
	<b>Employees</b>	558	592	570
<b>Materials used in fixing textiles and leather</b>	<b>Firms (Local units)*</b>	9	13	20
	<b>Employees</b>	132	179	357
<b>Wholesale trade of skins, including leather</b>	<b>Firms (Local units)*</b>	89	106	139
	<b>Employees</b>	207	272	340

\* Note: the figures refer to local units: a larger firm may have more than one local unit.

Source: Banca Intesa (2006).

This evolution gave renewed strength to the district and allowed it to take advantage of the revival of Italian downstream industries, which in turn had overcome the crisis of the 1980s. Moreover, this regained strength allowed the firms of the district to launch their conquest of international markets. These two factors combined to make the 1990s a period of high growth for the district.

In particular, the expansion of the district firms in international markets was quite remarkable and in itself the cornerstone of the success of the 1990s. In this period, the district became one of the most important players in the world tannery industry, with sales on foreign markets growing from 430 million Euros in 1991 to 1,537 million euros in 2000, with an average growth rate of more than 28% per year for the whole decade. In some markets, the growth of the value of exports was truly astonishing: more than tenfold<sup>30</sup> (see Table 5 below).

The number of firms engaged in the main form of industry grew by 44% and the number of people employed by 40%. This was a new golden period for the district, which achieved the highest number of firms and employees in that industry.

#### 5.4 Double-edged globalization

However, the evolution of the competitive environment was again moving in an adverse direction and the problems that were pointed out earlier when discussing of the evolution of the industrial districts were becoming graver. The international expansion of the firms of the district, which initially was aimed at gaining control and protecting the supply of hides, was changing in nature and motive. Initially, because many governments of

supplier countries pressed for higher prices for their exports, firms started delocalising the first phases of the tanning process. The alternative of buying the semi-processed hides from external suppliers did not appeal to the tanneries of the district, because using these inputs presented the risk of a loss of quality control and innovation in the upstream phases of production. The answer was to control, through various forms of Delocalization, the production phases located in the countries of origin of the hides.

Of course, the lower labour costs and the laxer environmental protection rules in those countries were strong additional motives for such a move. Indeed, the increasing price competition brought about by low-cost producers enhanced the attractiveness of a Delocalization strategy. Moreover, similar transformation taking place in the downstream industries (apparel, footwear, and furniture) made a *follow-the-client* strategy more attractive for the tanning companies of the district. In addition, some of these countries were developing their own industrial basis and represented interesting and growing markets of their own. However, this strategy required some of the tanneries to also shift the more advanced phases of the production process to the emerging countries where their clients had moved, or where new clients could be found. These were the ones with highest added value, and on which the competitive strength of the district was based.

**Table 4:** Evolution of the tannery industry in the Chiampo Valley at the turn of the century

Year	1991	1996	2001	2004
<b>Firms (Local units) *</b>	447	594	644	482
<b>Employees</b>	7,2	9,341	10,111	12,482

\* Note: the figures refer to local units: larger firms may have had more than one local unit.

The years after the turn of the century involved a tightening of competition, also due to the considerable appreciation of the euro against the dollar, which made it impossible to compete on price with the producers of emerging low-cost countries. These were years of renewed difficulty: performance on foreign markets significantly worsened, turnover and especially profits plummeted. The weakest firms were immediately in trouble, while the most robust ones kept on operating (with less profit) and even increased the number of their employees (see Table 4).

After the success and growth of the 1990s, when – as we have already seen – the number of firms increased by 44% and that of their employees by 40%, in the first few years of the twenty-first century one-quarter of all firms disappeared (-25.2% from 2001 to 2004). This was not immediately reflected in the employment figures: in 2004, the number of employees in the tannery industry reached a maximum of 12,482 (an increase of 23.5% over the same three years). Exports, the main engine of growth of the previous years,

faltered: in the three years leading up to 2003, exports were down by 4.8%, at a yearly rate of 1.7%. (see Table 5).

**Table 5:** Evolution of tannery industry exports from the Vicenza province\* (1991–2004)

	1991			2000			2004			91/2000	00/03	2004
Country	€M	%		€M	%		€M	%		Δ % yr	Δ % yr	Δ %
Germany	95.4	22.2		225.1	14.6		188.3	12.7		15.1	-7.5	5.5
USA	18.3	4.3		243.4	15.8		173.1	11.7		136.6	-7.9	-8.9
Hong Kong	12.3	2.9		144.7	9.4		170.4	11.5		119.6	6.5	-2.6
France	86.2	20.1		116.9	7.6		96.9	6.5		4.0	-13.2	26.8
Spain	26.5	6.2		97.8	6.4		81.2	5.5		29.9	-8.1	6.8
Poland	2.7	0.6		36.0	2.3		81.2	5.5		137.0	33.8	-6.0
UK	28.7	6.7		98.0	6.4		76.0	5.1		26.8	-6.8	-4.4
China	0.4	0.1		11.6	0.8		67.7	4.6		311.1	60.4	41.8
World	429.6	100.0		1537.4	100.0		1487	100.0		28.6	-1.7	1.6

\* Note: Statistical data for exports are available at the province level.

Source: Author's construction using data from Intesa Sanpaolo (2017) and ISTAT (2019).

Initially, this difficult period led to consolidation of the industrial base: while the number of firms decreased sharply, the number of employees kept rising. The effects of this consolidation were rapidly felt: by 2004 exports started increasing again, albeit at a snail's pace. As happened with the whole Italian economy, the district started growing again and kept growing (at a much reduced rate in comparison to the previous decade) for the next few years, reaching a peak in 2007 when products of a value of 1,700 million euros were exported.



**Table 6:** Evolution of exports of the tannery industry in the Chiampo valley (2000–2010)

Year	1991	2000	2004	2007	2008	2009	2010	2011	2016	2017
<b>Exports € million</b>	430	1,537	1,487	1,700	1,565	1,229	1,370	1,488	2,270	2,379
<b>Growth rate</b>	--	*16.9	°0.81	*4.77	<b>-7.9</b>	-21.5	11.5	8.6	*10.5	4.8
<b>Index (2000=100)</b>	28.0	100.0	96.7	110.6	101.8	79.9	89.2	96.8	147.6	154.7

\* Note: Average per year for the period, note ° idem, but 2004 saw an increase, see also Table 5.  
Source: Author's construction using data Unioncamere (2016) and ISTAT (2019).

This period of renewed growth was cut short by the Great Recession which started in the second half of 2008. In that year its hindering effects were already felt in the district, which saw exports decrease by almost 8% to return to the levels of eight years earlier, while the number of people employed in the tannery industry fell by more than 9% (see Tables 6 and 7).

**Table 7:** Evolution of the tannery industry in the Chiampo valley from 2004

Year	2004	2008	2010	2012	2014	2015	2016	2017
<b>Firms (Local units)*</b>	482	480	475	472	469	467	459	458
<b>Employees</b>	12,482	11,283	*8,183	8,220	8,358	8,341	8,324	8,498
<b>Value of Production \$ billion</b>	2.53	n.a.	2.29	2.48	2.8	2.81	°2.73	3.08

\* Note: the extremely sharp fall in the number of employees (72%) is partly due to a change in the way the statistical service counts people who are employed in industry. The decline in 2016, as well as the growth of 2017, were emphasized due to the vagaries of the dollar-euro exchange rate.  
Source: Author's construction using data Unioncamere (2016) and ISTAT (2019).

The full shock of the crisis arrived in 2009, when markets folded, exports collapsed (-21.5%) and companies started shedding employees. There was a reaction to this, and

2010 saw an upturn in exports, followed by another smaller one in 2011. However, the value of production and exports was still lower than in 2000, and the number of people employed was sharply reduced. The district as a whole stumbled along, and the situation, already quite bad, was made worse by the attempts of many local companies, among them some of the biggest ones in the district, to weather the storm by avoiding paying taxes.<sup>31</sup> The following few years brought additional troubles and it took until 2014 for the value of production to rise above the level of the year 2000.

The process of consolidation in the district continued, but at a much slower pace, and the fall in the number of employees stopped. The last few years have seen a good recovery (although with fluctuations): the value of production has stabilized and lately increased. Exports were the engine of this recovery, reaching new heights in 2016 and 2017.

### **5.5 Survival and recovery of the district**

The deluge caused by the successive bursting of the Chinese tanneries onto world markets and the Great Recession caused serious problems for the district. However, it was able to face the challenge and seems to have rediscovered ways to remain the world leader in the production of leather, safeguarding both the profitability of its companies and the compactness of the area, its firms, its institutions, and its population.

The firms in the district managed to overcome the challenge of the low-cost producers by focusing on the most profitable activities and positioning their products in the high-quality segments of the market. Innovation in production process and in inputs (machinery and chemicals) helped maintain and sometimes increase this lead in quality. This allowed the district firms to keep in the district a large part of higher added value activities, even increasing the value of some of them. Additional attention was paid to services or combinations of products and services that are particularly significant in the B2B markets in which they operate.

As already mentioned, the engine of the recovery is exports: an increase in sales in many traditional markets and successful penetration in new markets. Particularly remarkable is success on the Chinese market: having lost out to Chinese leather producers the low price segments of the international market, the Arzignano tanneries (as well as those of the other Italian tannery districts) have managed to establish themselves firmly as preferential suppliers for high quality leather to the downstream Chinese industries.<sup>32</sup>

A very important step in the recovery of the district and in the maintenance of the leading position in quality products and preserving the compactness of the district as a socioeconomic unit was the keen attention paid to – and huge investments in – controlling environmental impacts. Indeed, the choice to take the road of environmental sustainability and transparency with regard to the production process, in particular in the use of chemical substances, is a trend common to the entire Italian tannery industry. In

the year 2016 the industry spent on sustainability measures 4.4% of turnover, compared to 1.9% in 2002. This not only makes for a better living environment for the inhabitants of the district (from the owners of the firms in their villas halfway up the side of the hills to the shop-floor workers in their flats in the valley – both of whom breathe the same air), but also creates a competitive advantage in the eyes of downstream customers.

The top international brands (in fashion, the automotive industry, interior design and furniture) that are their most important clients deem having a sustainable business strategy a necessity and require this of their suppliers. Therefore, environmentally friendly suppliers are in a strong competitive position. Italian tanneries, including those in the Arzignano district, have been very proactive in this field. Most firms now have environmental certification; programs for reducing the use of water (consumption in 2016 was 20% lower than in 2003), energy (-32%) and chemicals (-4% from 2007) are widespread (Unione Nazionale Industria Conciaria 2018). Further efforts are being made to improve the treatment of waste water, reduce emissions to atmosphere and to recover and use waste products.<sup>33</sup>

Innovation, the search for new markets, attention to the sustainability of production and to the local environment have allowed the district to stand up to competition from other countries, to maintain its position as a leader in the industry, and to keep in large part intact the social structure that gives it its extraordinary resilience in the turbulent economic environment of the present times.

## 6            **The Manzano "Chair district"**

The "chair district," located in the eastern part of the Friuli-Venezia Giulia region (province of Udine, about 110 km north-east of Venice), includes 11 communes extending over 224 Km<sup>2</sup>, and has a population of 37,000 inhabitants. Economic activity in this area is heavily concentrated in the furniture industry, specifically chair-making, which employs 5,500 people in 878 local units that belong to 660 firms (Magliocchi 2015a; 2015b). It is one of the many (12) districts in Italy specialized in the production of furniture; indeed, it is among the five most important districts in this industry,<sup>34</sup> but it is the only one focused almost exclusively on making chairs.

The furniture industry is another of the strong points of Italian manufacturing. The furniture sector (excluding the upstream activities of the first processing of wood) comprises 18,000 firms employing 132,100 people and has a turnover of about 21 billion euros, of which 44% comes from exports.<sup>35</sup> This is another of the industries in which Italian producers have for a long time dominated international trade. Italy became the leader in world exports in the 1980s and 1990s, and in particular in the first half of the 1990s when the devaluation of the lira noticeably increased the competitiveness of Italian producers. From the turn of the century, this position was gradually eroded, due both to an unfavourable trend in the exchange rate<sup>36</sup> and to the diffusion in the international markets of products from emerging countries (see Table 8).

**Table 8:** Exports of Product 94: Furniture; bedding, mattresses, cushions, etc. Million US \$

Year	2001		2004		2008		2010		2012		2014		2016		2017	
Country	M US\$	%	M US\$	%	M US\$	%	M US\$	%	M US\$	%	M US\$	%	M US\$	%	M US\$	%
China	2,421	7.4	5,986	13.0	13,737	19.2	18,041	27.7	27,017	34.4	28,435	33.3	25,912	32.6	26,560	31.4
Germany	2,874	8.8	3,951	8.6	7,688	10.8	6,639	10.2	7,492	9.5	7,912	9.3	7,228	9.1	7,462	8.8
Italy	4,836	14.8	6,286	13.7	9,315	13.0	7,049	10.8	7,293	9.3	7,919	9.3	6,910	8.7	7,223	8.6
Vietnam	199	0.6	716	1.6	1,841	2.6	2,129	3.3	2,655	4.0	3,430	4.0	3,901	4.9	5,882	7.0
Poland	1,123	3.4	1,937	4.2	3,644	5.1	2,920	4.5	3,154	5.0	4,234	5.0	3,985	5.0	4,314	5.1
USA	1,819	5.6	1,826	4.0	2,922	4.1	2,607	4.0	3,122	3.8	3,233	3.8	2,893	3.6	2,946	3.5
Canada	3,184	9.7	3,337	7.3	2,874	4.0	1,993	3.1	2,115	2.7	2,273	2.7	2,758	3.5	2,818	3.3
World	32,683	100.0	45,963	100.0	71,486	100.0	65,214	100.0	78,648	100.0	85,436	100.0	79,381	100.0	84,454	100.0

Source: International Trade Centre (2018).

In particular the entry and success on the international markets of producers from countries with cheap labour (*in primis*, China) exerted considerable competitive pressure, above all on Italian production positioned in the medium-low market segment. This caused a loss of market share in world exports as early as in the first half of the 2000s, which after a short recovery became steeper after the crisis of 2009 and steadied only after 2015.

As is made clear by Table 8, although other players gained significant market share in the 17 years of this century, the real disruptive influence was China, whose share grew from 7.4% in 2001 to 31.4% in 2017.<sup>37</sup> Italy is now in third place as an exporter of furniture and has been overtaken by Germany, which declined more slowly after the crisis.

However, the decline did not affect all the Italian furniture companies to the same extent; some of them managed to weather the storm better than others. Comparison of the performance of the main districts explains these differences. In the first years of this century, when Chinese competitors appeared on global markets, some districts (Murgia and Manzano) felt more stress than others. They also missed out on the partial recovery in the middle of the decade and felt most heavily the impact of the 2009 Great Recession. The explanation for the great difficulty encountered by these two districts is in their competitive positioning in terms of production processes, product quality and product differentiation. Those districts, which were already focused on high quality furniture and differentiation of their offerings, could better withstand the price competition from emerging countries and even take advantage of the purchasing power of the increasingly rich segments of those countries.

The Murgia and Manzano districts, however, were negatively affected by their focus on a single type of product that in the heyday of their companies did not require much

attention to high quality. These characteristics fully exposed the firms of these districts to the strong price competition of Chinese producers. Within a few years, the latter had taken leadership positions in all the main markets of the sectors in which the firms in the Murgia and Manzano districts were specialized (upholstered furniture and chairs, respectively). The situation of the firms in these two districts worsened after the 2009 Great Recession and few of them have managed to maintain or regain their competitiveness. As a consequence, these two districts have gone through a very disruptive experience.

## 6.1 Historical development of the Manzano district

Although the origins of chair-making in the eastern part of Friuli can be traced back to the second half of the eighteenth century, the initial establishment of chair-making producers in Manzano is dated to 1878. In short, a growing number of craft undertakings and small family businesses developed in three neighbouring municipalities,<sup>38</sup> bringing into being what became known as the "*Triangolo della sedia*" (the "chair triangle"). In the years around the turn of the nineteenth century chair-making activity spurred the process of industrial development of the area. The First World War brought to an end this initial development. For more than three years the front line at Isonzo was less than twenty kilometres away. Austro-Hungarian forces then occupied the area after the battle of Caporetto, and it was liberated by Italian forces one year later, after the battle of Vittorio Veneto, just before the armistice that brought to an end the war on the Italian front. At the end of the war, 70% of the industrial potential of the area had been destroyed.

In the following years, the area recovered (also thanks to the expansion of the border of Italy to the east) and by 1928 a few hundred firms were active in the wood and furniture industry. Almost all were small or very small family-run, artisan businesses, usually located within family homes. Some elements of the district structure started to appear, insofar as the process of specialization commenced with the development of a network of firms that complemented each other, with the largest ones subcontracting some of the components of the final products.

The Second World War also brought disruption to the area, and the recovery took some time. However, in 1951 the district already counted 3,545 people employed in the wood and furniture industry (91% of whom within the three original communes of the "chair triangle"). As with most of Italy, the 1950s and 1960s were times of growth. For most of this time, the development of the district followed the same pattern as the interwar period. Craftsmen and businessmen (the latter most often belonging to the former group) built their plants or – usually – workshops close to their homes. These small firms seldom had the resources to manage the whole production process internally, and this created the mesh of interdependency that bound them together.

Here, too, the district as a socio-economic phenomenon emerged. Local firms, although pursuing their own interests, closely interacted. This was justified in economic terms by

the division of labour that – by having each firm focused on a single or a few phases of production – fostered the development of highly specialized skills. This helped the district as a whole to act as a vertically integrated company, in which each phase was carried out by a different firm that worked to the highest standards. Close interaction was also justified (and fostered) on social grounds, facilitating collaboration based on mutual trust. Most of the owners of these firms knew each other. As villagers, they went to the same school, met in the same bars, shared leisure activities, and often had links of kinship or friendship. For these reasons, the risk of opportunistic behaviour was much reduced and transaction costs between local firms were very low.

This season of growth was brought to a temporary halt by the end of the Italian "economic miracle" in the late 1960s, followed by the oil crisis and general worsening of the global economic atmosphere of the early 1970s. Just when a slow process of recovery had just started, an additional blow hit the area in 1976 in the form of a disastrous earthquake. The district was only partially affected, with six municipalities out of eleven being designated "damaged localities" (one of which "gravely damaged").<sup>39</sup> Industrial activity also suffered, but the process of recovery from the slump of the early 1970s, already under way, slowed but did not stop. By 1981, the district was again growing rapidly. It had close to 1,000 local units in the wood and furniture industry, with 12,000 employees (see Table 9).

**Table 9:** Local units and employees in the Chair District of Manzano (1951–1991)

Year	1951	1981	1990	1991
local units	n.a.	n.a.	1,126	1,022
employees	3,545	12,045	11,661	10,188

Source: Jelen (1993, 168).

The 1980s were a period of growth, marred by some slowdowns, particularly towards the end of the decade. By 1991, the number of units, after some additional growth, had returned to the number at the beginning of the decade and the number of people employed had declined to around 10,000.

The heyday of the chair district was the 1990s. The globalization process entered an accelerated phase and the firms in this district took full advantage of it and of a favourable environment. Exports soared, and within a few years the Manzano district had become the world superpower in the chair industry. About 50% of all the wooden chairs produced in the then 12 countries of the European Union and almost 80% of those made in Italy were produced in the district (Jelen 1993). An important component of this growth was expansion into foreign markets.

**Table 10:** Italian exports of chairs and seats (ATECO CM31092) (1991–2000)

	1991	1993	1995	1997	1999	2000
Thousand euros	472,498	627,409	810,335	882,204	1,015,484	1,140,597
% of world exports	n.a.	n.a.	18.8	18.0	18.5	19.4

Source: Author's construction using Coeweb-ISTAT (2019) and UNCTAD data (2019).

Around 90% of Italian exports of chairs came from the Manzano district; in this decade they increased by 142% to reach a value of 1.14 billion euros (see Table 10). The district dominated trade in this type of product and for a long time was the largest world exporter of this item of furniture, with close to one-fifth of all chairs sold across borders coming from its eleven municipalities. However, towards the end of the century signs that things were changing started appearing. Competition from emerging countries strengthened and Chinese producers began a phase of expansion that would lead to the conquest of international markets.

## 6.2 The crisis of the Manzano district

Since the beginning of the 2000s, the Manzano chair district has entered a period of productive and occupational crisis that has almost brought about its demise. The downturn was sudden and due to a combination of factors. Endogenous structural factors (the obsolescence of products and scarce technological innovation) affected the competitiveness of the district and weakened it, making it more vulnerable to the influence of subsequent exogenous factors triggered by the global crisis of 2009.

The most obvious exogenous factor was the competitive push of Chinese firms. Chinese producers, who had begun their expansion in the second half of the 1990s a few years after the accession of China to the WTO, stormed world markets and obtained a hegemonic position (see Table 11), accounting for 6.3% of world exports in 2001, reaching a high tide mark of 34.1% in 2014.<sup>40</sup>

**Table 11:** Share of exports in seats, etc. (SH4 9401); selected countries (2001–2017)

Year	2001	2004	2008	2010	2012	2014	2015	2016
Italy	14.3	12.1	7.9	6.1	4.9	4.9	4.5	4.7
China	6.3	11.2	24.5	28.8	34.1	32.3	33.5	30.7
Mexico	10.1	9.0	5.8	6.4	7.3	8.5	8.9	9.1
Poland	5.1	7.4	8.0	7.8	7.1	7.6	7.3	7.7
USA	11.1	7.2	5.8	5.7	5.8	6.1	6.4	6.4
Germany	8.0	7.9	7.8	6.9	6.6	6.1	5.9	5.7

Source: Author's construction based on International Trade Centre (2018) data.

Considering that until the end of the century Italian producers had befit from the competitive devaluation of the lira, the adoption of the euro – and the consequent impossibility of devaluing the currency – itself constrained their competitiveness. To this must be added that after the freezing of the exchange rate of lira-euro in 1999, after a period of slight weakening the euro appreciated significantly in relation to the US Dollar (by 2004, the dollar exchange rate had fallen by 39.8% and touched its lowest point in 2008 when the fall reached -65.3%<sup>41</sup>). One of the most important factors that had driven exports and the production volumes of the district, *price competitiveness* – linked to the exchange rate, lower labour costs compared to European competitors and the “district economies” – had suddenly disappeared. Moreover, an additional threat on the international market became evident: producers from Central-Eastern Europe, in particular Poland. An additional factor of the structural weakness of the Manzano district became apparent: wooden chairs are not a complicated product to make, and many small firms from the district had never tried to improve them. Competition from Asian and central-Eastern European producers was strongest in the market for low-cost products, which were also those items sold in the largest quantities.

The result of these changes was a general loss of competitiveness of district firms on international markets, which led to a sharp decline both in the value of exports (-22.3% from the peak of 2000 to 2008) and in the share of world exports (see Table 12). The growth of new competitors, in particular Chinese ones, was a structural feature of the competitive context of the sector. This explains why the crisis of the district did not abate, as happened in the Arzignano tannery district after the middle of the decade. The plunge in exports caused, as a result, a fall in the production and profitability of almost all businesses; numerous closures of firms, and a corresponding loss of jobs. An additional factor amplifying the production and employment crunch was – as happened in most Italian districts – the (partial) Delocalization of the production process undertaken by some of the large firms from the district.



**Table 12:** Italian exports of chairs and seats (ATECO CM31092) (2001–2008)

	2001	2002	2003	2004	2005	2006	2007	2008
Thousand euros	1,130,637	1,102,137	1,009,807	961,336	896,051	903,966	915,601	886,614
% world exports	16.4	16.2	15.2	13.0	10.7	9.4	9.0	8.1

Source: Author's construction using Coeweb-ISTAT (2019) and UNCTAD (2019) data.

These firms assigned to their newly established subsidiaries or joint ventures in countries with low labour costs the task of supplying semi-finished products previously supplied by small-sized district firms. The latter had prospered by performing this task well, but could not match the low cost of production of the former countries. The outsourcing strategies implemented by their traditional district customers shrank their market and caused their demise in growing numbers.

From 2001 to 2008 the number of local units fell by 38% and employment in the sector fell by 21% (see Table 13), and the worst was yet to come. Even more threatening for the fate of the district than the shrinking number of companies and employees was the loss of know-how and professional skills necessary for carrying out the various phases of production.

**Table 13:** Local units and employees in the Chair District of Manzano (2001–2010)

Year	2001	2004	2008	2010
local units	1,289	1,212	796	734
employees	10,684	9,253	8,326	7,299

Source: Author's construction using Grandinetti (2003) and Unioncamere (2016) data.

Innovation trends that pushed designs and models towards lacquered or laminated furniture and panels and parts and components made with materials other than wood also hit the district and its wooden chair manufacturers, particularly the smaller subcontracting companies. Moreover, the increasing number of products on the furniture market made in a standardized way without using specific manual processes progressively replaced traditional production processes and the traditional skills involved in them, as well as more traditional styles of furniture.

The Great Recession of 2009 hit the districts of the home furnishing industry harder than other Italian districts with a different specialization; the Manzano chair district was one of the hardest hit. Besides the previously mentioned factors (the entry of new competitors and unfavourable exchange rate) that were at the root of the troubles of the district since

the beginning of the century, others came into play. The recession caused a slump in real estate markets everywhere, thus the market for producers of house fittings was essentially frozen for a few years. Another factor specific to the Manzano district was the inability of many firms, particularly the smaller ones, to introduce specific innovations in production processes and in products that would have made it possible to differentiate their products from those of the rising competition. Again, the firms most affected were small artisanal ones (those with up to ten employees, classified as micro-enterprises) that by not making a finished product but only components were the captive suppliers of the larger firms in the district. These firms (making up about two-thirds of the firms in the district) had almost no contractual power and were decimated by the combined pressure of shifting market preferences, increasingly difficulty in accessing credit, and growing recourse to the delocalized supply of their larger customers.

For the Manzano district, the impact of the competition of low-cost producers that appeared in the first years of the twenty-first century was not simply a cyclical factor but a structural feature of the competitive context that exposed structural weaknesses in the district. As a consequence, the crisis was not of provisional duration as it was in other Italian districts. The downwards trend in employment, exports, and the number and profitability of local firms remained constant from the beginning of this period and continued for fifteen years (see Tables 13 and 14). By 2010, the former were back at the levels of the late 1980s and continuing to decrease.

**Table 14:** Local units and employees in the Chair District of Manzano (2010–2016)

<b>Year</b>	<b>2010</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>
<b>local units</b>	734	643	635	644
<b>employees</b>	7,299	4,500	4,400	n.a.

Source: Author's construction using Passon et al. (2016).

The outcome of this movement was that some of the factors in the success of the chair district almost disappeared. Recourse to outside suppliers or the area's own delocalized production facilities tore apart the fine mesh of interrelationships among the district firms. The degree of personal acquaintance between business owners diminished, and with it their ties of kinship or friendship; because of the fall in number of operational units and employment, the chair industry (and therefore the district) ceased to be the point of reference in terms of job opportunities for the local population. Moreover, because of the Delocalization, the long-lasting relationships between business owners and their employees became frayed; this relationship had allowed the former to ask for additional effort from the latter (such as working on weekends to complete urgent orders) and gave the district firms an additional competitive advantage.

### 6.3 Survival of the Manzano District

In these years, the district clearly evolved in the direction of a dichotomous model. A few (larger) leading firms, through their propensity to innovate, managed to influence the network of smaller firms that by changing and innovating remained linked to them, and continued to be competitive on world markets, while a large number of smaller firms, unable to adapt, remained inescapably behind and struggled – and often failed – to survive.

One of the decisive factors in the survival of firms was their export orientation. Firms focused on innovation with an export orientation also achieved positive results in these years. Particularly after the recession of 2009, firms that focused on the national market suffered heavily, be they subcontractors or final product assemblers or producers. Indeed, the small companies that best weathered the storm were also the ones which were strongly export oriented or which had managed to join the networks of bigger ones (also export oriented).

The efforts of those firms indicated the direction of survival of the district: innovation, partial replacement of wood as the raw material for furniture, product differentiation, and expansion of the product range beyond chairs. The district structure, with its strong interaction between institutional actors and firms, also helped survival. Regional and local authorities launched initiatives aimed at regrouping the firms of the district and supporting them through coordinated efforts. The establishment of the consortium *Cluster Arredo e Sistema Casa*<sup>42</sup> in the region Friuli-Venezia Giulia and its branch that operates in the chair district (the Italian Chair District) helped to modernize district firms and maintain their presence on international markets. The exports of the chair district started recovering in 2015 and since then have modestly but continuously trended upwards (see Table 15).

**Table 15:** Rate of growth of exports of the chair district

Year	2013	2014	2015	2016	2017
Exports	-3.1	+1.3	+1.1	+1.2	+2.9

Source: ICD (2019) data.

The recovery of exports also led to an inversion in the downward trend in the number of firms and employees that in 2016 grew at the same pace as exports. It is too early to say whether these are signs of a definitive revival of the district; however, the fall appears to have stopped and the capacity for penetration into foreign markets of the surviving firms appears to be good and increasing.

## 7 Conclusions

The first two decades of the twenty-first century saw great changes in world economies and in the relative economic comparative weights of many countries. Although the countries that had the largest economies are still in great part the same, the new entrants to this group have caused significant disruption in many industries and affected the economic conditions of many countries. Italy, too, was affected by this evolution, somehow more than other countries (Italian GDP growth in this period was the lowest among the largest economies). Even though Italy remains one of the biggest exporters in the world (ninth in 2017), and has had – since 2011 – the second largest trade balance surplus among the G7 and the third among EU countries, it has felt the severe effects of the double disruptions of this century (first, the bursting of China onto world markets, and then the Great Recession of 2009). Given that the Italian industrial structure is based on the Area Sistema industrial districts, it is inevitable that the districts fully felt the brunt of this disruption. Some districts managed to weather this deluge in a relatively short time (within a couple of years after Chinese accession to the WTO, five years after the recession), while others have barely survived (being in decline since the first years of this century). An example of the former is the tannery district of Arzignano, and of the latter the chair district of Manzano.

The factors that determined the different performance of these two districts are varied. They typify the reasons for the ability of the district model to resist and react to the disruption. The most important one is the reactivity of the business-people of the area. Only if the districts' firms are able to adapt and possibly to anticipate changes in the competitive environment can they keep abreast of the changes and remain vital. Product innovation that follows if not instigates the changing trends in the market is essential. Too many firms (particularly small ones) in the Manzano district remained anchored to making wooden chairs of a traditional design and average quality, and were crushed by producers who could sell the same products at a much lower price. Only quite late in the day was a strategy of product innovation and the use of different materials pursued by some of the firms.

In the Arzignano district, in contrast, most firms kept making leather but managed to maintain and improve the high quality for which they were already well known. For this, they also had to improve their production processes. Process innovation can not only reduce cost, but, more importantly, may allow the exploitation of new technology, fostering the making of things in new ways, and improving quality and reducing waste. This was certainly the winning card played by the Arzignano district. The introduction of new tanning processes and new machinery allowed the district firms to exploit the shift in consumer demand for more environmentally friendly products, helping them become the leaders in "green" innovation in the industry.

The process of "greening" leather production and the whole district was significantly helped by the facilitating support, and sometimes the more direct role, of public

institutions, and in particular of local municipalities. In the Arzignano district institutions had learnt to play a facilitating role in the development of the Area Sistema since the 1980s and this expertise played an important part in the relatively rapid recovery of the district. The Manzano district saw the less proactive role of local institutions, which became significant only after the crisis had almost destroyed the area.

Finally, the social structure of the districts endured a severe battering, because, besides the usual problems faced in previous downturns (closures of businesses, unemployment, and reduced spending power affecting all facets of the local economy), the structural shift caused by the delocalization policies of many of the larger firms sapped the trust between district stakeholders. This development might have caused the demise of the districts as they are normally portrayed (and in Manzano this came close to happening). However, the nature of the districts and the combined efforts of all stakeholders led to success in working out a response to this existential crisis. Smaller companies (the surviving ones) learnt new methods of production and management that allowed them either to access directly final users or to play a supporting role for the larger firms through their capacity for innovation. Larger companies realized that the process of internationalizing their supply network was giving diminishing returns and undermining one of the most important sources of their strength; they thus paid more attention to maintaining a local supply base, thereby helping smaller companies come through the crisis.

Institutions played an important role by stimulating and supporting innovation in firms, by establishing or strengthening training programs and specialized schools, and by supporting joint efforts to develop district-wide infrastructure. This concerted effort managed to restore trust among stakeholders, at least to the level where it was once again a significant factor in the socio-economic environment of the district.

This path to recovery is common to the two districts. However, in Arzignano this process started earlier, in an environment where some aspects of success were already integrated. This allowed the district to get through the first disruptive wave of low-cost competition and recover their leading worldwide role in industry before being hit by the second and more disruptive wave of the Great Recession combined with the explosive growth of Chinese exports. This second crisis was deeper and more destructive than the first one, but the district was in a good situation and many of the instruments and attitudes necessary for overcoming the challenges were already in place.

As a consequence, the district managed to recover after five long years of troubles and reassert its leading role, returning to an expansion of production, exports, and profits in the five years afterwards. In Manzano, initial conditions were not as good and the process started much later. The district was hit much more forcefully by the first wave and had not recovered before being hit by the second one. The disruption in this district was much more severe; the response only came later and in a more damaged socioeconomic environment. The revival of the district started after 13 years of steeper decline, and it is

still tentative. That it is reviving at all is testament to the inherent strength of the district model and its resilience as a socioeconomic unit.

#### Notes:

<sup>i</sup> The term "industrial district" was defined first by the economist Alfred Marshall (1842–1924). Marshallian industrial districts show a high degree of vertical and horizontal specialisation. Firms are geographically clustered, tend to be small, specialised and competitive, and rely on market mechanisms for exchange. The communities where skilled labour is based are close-by, making it relatively easy to recruit staff for firms, while technical knowledge is easy to disseminate and enables a decrease in transaction costs.

<sup>1</sup> The proportion of employment attributable to industry among those countries is Italy 28.3%, Japan 26.2%, Germany 24.2%, USA 20.3%, France 20%, UK 15.2% (CIA 2018).

<sup>2</sup> The proportion of GDP attributable to industry among the same countries is: Germany 30.1%, Japan 26.2%, Italy 24%, France 20.1%, USA 19% and UK 19% (CIA 2018).

<sup>3</sup> These are the sectors that propel Italian products in international markets and where excellence linked to Italian mastery in crafts makes for a strong and successful competitive position. The "four As" come from the Italian words for the related sectors: *Alimentari-vini* (food and wines), *Abbigliamento-moda* (clothing and fashion – including textiles), *Arredo-casa* (home furnishings) and *Automazione-meccanica* (automation and mechanical engineering).

<sup>4</sup> We call it an *Italianate* industrial district to indicate that it has become an archetype in itself and may become a model reproduced in other countries. Use of the term *Italianate* for such Italian districts is found in an old paper from Alberti (2018).

<sup>5</sup> The concept of the Marshallian industrial district did not imply that local actors needed to consciously cooperate to ensure the existence and successful operation of the district. In the *Italianate* district conscious cooperation among actors is widespread, and indeed is one of its characteristics.

<sup>6</sup> Besides Becattini (1990), who was the first to identify these elements, I refer to Gandolfi and Cozzi (1988) and to Tripodi (2000).

<sup>7</sup> As may be remembered, in 2001 ISTAT identified 181 manufacturing industrial districts, while in 2011 it found 141 of them – some of them new.

<sup>8</sup> The term "cluster" denotes a similar, but not identical phenomenon. The classification of clusters is based on similar, but not identical concepts. See Enright (2003) where *working*, *latent*, *potential*, *policy driven* and *wishful thinking* clusters are mentioned.

<sup>9</sup> "*In fieri*" (Latin): Being in the course of accomplishment, in the process of execution; a thing commenced but not completed.

<sup>10</sup> Sobriquet: nickname.

<sup>11</sup> In those years, 12.4% of the world exports of shoes came from Italy, as well as 20% of leather and 49% of global exports of ceramic tiles. However, this world leadership was not limited to such "traditional" industries. For example, 11.2% of world exports of machinery for agriculture and forestry and 12% of industrial machinery also came from Italy.

<sup>12</sup> This was a way to compensate for the loss of international competitiveness due to differences in inflation from Italy's main international competitors (primarily Germany) and the other inefficiencies of the "country-system" of Italy, which regularly put Italian firms at a disadvantage.

<sup>13</sup> It should not be forgotten that, at least in part, the devastating competitiveness of low-cost competitors (in particular, of Chinese companies) was facilitated by the frequent practice of engaging in unfair methods. The appropriation of intellectual property (sometimes by simply copying, or reverse-engineering a product) and below-cost pricing (either straightforward dumping,

or due to state financial support for exports) were – and still are – quite common. Another common and damaging practice is counterfeiting, which causes serious losses due to impacts on sales, leading to loss of market share, and often to lower quality products and thus a decrease in brand image.

<sup>14</sup> Innervate: to supply with nerves, to pervade.

<sup>15</sup> However, the fact should not be overlooked that for a proportion of the delocalising firms the reason for doing so was to exploit the possibilities offered by markets growing at a much faster pace than the national one.

<sup>16</sup> The growth rate of Italian GDP (in real US Dollar terms) in comparison with other main European countries was:

Country	00	01	02	03	04	05
Italy	3.71	1.77	0.25	0.15	1.58	0.95
France	3.88	1.95	1.12	0.82	2.79	1.61
Germany	2.96	1.70	0.00	-0.71	1.17	0.71
UK	3.66	2.54	2.46	3.33	2.36	3.10
Spain	5.29	4.00	2.88	3.19	3.17	3.72

Therefore, in these six years Italy’s economy performed worse than that of the other big European countries, except for Germany.

<sup>17</sup> Filière: network, industrial network.

<sup>18</sup> OPT (Outward Processing Traffic) is a form of delocalization that affects only part of the production process and results in a dual flow of goods: first of basic materials or components from the de-localizing firm to the processing one, then of the processed components back to the first firm. According to an OECD definition, the temporary export of goods for outward processing is a customs procedure under which goods that are in free circulation in a customs territory may be temporarily exported for manufacturing, processing or repair abroad and then reimported with total or partial exemption from import duties and taxes.

<sup>19</sup> After all, China is certainly the country that has the greatest potential, and therefore represents the greatest menace in both the traditional and new export markets of the districts.

<sup>20</sup> Altogether, Italy was in recession for 60 months, including six months in the second half of 2007, and 15 months from Q2 of 2008 to Q2 of 2009. After two years’ recovery, Italy fell back into recession again in Q3 of 2011 and remained in this state for 27 continuous months until Q3 of 2013. Finally, it returned to recession for the whole of 2014 (Eurostat 2018).

<sup>21</sup> Italian law defines industrial districts as “local territorial areas characterized by high concentration of small businesses, with particular reference to the relationship between the presence of companies and the resident population and the productive specialization of all companies” (Art. 36, Law 317/1991). The two main criteria for identifying an industrial district are thus: a) high concentration in the area of industrial firms, with a prevalence of small and medium-sized ones; and b) productive specialisation of the business system.

<sup>22</sup> However, for the majority of district firms (53%), the main suppliers are still located in the same province or region. This suggests that proximity, albeit not narrowly restricted to within the few towns of the district, certainly helps with the formation of solid and effective networks (Unioncamere 2016).

<sup>23</sup> The *Country of Origin Effect* (COE) manifests itself in two ways. When consumers are not familiar with a product and cannot tell its actual quality, they refer to the image they have of the country of origin (or the country they associate with the product) to infer its quality. This is the *halo effect*, which directly influences consumers’ beliefs about product attributes and indirectly

affects the overall evaluation of that product through initial beliefs. When consumers are familiar with certain products from a given country, they abstract from this knowledge an evaluation of the quality of other not known products from the same country. This is the *summary effect*. Thereby the country image consumers have constructed through their appreciation of different products directly affects their attitudes towards unknown brands or products from the same country. See: Han (1989).

<sup>24</sup> Although increasingly used, equity and non-equity agreements, as well as foreign direct investment, are still the domain of a very small number of firms (Mariotti and Mutinelli 2017).

<sup>25</sup> Lymph is a fluid that circulates throughout the lymphatic system of the human body. In this context “circulating vital lymph” means maintaining the efficiency of economic operations.

<sup>26</sup> Until the year 1997 Italy was the biggest producer of leather in the world (with 2,020 million square feet), ahead of China (1,969 Mft<sup>2</sup>), South Korea (1,235 Mft<sup>2</sup>) and India (1,036 Mft<sup>2</sup>). China overtook Italy the following year, but Italy remained the second largest producer (in 2006, China was by far the biggest producer in terms of quantity, with 4,000 million square feet, followed by Italy, 2,039 Mft<sup>2</sup>; Brazil, 1,655 Mft<sup>2</sup>; Russia, 1,410 Mft<sup>2</sup>; India, 1,119 Mft<sup>2</sup>; and South Korea, 1,090 Mft<sup>2</sup>). Source: Banca Intesa (2006).

<sup>27</sup> However, this was 34% of the total value of exports of finished hides and 22% of the total exports of the industry (including raw hides and semi-finished products) Source: Banca Intesa (2006).

<sup>28</sup> The wool industry remained a mainstay of the industrialisation of the province of Vicenza. In particular, in the next valley to the east of the Chiampo, the Valle dell’Agno is still located one of the largest Italian textile groups, the Marzotto Group, established in 1836 as Lanificio Luigi Marzotto e Figli.

<sup>29</sup> The first tanning machines arrived in Arzignano in the 1950s, and were of German manufacture, in which country a well-established specialized industry had existed for a long time. Subsequently, the first producers of machines and drums for tanning began to appear in the area. By the 1980s a local industry was well established and started developing specialised know-how.

<sup>30</sup> For example, the value of exports to the USA grew more than 13 times, from € 18M to € 243M, at an average rate of 136% per year; those to China grew 29 times, admittedly from a low base, from € 0.4M to € 11.6M, at an average yearly rate of 311%.

<sup>31</sup> The *Guardia di Finanza* (Financial Police) identified a number of business people, including some of the owners of some of the biggest groups in the district, who had evaded taxes in amounts greater than € 100 million.

<sup>32</sup> However, this might spell trouble in the future to the Italian downstream industries as their Chinese competitors are improving the quality of their production.

<sup>33</sup> Among the best practices in this field implemented in the Arzignano district, it is worth mentioning the establishment, through collaboration of firms and the local administration, of a company that recovers the solid waste from the production process and transforms it into fertilisers and other products for agriculture, and the start of the Arzignano Green Land programme that fosters the efforts of the districts to promote a circular economy, and to publicise the latter.

<sup>34</sup> The five most important districts in the furniture industry, in order of turnover, are: the wood and furniture district of Brianza (Lombardy), the furniture district of Livenza e Quartier del Piave (Friuli-Venezia Giulia and Veneto), the kitchen district of Pesaro (Marche), the chair district of Manzano (Friuli-Venezia Giulia, and the upholstered furniture district of Murgia (Apulia and Basilicata).

<sup>35</sup> Ministero dello Sviluppo Economico. 2018. *Statistiche relative all’interscambio commerciale italiano nel settore dei mobili*. Available at: [https://www.mise.gov.it/images/stories/commercio\\_internazionale/osservatorio\\_commercio\\_internazionale/interscambio\\_settoriale/mobili\\_19\\_01\\_2018.pdf](https://www.mise.gov.it/images/stories/commercio_internazionale/osservatorio_commercio_internazionale/interscambio_settoriale/mobili_19_01_2018.pdf) (15 March, 2019).



<sup>36</sup> In a few years, the US\$-€ exchange rate went from 0.82 to 1.20, representing an increase of more than 46% in the value of the euro. This sapped the competitiveness of exports from all the countries in the Eurozone.

<sup>37</sup> Peaking at 35.7% in 2015, not shown in the Table 8.

<sup>38</sup> The municipalities of Manzano, Corno di Rosazzo and San Giovanni al Natisone.

<sup>39</sup> The earthquake hit Friuli, with its epicentre north-west of the district. It caused 990 deaths, and 45 municipalities were declared "disaster areas," meaning that very few buildings were left standing. Although the district was only partially affected, 1,057 residential buildings had to be rebuilt or significantly repaired (meaning that until repaired they were not safe to live in). Industrial activities were similarly affected, particularly those small firms which had their workshops on the ground floors of houses or in attached buildings.

<sup>40</sup> The share of international exports of Italy as given in Tables 10 and 12 is different from those provided in Table 11 because the sources used different classifications for the products. ATECO CM31092 goes into finer detail than SH4. Moreover, SH4 includes types of furniture whose sales rebounded faster than those of chairs. This explains why the market share of Italy differs so markedly in the two sets of data after the year 2008.

<sup>41</sup> Based on the annual average.

<sup>42</sup> The consortium offers tailored services to companies in the furniture sector. Its other task is to propose and implement strategies for the development of the entire furniture and home system sector.

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## History of Success: Regensburg – A Local Growth Miracle

NICOLE LITZEL & CHRISTOPH RUST

**Abstract** Regensburg, the fourth largest city in Bavaria, and its surrounding areas were until the early 1980s considered to be among the crisis regions of Germany. In the past 30 years, however, the region has experienced deep structural transformation and is nowadays ranked as one of Bavaria's economic hot-spots. Several decisions can be seen as catalysts for this still ongoing dynamic development. Probably the most important one – apart from the establishment of a BMW production plant – was the opening of the University of Regensburg in 1967, which had and still has a strong impact on the skill structure of the local labour force. The city also implemented a regional cluster policy that connected economic activities with the new opportunities arising from the young higher education institute. In this paper we take a closer look at where all the graduates of the University of Regensburg have gone since 1995 by drawing on a unique data source in which data about individual graduates is linked to German social security data. Through this we are able to evaluate to what extent graduates stay in the region after finishing their studies. We find a significant “adhesive effect” both for students originating in the region and students from outside the region. We therefore conclude that the university plays a key role in the dynamic economic development of the region.

**Keywords:** • economic development • regional cluster policy • business  
• universities • mobility patterns

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## 1 Introduction

The University of Regensburg in Bavaria was founded in 1962 and opened in 1967 as a regional university. Since then, Regensburg and the surrounding areas have experienced deep structural transformation. Until the 1980s, the location was considered to be among Germany's crisis regions. Now, by contrast, Regensburg is ranked as one of Bavaria's economic hot-spots. In contrast to the national trend, manufacturing jobs constitute a considerable share of employment. Several high-tech firms are located in the region along with important manufacturing firms, among which there are several so-called "hidden champions". Together with this astonishing economic development, a change in cultural life can also be observed. Cultural offerings now range from high-quality cinemas, music and film festivals to theatre and poetry. The atmosphere has changed from that of a provincial town to one of openness, diversity and creativity. Due to the variety of local amenities, the quality of life in the location has improved enormously.

Economic success has manifested in a low unemployment rate in the region (2.2% in May 2017), along with an increase in employment, wages and housing prices. The city of Regensburg in particular has a growing population and is strongly attracting young people. Due to these developments, Regensburg is one of the regions with the lowest average population age in Germany. In this paper, we shed some light on the factors that are, we believe, primarily accountable for driving this development.

It turns out that a fortunate combination of investments from various high-tech companies, successful regional economic policy, and – possibly the most important factor – the foundation of the University of Regensburg have driven this exceptional development.

This paper is structured as follows: The next section describes important milestones in the economic development that has occurred since the 1980s. In section three we analyse the mobility patterns of graduates from the University of Regensburg which have different core implications for regional economic development. Section four concludes.

## 2 Regensburg, the case study

### 2.1 Economic history and milestones

Until the 1980s, Regensburg was often referred to as a "sleepy administrative city". The location was then marked by a declining population,<sup>1</sup> having one of the lowest birth rates and tax incomes in Germany, along with a declining textile and clothing industry. Unemployment rose above twelve percent at the time. In comparison, since 2010 the former has been continuously and clearly below four percent in the city and the surrounding area, while in spring 2018 it was as low as 2.2% (German Federal Employment Agency).<sup>2</sup>

One strong boost to the economic development of the city came from the foundation of the University of Regensburg, which started operating in 1967. Additionally, the opening of the University of Applied Sciences Regensburg (today the Eastern Bavarian Technical University Regensburg, OTH<sup>3</sup>) followed in 1971. It typically takes a few years for the impact of a university to unfold in a region (Goldstein and Drucker 2006; Warnecke 2016). The staff of lecturers and administration must be built up, faculties gradually take up their activities, economic actors recognize and increasingly make use of the opportunities offered by joint research projects, and the first students graduate after several years and look for their first jobs.

In Regensburg, these effects merged with a second development: industry discovered the potential of the location, stimulated by the active economic policy of the city. An analysis in the 1970s indicated the lack of space for development, so a new structural policy with new targets was conceived. As a first step, a political process of annexation was implemented. This made the city area 1.5 times larger, creating new space for business and increasing flexibility in terms of efforts to attract investment. The active economic development policy led to the establishment of a BMW car plant in 1983,<sup>4</sup> which also attracted suppliers and encouraged long-established companies to expand. Further corporate decisions that led to a significant improvement in the image of Regensburg were the expansion of a preexisting Siemens location into a mega-chip plant<sup>5</sup> in 1984, the establishment of Toshiba's first European notebook production facility in 1989,<sup>6</sup> and the company-internal creation of Siemens Automobiltechnik<sup>7</sup> in the same year (Damingier and Litzel 2017).

## 2.2 External shocks

In the same decade, the international trend in business to slice up value-added chains (Krugman 1995) gained momentum. Moreover, in 1989 the Iron Curtain fell and the ensuing path towards EU-enlargement in 2004 turned formerly peripheral regions into centrally located economic spaces. For Regensburg, located close to the border to former Czechoslovakia, the combination of these two external shocks brought drastic changes. The integration of markets, fueled by the opening of the former Eastern Bloc, created new opportunities for firms, especially in the border regions. On the supply side, new sourcing partners made efficiency gains possible, while on the demand side the new markets brought new customers and the opportunity to shift production to a nearby neighbouring country with much lower labour costs ("in the mid-1990s wages were at current exchange rates more than eight times higher in the eastern Bavarian border region than in the Czech Republic"; Moritz 2011, 42). These factors made corporations as well as small and medium-sized firms think about relocating business activities there. Companies were forced to keep up the pace by making efficiency gains just to stay in business, and also reorganized their internal processes accordingly.

The increasing disintegration of the production process combined with outsourcing and offshoring required more coordination between business partners. Both forward and

backward linkages and informal co-operation gained in importance, partly because more complex parts of the value-added chain were gradually outsourced and business partners became integrated into the innovation process. Hence, co-operation and interaction between partners had to become more intense, a situation made easier due to geographic proximity.

Relocating businesses are attracted by locations that offer favourable regional conditions, which are often found not in places with cheap production factors, but in locations with a supply of the relevant skilled labour, opportunities for co-operation, local suppliers and customers, as well as research and higher education institutions – in other words, in locations with clusters (see Litzel and Möller (2011) for an overview). These are defined “...as significant geographic concentrations of major end-market industries, their extended supply chains, other sectors that share close technological or human capital affinities, and various specialized supporting institutions” (Feser and Sweeney 2002, 111). It is now at the regional rather than the national level that competition for economic activities and skilled labour has emerged between economic spaces. It can be observed “that even as competition and economic activity globalize, ... competitive advantage can be localized” (Enright 2003, 100). Porter (1990) calls this the “location paradox”. Cluster policy was an important economic and science policy instrument at the beginning of the 1990s – as it still is today in an advanced form.

### **2.3 Cluster policy in Regensburg**

For a location like Regensburg to compete with other economic spaces and find its own distinctive position, the policy of promoting regional clusters offered an opportunity to make its existing economic strengths, advantages and distinctive features more visible, and to increase innovation by establishing business contacts that would not have come about without such an external initiative.

Building on the leading industries in the region and, above all, on the competencies of the University of Regensburg and the Regensburg University of Applied Sciences, the city administration began to support networking between science and business in the mid-1990s. The first cluster – biotechnology – represents an example of the path taken by the municipal economic development department: at that time, the German government put the BioRegio initiative<sup>8</sup> out to tender. Regensburg was already a renowned location due to the University Hospital, which went into operation in 1992, and due to the life-sciences-related research and educational activities at the University of Regensburg. Young, ambitious scientists produced high-calibre research achievements there. The Regensburg University of Applied Sciences, with an orientation towards applied research, also offered important opportunities for making connections, for example in the field of medical technology. The initiative involved organizations from science, industry and administration with highly qualified personnel who recognized the opportunity for commercializing biotechnology and developed the ambition to take part in the BioRegio competition – not least because of the funding opportunities. And not without success: in



Regensburg development was initiated that is now unparalleled anywhere in Germany. In addition, the establishment of a biotechnology-oriented start-up scene provided a boost to innovation for the entire region. In 1997, 13 biotech companies were already active in Regensburg. In 1999, the city of Regensburg founded BioPark Regensburg GmbH as a municipal subsidiary in order to provide a stable organizational structure for coordination-related tasks. On campus, the Hans Vielberth University Foundation erected a multifunctional building and developed it into the first BioPark. Since 2005, the number of employees in the participating organizations has increased by 50%. Today, 33 companies work in three buildings with high-quality laboratory and office space, whose approximately 550 employees have direct access to university infrastructure due to their location on campus, such as the library, canteen, and seminar rooms – and, of course, to the know-how of scientists.

Spurred on by these noticeably positive effects, the city successfully participated in broader competition, this time in the field of information and communication technology. Together with the State of Bavaria, Hewlett-Packard and the city of Regensburg initiated the establishment of an IT start-up centre, in which support was offered to the related field. Today, the IT-cluster has developed into an IT-security and IT-logistics cluster now active throughout Bavaria and located in the municipal subsidiary R-Tech GmbH. Both clusters bring together small and medium-sized companies, large enterprises and various higher education institutions; they also initiate numerous research and development projects and advise and support spin-offs from universities and young companies. Similar initiatives exist in the fields of sensor technology, e-mobility, energy, and, since 2015, in the health industry and the cultural and creative industries.

The city will continue to follow the path it has already taken. Its “Vision 2030” is formulated accordingly: “Economy and science in Regensburg merge into a place of knowledge and innovation. The city is an attractive place for developers and an important centre for the production of high-quality goods” (Daminder and Lautenschläger 2018).

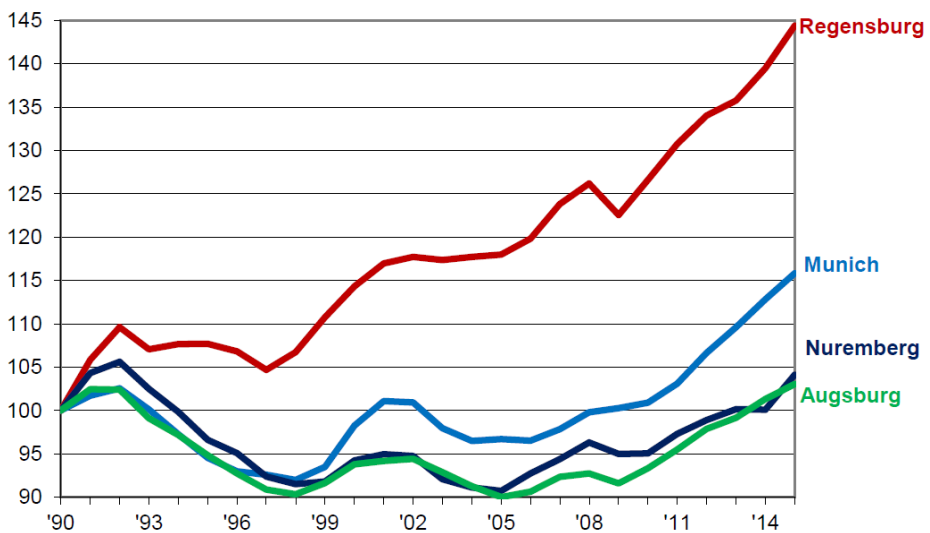
In this context, a major investment was made into establishing an industrial zone, the TechCampus, in the immediate vicinity of the University of Regensburg, the Eastern Bavarian Technical University Regensburg (OTH), and the University Hospital. The TechBase building opened on this campus in 2016, offering offices, workshop and research space to high-tech companies and development groups. Teaching, research, innovation and production take place on one campus. This is where business and science merge.

The city will continue to vigorously expand this model. Together with the university, for example, it is working to create non-university research institutions. Together with other partners it has launched a Digital Start-Up Initiative for the region and aims to establish STEM funding for children and young people in co-operation with the University of Regensburg, Eastern Bavarian Technical University Regensburg (OTH), the districts of Regensburg and Kelheim, and several companies, foundations, schools, chambers and

associations. It is also considered important to create good conditions for company start-ups and spin-offs from universities. Thus, numerous consulting offers for entrepreneurs exist to facilitate the startup of young companies.

The networking of companies from trade and industry as well as young and well-established companies of all sizes, universities and institutions creates a network that distinguishes the Regensburg economic area and makes it unique. Such a network is also a factor in why companies stay in the area and continue to grow.

**Figure 1:** Employment subject to social security



\* Graph: Stadt Regensburg, Amt für Stadtentwicklung, 09/2016.

Source: Statistics of the German Federal Employment Agency, German Federal Statistical Office (Bundesagentur für Arbeit, Statistische Ämter des Bundes und der Länder) (2019).

## 2.4 Development in figures

The dynamism of the business and science location has had an effect on the entire city and region. Regensburg is attractive for both living and working: At the end of 2016, just under 164,000 inhabitants were registered as living there; the population has thus increased in the last decade by almost 13%.<sup>9</sup> The labour market is extraordinarily well established: More than 148,000 people are employed,<sup>10</sup> the number having risen by almost 13% over the last ten years (in comparison: Bavaria +6%, Germany +2%) (City of Regensburg 2017, 135). The number of academic jobs doubled during this time (16% of all jobs).<sup>11</sup> If only employees liable to social security are taken into account, the number

of employees represents – at 780 per 1,000 inhabitants – the third highest employment density in Germany, after Wolfsburg and Erlangen (City of Regensburg 2017, 361). Figure 1 shows how dynamically the labour market has developed compared to other Bavarian cities since 1990. For example, while employment in Nuremberg and Augsburg after periods of heavy job losses increased by just under five percent, in Regensburg it increased by 45%. The unemployment rate in the city and district has been continuously below four percent since 2010, while in June 2017 it was 2.5%, reaching almost full employment. Regensburg is also a location for production. The share of the gross value added of the manufacturing industry (46.3%; Bavaria 34.3%) is comparatively high for a city of that size (City of Regensburg 2017). Regensburg continues to attract new companies engaged in production. Thus in 2015 and 2016 the economic development department of the city addressed about 120 cases of business settlement, of which about 90% originated in the region and had grown or wanted to get closer to the universities or other network partners.<sup>12</sup>

Trade tax revenues in 2015 of 226 million euros and income tax of 82 million euros reflect the good employment situation. In 2016, the lowest level of per capita debt since 1994 (less than 1,000 euros) was achieved (City of Regensburg 2017, chapter 15). Revenues (2016 to 2020) will be used for urban projects, in particular for (social) housing, infrastructure, education and childcare services; i.e., investing in the fields that are affected by population growth. The overall budget for the above-mentioned areas will be just under 900 million euros, the highest sum in the recent history of the city.

### **3 Impact of the University of Regensburg on regional development**

It is clear that the economic success of Regensburg cannot be explained by the establishment of manufacturing firms alone. The continuing path of growth – in our understanding – can only be explained by a related change in the city's cultural life. This cultural change is undoubtedly related to the foundation of the University of Regensburg, which had and still has a profound impact on Regensburg's overall appearance. The literature has identified various channels through which universities can influence their environment. They range, inter alia, from direct and indirect spending effects (e.g. Blume and Fromm 1999), knowledge production and the formation of human capital, to changes of regional milieu (see Goldstein *et al.* (1995) for an overview of possible channels). Such changes make a location attractive to the so-called creative class (Florida 2014), a term that refers to people who are active in the creation of new ideas (new technology, artwork, etc.) and who establish a breeding ground for innovation activities, which in turn facilitates local economic development.

With the opening of the University of Regensburg and the growing share of students in the local population (Regensburg in 2017 had roughly 160,000 inhabitants and around 33,000 students), many amenities have become locally available, making Regensburg an attractive place. Many bars, clubs and cafés nowadays strongly influence the overall appearance of the city. Moreover, the university hosts a variety of cultural events, such

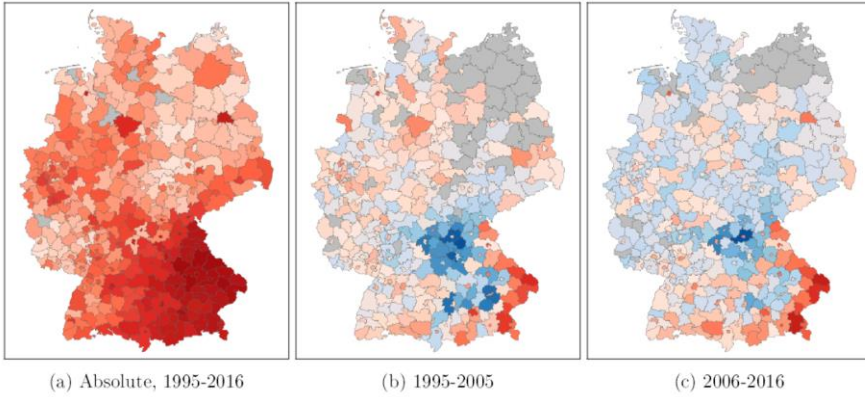
as concerts, theaters and exhibitions. Empirical evidence for the attractiveness of the city is given in Möller and Rust (2017), for example.

Finally, and probably most importantly, every year a significant number of graduates leave university and enter the labour market as part of the highly qualified labour force. These employees (or self-employed persons) create an essential basis for innovation and economic development. In terms of regional development it is therefore of significant relevance in which regions graduates start to work. Graduate mobility, therefore, has received increasing attention in the literature in recent years. The empirical part of this contribution is devoted to examining the choices of graduates from the University of Regensburg by drawing on a unique data source which allows us to address the mobility of graduates in a very detailed manner.

### 3.1 Data

This data source is based on process data made available by the University of Regensburg and contains information about all students who obtained degrees between 1995 and 2015. The information in this dataset encompasses, among other details, the field of study, university entrance certificate grade, date of graduation, final grade, and region of origin (see Figure 2). This data source has been linked to official register data from the German social security system (Integrated Employment Biographies, IEB), available at the Institute for Employment Research (IAB), and contains information (which is exact to the day) about individual employment status and type of occupation, region of workplace, wages, profession, sector and many more characteristics related to labour market topics; see for example Dorner *et al.* (2010) for a detailed description of the IEB.

The two data sources were combined based on a well-established linking procedure developed at the IAB (Sakshaug *et al.* 2017) while – due to the fact that both sources are based solely on register data – the final dataset includes very reliable information. The linked data set finally contained employment spells for more than 35,000 graduates. Note that as a consequence of the nature of the German social security system, several groups are not contained in the data: these include civil servants and self-employed persons.

**Figure 2:** Spatial distribution of graduates' origin

\* Left panel: absolute number of graduates per NUTS-3 region (darker red corresponds to higher number). Middle and right panel: deviations from predictions of a linear model on the NUTS-3 level including the predictors distance, population and time-fixed effects (blue scales correspond to negative values, red scales to positive deviations).

### 3.2 Empirical results

#### *Distribution of graduates' spatial origin*

Assuming that only a small number of graduates moved from one region to another prior to receiving their university entrance certificate (Abitur), one can take the region where the entrance certificate was acquired as a reasonable proxy for the graduates' region of origin. Looking at the spatial distribution of the region of origin for those students who went on to study at the University of Regensburg, one finds three strong predictors: (i) the population of the region of origin, (ii) (average) distance to the University of Regensburg, and (iii) a time effect, because the number of university students increases over time. To characterize the specific attractiveness of the University of Regensburg for the various regions of origin one can purge these effects from the raw data.

To this end, we estimate on NUTS-3 level data the following model:

$$\log(grad_{i,t}) = g(dist\_to\_rgb_i) + \beta_1 \log(pop_i) + \beta_2 bavaria_i + \phi_t + \varepsilon_{it}, \quad (1)$$

where  $grad_{i,t}$  is the number of graduates in year  $t$  who originate from region  $i$ , and the function  $g(\bullet)$  is a spline-based<sup>13</sup> nonlinear transformation of the distance of the region of origin to the University of Regensburg,  $dist\_to\_rgb_i$ . The parameter  $\beta_1$  accounts for the effect of the origin region's population,  $pop_i$ , and is the coefficient of a dummy variable indicating whether the region is located in Bavaria.  $\Phi_t$ , finally, are cohort-specific fixed effects. The residuals of the regression model can now be interpreted as an indicator of the attractiveness of the University of Regensburg in a specific region.

The spatial distribution of graduates' regions of origin is depicted in Figure 2; the left panel shows the absolute number (aggregated over the whole period) of graduates originating from each region, while the middle and right panel depict the aggregated residuals from model (1) for the periods 1995–2005 (middle panel) and 2006–2016 (right panel). In absolute terms, the University of Regensburg primarily receives its students from the surrounding regions, most predominantly from eastern and south-eastern Bavaria. After controlling for population, distance and time effects, at first glance the spatial distribution of the (purged) attractiveness seems to be characterized by a very similar pattern for both cohort groups. For the more distant regions, relatively more graduates originate from the eastern part of Lower Saxony and Saarland, while relatively few, by contrast, originate from the Ruhr area. The highest attractiveness of the University of Regensburg is found in regions in the eastern part of Bavaria, especially for those located within or close to the Bavarian Forest. Moreover, one can clearly identify regions within Bavaria in which the university is of comparably low attractiveness (for instance, Nuremberg, Würzburg, Bamberg, Augsburg, Munich and Landshut). All of these regions are university towns or at least located close to other full universities or universities of applied sciences. Hence, the lower attractiveness of the University of Regensburg is very likely due to intervening opportunities.<sup>14</sup>

This indicates that there are regional preferences that influence the location of study beyond the effect of sheer distance. The existence of a local university can mobilize this potential. Comparing the outcome of the attractiveness indicator for the two cohort groups, one can observe that regional concentration is less pronounced for the cohorts 2006–2016, reflecting greater attractiveness of the University of Regensburg for students throughout Bavaria in recent years.

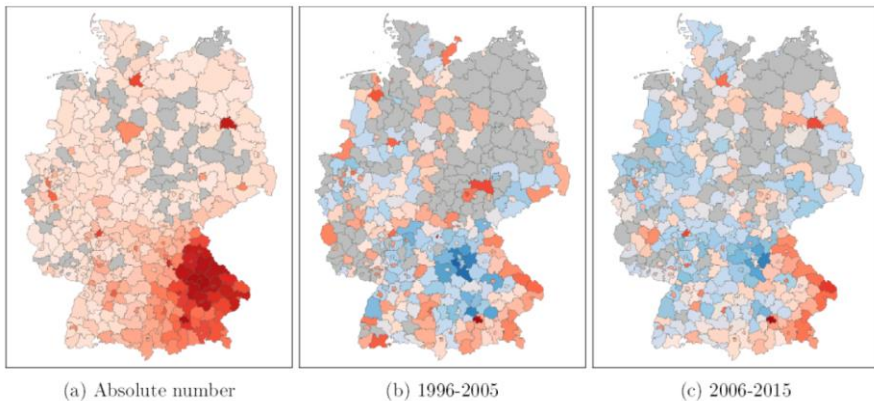
#### *The location (region) of graduates' first workplaces*

The same methodology was applied to the location of graduates' first workplaces after graduation as for the region of origin. In the selection of this first workplace we only considered regular employment spells, but imposed no restriction regarding the time between the first occurrence of such a spell and graduation. Note that for a minor share of graduates we cannot identify any regular employment spell. This could be for various reasons; for instance: (i) the graduate went abroad and thus is no longer visible in the German administrative employment register; (ii) the graduate worked as a civil servant or in a liberal profession (as a teacher, doctor, lawyer or consultant, for instance); or (iii) the person did not enter the labour market during our observation period, perhaps for family or other reasons (e.g., raising a child).

The regional distribution of the first workplace is illustrated in Figure 3. The left panel again shows the absolute number of graduates starting to work in the corresponding region and reveals that graduates of the University of Regensburg overwhelmingly tend to begin their labour market careers rather close to their place of study. The lion's share take up their first employment in the eastern and south-eastern part of Bavaria. Outside of Bavaria, a significant number of graduates can be found only within a few regions.

Unsurprisingly, when absolute numbers are considered these regions coincide with Germany's most populous cities (e.g., Berlin, Hamburg, Frankfurt, and Stuttgart). The fact that a relatively large number of graduates remain within the wider region around the city of Regensburg for work is in large part explained by the factors included in the linear model; in particular, by distance and the homeland effect. However, even after we control for the systematic factors included in the linear model, there remains an over-representation not only of the city of Regensburg but also some regions in Eastern Bavaria, in particular those along the eastern and south-eastern borders of Bavaria. Outside Bavaria it is visible that Berlin increasingly attracts relatively large numbers of graduates. In absolute terms, Munich is the most important location for the employment of graduates among all large German cities. By contrast, the greater Nuremberg area receives significantly fewer graduates than is suggested by the linear model; i.e., according to the conditional average given distance and population and the other factors contained in the linear model.

**Figure 3:** Spatial distribution of graduates' first workplace.



\* Left panel: absolute number of graduates working in the respective NUTS-3 region (darker red corresponds to higher number). Middle and right panel: deviations from predictions of a linear model on the NUTS-3 level including the predictors distance, population and time-fixed effects (blue scales correspond to negative values, red scales to positive deviations).

As pointed out earlier in this paper, it is of particular importance how many of the university's graduates remain in the region after graduation. Based on the linked data, we evaluated for a period of up to 10 years after graduation how many graduates were working within the wider Regensburg region (consisting of NUTS-3 regions within a circle with a radius of 100 km around Regensburg) and how many had left it for another area. The result is given in Figure 4, where on the left panel is illustrated the share for graduates coming from outside the region, and on the right for those who originate from the region.

The findings reveal that 50% of graduates from outside the region who found a job immediately after graduation stayed in the region. This can be termed the “adhesive effect” for incoming students. Due to the mobility of highly skilled workers, the adhesive effect declines over time. However, approximately 20% of the graduates from outside the region were in regular employment within the region even 10 years after graduation. Thus, a significant part of the adhesive effect is permanent. The adhesive effect for graduates originating from the region is considerably larger: 90% of graduates who found regular employment immediately after graduation remained in the region and after 10 years roughly two-thirds were still in the region. It is quite obvious that a larger part of this group would have permanently left the region if the university had not existed. The adhesive effect thus has the potential to mobilize highly skilled workers in the region, and is thus an important driver of regional development. Note that this effect is probably reinforced by those graduates who are not included in our data set, such as civil servants and the self-employed.

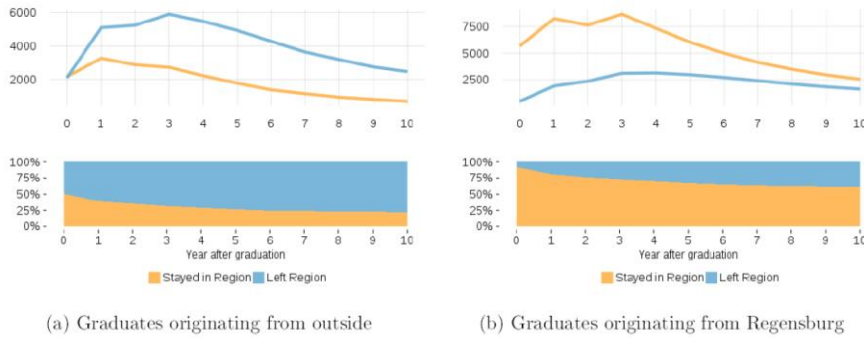
*Modeling mobility decisions: results of a discrete choice approach*

To be able to quantify in greater detail what covariates are associated with a higher probability of working in the region, we estimated both an ordered choice model and various binary choice models.

$$P(D_i = d_j | \mathbf{x}_i) = \Lambda(\mathbf{x}_i' \beta), \quad (2)$$

The empirical models are of the class where the dependent variable  $D_j$  is a discrete choice variable with values  $d_j, j = 1, \dots, J$ . Depending on the actual location of the individual's workplace,  $D_i$  has five different outcomes in the case of the ordinal model: (i) Germany, (ii) Bavaria, (iii) the wider region around Regensburg, (iv) the County of Regensburg, and (v) the City of Regensburg. In the case of the binary choice models, we used different aggregations of this ordinal variable. The first setup models the probability of working within the wider region around Regensburg (thus,  $D_i = 1$  if person  $i$  is working in the greater Regensburg area,  $D_i = 0$  otherwise), while the second specification investigates the decision to work in the city of Regensburg. Finally, the third specification's dependent variable is a dummy indicating whether the individual is working in the wider region, which in this case does not include Regensburg City. For the link function  $\Lambda$  we chose a logistic function. The covariates comprise educational characteristics (such as field of study, type of university degree obtained, and overall performance measured via final grades), the individual's gender and regional origin (proxied via workplace; see also previous section, making the same distinction as the ordinal dependent variable). Furthermore, we also include a discrete variable for firm size and dummies for the years after graduation to capture possible dynamics in the time domain. These models were estimated based on a specific selection of social security spells.<sup>15</sup> For each graduate we took a sequence of employment spells such that the first spell included the day one year after graduation, the second spell included the day two years after graduation, and so forth, covering at most a period of 10 years after graduation.



**Figure 4:** Absolute number and share of graduates taking up regular employment**Table 1:** Ordered Logit Estimate for Graduates Working in the Region

Dependent variable:	ordinal	binary		
	(1)	(2)	(3)	(4)
		wider region	city	region w.o. city
<i>Field of study (reference: Humanities)</i>				
Sports	-0.269	-0.585*	0.019	-1.070**
Law/Economics/Social Sciences	-0.269***	-0.280***	-0.332***	0.006
Mathematics/Natural Sciences	0.045	0.091	0.150**	-0.041
Medicine/Health	0.467***	0.502***	0.292***	0.424***
Informatics	-0.268***	-0.328***	-0.498***	0.078
Arts	0.036	-0.139	0.135	-0.416***
<i>Type of degree (reference: Bachelor)</i>				
Master	0.637***	0.521***	0.807***	-0.128
Diploma	0.644***	0.582***	0.664***	0.100*
Magister	0.797***	0.738***	0.979***	-0.05
Teaching Profession	0.813***	1.434***	0.246	1.270***
Medicine SE	0.238***	0.211***	0.490***	-0.258***
Pharmacy SE	0.117	-0.011	-0.757***	0.640***
Law SE	1.222***	1.304***	1.047***	0.590***
<i>Grades</i>				
final grade	0.044**	0.080***	-0.121***	0.211***
grade univ. entrance qualif.	0.165***	0.209***	0.141***	0.113***
<i>Firm size (reference: 1-50 empl.)</i>				
51-250 empl.	-0.296***	-0.355***	-0.440***	-0.021
251-1000 empl.	-0.380***	-0.427***	-0.434***	-0.118***
>1000 empl	0.072***	0.037	0.252***	-0.245***
log_dist	-0.303***	-0.343***	-0.016	-0.416***
female	0.048**	0.015	0.100***	-0.087***
Constant		2.601***	-1.645**	2.100***
Observations	37,386	37,386	37,386	37,386
Log Likelihood	-52,857.090	-22,059.700	-19,191.720	-18,551.150

*Additional variables not reported:* year after graduation, region of origin

*Note:*

\*p<0.1; \*\*p<0.05; \*\*\*p<0.01

The estimation results are given in Table 1, where the first column refers to the ordinal model and the remaining columns refer to the different binary outcome models: Column 2 distinguishes between working inside and outside of the wider region of Regensburg, and Column 3 distinguishes between working inside and outside the city of Regensburg. The choice to work in the greater Regensburg region but outside the city of Regensburg is incorporated in the model corresponding to Column 4. Thus, the model corresponding to Column 2 can be seen as a more aggregated version of the ordinal model, while the models in the latter two columns split the decision into two different choices. We decided to use these specifications because choices made in favour of the city of Regensburg seem to follow different patterns and should be analysed separately. In doing this, one can clearly identify specific drivers related to the location decision. By comparing different fields of study, for instance, we find that graduates in the fields of law, economics, social sciences and informatics tend to leave the Regensburg region, while medical graduates are more likely to stay in the region. Doctors (having completed a state examination (SE) in Medicine) mainly stay in the city of Regensburg, while pharmacists tend to work in more peripheral locations. Moreover, teachers and law graduates exhibit a higher propensity to stay in the Regensburg area. Comparing master's and bachelor's degrees, we observe that graduates with the former are particularly likely to remain in the city and the latter are slightly more liable to work in the wider region. Furthermore, women are more likely to stay in the city, as are those who have finished their studies with higher average grades. This indicates that Regensburg is considered an attractive place to work.

Finally, results related to firm size show that the probability of remaining in the region is higher if the individual is either working in a small- (up to 50 employee) or a very large firm (more than 1000 employees). The corresponding coefficients in Columns 4 and 5 reveal that working for a very large firm is associated with a higher probability of working in the city of Regensburg, while working for a small firm increases the probability of working in the wider region (not including the city). One can also conclude from these results that graduates who choose to work in the city of Regensburg are more often employed by very large firms, while those working in the wider region tend to be hired by very small firms; this implies, vice versa, that small firms particularly benefit from the increased availability of a highly skilled labour force.

#### 4 Conclusion

In this paper we have taken a closer look at the economic development of Regensburg, a city located in the German state of Bavaria, which has experienced exceptional development since the 1980s. The city and its surrounding areas until that time were considered to be among Germany's crisis regions. Nowadays, by contrast, the region is one of Bavaria's economic hot-spots. We believe that a combination of different events played a decisive role in this development. The large-scale investments of high-tech and manufacturing firms and an active regional economic policy that stimulated economic activity occurred at roughly the same time as an increasing number of highly skilled workers became available as a result of the opening of the University of Regensburg in

1967. Among other aspects, this led to lasting change in Regensburg's overall appearance as diverse amenities were created, making the city increasingly attractive, especially to highly skilled people. The combination of these different events and political measures can ultimately be seen as the basis for the impressive development of Regensburg into one of the most economically dynamic locations in Germany.

#### Notes:

<sup>1</sup> From 132,200 in 1979 to 127,800 in 1987 (in 2016: 164,000) (numbers rounded). Source: City Regensburg, statistics, information and numbers, total population, long-term time series with gender (Stadt Regensburg, Statistik, Informationen und Zahlen, Bevölkerungsstand Gesamtstadt, langfristige Zeitreihe mit Geschlecht) (2019).

<sup>2</sup> Source: Statistics of the German Federal Employment Agency, German Federal Statistical Office (Bundesagentur für Arbeit, Statistik, Statistik nach Regionen, RD Regensburg) (2019).

<sup>3</sup> *Ostbayerische Technische Hochschule Regensburg* (OTH); i.e., Regensburg University of Applied Sciences.

<sup>4</sup> Today nearly 10,000 employees.

<sup>5</sup> Today Infineon Technologies AG, approx. 2,500 employees.

<sup>6</sup> Production ended in 2007, today only a small service unit is left.

<sup>7</sup> Today Continental Automotive GmbH, with approx. 8,500 employees and headquarters for two of the five corporate divisions.

<sup>8</sup> The BioRegio initiative was a funding initiative of the Federal Ministry of Education and Research (BMBF) that operated from 1997 to 2005 to strengthen the use of biotechnology in Germany and improve the economic implementation of the results of biotechnology research.

<sup>9</sup> Source: City Regensburg, statistics, information and numbers, total population, long-term time series with gender (Stadt Regensburg, Statistik, Informationen und Zahlen, Bevölkerungsstand Gesamtstadt, langfristige Zeitreihe mit Geschlecht) (2019).

<sup>10</sup> Employees liable to social security, the self-employed, and civil servants.

<sup>11</sup> Source: Statistics of the German Federal Employment Agency, German Federal Statistical Office (Bundesagentur für Arbeit, Statistik) (2019).

<sup>12</sup> Source: City of Regensburg (2019), Department for Economic and Research Affairs.

<sup>13</sup> Splines are piecewise polynomials joined together to make a single smooth curve.

<sup>14</sup> Intervening opportunities: Opportunities offered by locations other than Regensburg. In migration theory, Stouffer's law of intervening opportunities states that "[t]he number of persons going a given distance is directly proportional to the number of opportunities at that distance and inversely proportional to the number of intervening opportunities" (Stouffer 1940, 846).

<sup>15</sup> Spell = time period.

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## Travel and Tourism: Impacts on Local Development

ZSUZSANNA E. HORVÁTH

**Abstract** Economies that rely on Travel and Tourism have an advantage over others in terms of the diversification of the economy and thus in the maintenance of resilience to external events and developments that can make national economies vulnerable. A diversified economy is less sensitive to fluctuations in any particular sector because risks are spread evenly across a number of industries. Travel and Tourism can also boost development in sectoral restructuring or transformation, in particular in dominantly rural and low-income countries and regions that previously relied heavily on agriculture and natural resource extraction. Other than the extended economic benefits and employment creation, Travel and Tourism development is capable of promoting cultural heritage and traditions. The chapter below will investigate and explore the reasons why and ways how tourism and travel development can impact local development. At the end of the chapter, a case study will offer parallels between the approach of two countries regarding heritage tourism as a specific driver of local development.

**Keywords:** • travel • tourism • planning • heritage • Hungary • Poland

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## 1 Travel and tourism in the global economy

*The significance of tourism in the global economy* is demonstrated by the fact that 2017 has been designated the International Year of Sustainable Tourism for Development by The United Nations. Travel and Tourism (TT) is one of the world's largest economic sectors, and by creating jobs and driving exports, generates prosperity at national, regional and local levels. According to the main authority in matters of tourism development and statistics, the World Travel & Tourism Council, in 2016 the sector yielded direct global GDP growth of 3.1% and generated six million net additional jobs. In terms of value, the contribution of TT to overall GDP amounted to US\$7.6 trillion (10.2% of global GDP) and provided 292 million jobs. This accounts for one in every ten jobs in the global economy (WTTC 2017). The sector accounted for 6.6% of total global exports and almost 30% of total global service exports, outpacing global economic growth (2.5%) for the sixth successive year (UNWTO 2007).

*Europe* is acknowledged as the world's number one tourist destination, measured by a record figure of more than 620 million tourist arrivals in 2016, just over half of the world's total (50%) (ETC 2016). The competitive advantage of Europe as a destination in relation to volatile political and socioeconomic variables and against the threat of other rapidly emerging destinations lies in the ease of travelling, supported by improved air connectivity, low-cost flights, technological progress in transportation, and the diversification of accommodation that gives rise to various forms of shared consumption. Demand for European destinations remains strong, fueled by intra-European tourism demand (ETC 2016).

The major public and private stakeholders in the field have come to the conclusion that the role and share of Tourism and Travel in Europe cannot be maintained and further developed without a unified policy, leading to the publishing of a *Tourism Manifesto for Growth and Jobs* (Tourism Manifesto 2017). The legal background supporting the Manifesto is Art. 195 of the TFEU<sup>1</sup> in the Treaty of Lisbon, bestowing on the European Union "the responsibility to promote the competitiveness of the European tourism sector by creating a favourable environment for its growth and development and by establishing an integrated approach to the travel and tourism sector" (Tourism Manifesto 2017, 1). The Manifesto refers to local development when it stipulates that "tourism often regenerates dilapidated areas and less developed regions, particularly rural ones".

The development of responsible, sustainable, and universally accessible tourism through the dissemination of the Global Code of Ethics for Tourism<sup>2</sup> has been the major target of the UNWTO (UNWTO 2007). While the scope of the activity of the organization is global, special focus is laid on emerging economies.

WTTC<sup>3</sup> (2017) research that assessed the role that TT plays in the global economy in comparison to other key sectors asserts that it has unique advantages in driving global economic growth, and catalysing global economic integration. In order to map the contribution of



tourism to national economies at the macro-economic level, direct, indirect, and also induced impacts can be monitored.

The *direct contribution* of TT to GDP reflects “internal” spending on TT as well as government “individual” spending – on services directly linked to visitors, such as cultural assets (e.g. museums) or recreational ones (e.g. national parks). Consistent with output, TT’s direct contribution to GDP (in other terms, Tourism GDP) is expressed in National Accounting and is collected from tourism-characteristic sectors such as hotels, airlines, airports, travel agents and leisure and recreation services that deal directly with tourists. The significance of TT in the overall economy is measured by its wider impacts (i.e. indirect and induced impacts).

*Indirect contributions* include the share of GDP and jobs that are created due to the following activities:

- TT investment spending – both current and future activity, such as the purchase of new aircraft and construction of new hotels;
- Government “collective” spending supportive of TT and benefiting the “community at large” – e.g. tourism marketing and promotion, aviation, administration, security services, resort area security services, resort area sanitation services, etc;
- Purchases of commodities and services by TT service providers – e.g. food and cleaning services by hotels, fuel and catering services by airlines, and IT services by travel agents;
- The “induced” contribution measures GDP and support for jobs derived from the spending of those who are directly or indirectly employed in TT (WTTC 2017, 2).

The *wider economic impacts* of TT are also substantial. Economies that rely more on TT have an advantage in terms of diversification and thus in the maintenance of resilience to external events and developments that can make national economies vulnerable. A diversified economy is less sensitive to fluctuations in any particular sector because risks are spread evenly across a number of industries. TT can also boost development in sectorial restructuring or transformation, in particular in dominantly rural and low-income countries and regions which previously relied heavily on agriculture and natural resource extraction. Other than the extended economic benefits and employment creation, TT development is capable of promoting cultural heritage and traditions. The wider economic impacts originating from TT are:

- Improved access to international markets and increased trading opportunities;
- Increased foreign investment;
- Investments in public and private infrastructure; and,
- Local economic development (WTTC 2012).

TT generates valuable spinoff benefits by developing infrastructure which creates externalities that other industries can use. It boosts trade, skills, and investments in other industries that are not directly related (WTTC 2017). As TT is essentially location-based,

requiring local production and development, it represents a major driving force in local development (in many of its ramifications), and in the creation or revival of cultural and historical heritage.

Oxford Economics<sup>4</sup> found that TT as an industry has a bigger multiplication effect on GDP than most other sectors, such as communications, financial services, education, agriculture, and mining (WTTC 2012). Industries can also be evaluated on the basis of how spending flows to households and to other parts of the economy. “The sectors most supportive of economic development tend to be those that generate the most household income and retain a higher share of expenditure within the local economy after accounting for imports. For every \$1 million in TT spending, \$701,000 in income is generated” (WTTC 2012, 5).

## 2 Sustainable tourism (ST)

UNWTO<sup>5</sup> has acknowledged the significance of sustainable tourism by announcing 2017 as the year of Sustainable Tourism Development. The concept of sustainable development as such was fully formulated at the Rio Conference of 1992, and its guiding principles were adopted at the UN Conference on Sustainable Development (Rio + 20) (UNWTO 2018b).<sup>6</sup>

The principles that can guarantee long-term sustainability pertaining to TT encompass the ecological, economic, and socio-cultural components of tourism development. Tourism development strategies must establish a careful balance between these three dimensions. According to UNEP<sup>7</sup>-UNWTO-relevant guidelines, sustainable tourism should:

- “Make optimal use of environmental resources that constitute a key element in tourism development, maintaining essential ecological processes and helping to conserve natural heritage and biodiversity.
- Respect the socio-cultural authenticity of host communities, conserve their built and living cultural heritage and traditional values, and contribute to inter-cultural understanding and tolerance.
- Ensure viable, long-term economic operations, providing socioeconomic benefits to all stakeholders that are fairly distributed, including stable employment and income-earning opportunities and social services to host communities, and contributing to poverty alleviation.
- ST development requires the informed participation of all relevant stakeholders, as well as strong political leadership to ensure wide participation and consensus building. Achieving sustainable tourism is a continuous process and it requires constant monitoring of impacts, introducing the necessary preventive and/or corrective measures whenever necessary.
- ST should also maintain a high level of tourist satisfaction and ensure a meaningful experience to the tourists, raising their awareness about sustainability issues and

promoting sustainable tourism practices amongst them” (UNEP and UNWTO 2005, 11).

### 3 The need for planning

Planning is essential for securing the viability of any development activity, regardless of its scope or scale. Owing to the multi-sectoral, complicated and fragmented character of TT, its development requires planning, and project development coordination is necessary. Planning creates the rational basis for development staging and project programming. Because of the specific nature of tourism, its development has a direct impact on a variety of stakeholders, including the ecosystem it is nested in. Governments around the world should consider TT as an integral part of their economic development strategy, as the policies which foster the development of TT generate a broad set of benefits that extend throughout the entire economy. The viability of tourism development can be secured by carefully matching tourist markets and products in the initial planning process. Integrated planning will enable the optimization of direct and indirect economic benefits, and eliminate or diminish various socio-cultural problems that are liable to occur.

*Tourism development strategic plans.* In harmony with broader strategic development objectives, detailed planning objectives encapsulate the rationale for the implementation of the planning phase before any ST development intervention (Walker and Walker 2010, 125). Such objectives can be summarized as below:

- “To determine the optimum level of tourism that can result in the achievement of environmental conservation objectives.
- To ensure that natural and cultural resources are indefinitely maintained in the process of development.
- To upgrade and revitalize existing outmoded or badly developed tourism areas and plan for new tourism areas in the future; and
- To satisfy the manpower skills and capability requirements of ST development”.

The success of the implementation of tourism development plans at a local level depends on a number of driving factors, the significance of which differ in magnitude. For example, stakeholders may all have very different agendas, driving them to follow a variety of paths, although ST is about finding a balance between conflicting interests (Maxim 2015). A proxy for the successful implementation of sustainable tourism policies and consistent strong economic returns is the collaboration of stakeholders, oriented and supervised by efficient destination marketing and management (TDM). UNWTO in its official policy documents advises national policy-makers to encourage private sector actors to take responsibility and work in partnership with local authorities in the framework of so-called Destination Management Organisations (DMOs) (UNWTO 2007).

The role of DMOs<sup>8</sup> is ever increasing as travel customers, in an era of post-modern tourism consumption, seek and respond to a diversified set of value clusters (i.e. combinations of experiences, products and prices that suit their individual preferences). Destinations must design, promote and coordinate a satisfying total visitor experience that maximizes the economic contribution to the destination, and one that stimulates return intention and referral behaviour (Horváth 2016). A truly competitive destination provides satisfying, memorable experiences in a profitable way, and contributes to the well-being of destination residents and preservation of ecosystems.

#### **4 Heritage tourism as a driver of local development**

In this section, the impact of ST development as exerted on local (socioeconomic and cultural) development will be discussed through the lens of a particular type of tourism: heritage tourism. Heritage tourism can incorporate tangible or intangible products, such as a castle hotel (tangible, and pertaining to historical/cultural heritage) or Easter customs and traditions (intangible, and pertaining to cultural heritage). Heritage-based tourism is a sector of tourism that, *par excellence*, represents sustainability: elements of history are preserved and revived in a modern setting. While historical heritage is nested in history, thus providing the framework and/or setting for it, heritage is a contemporary commodity purposefully created to satisfy contemporary consumption (Ashworth 1998). The creation of tourism attractions using existing assets – whether natural, cultural, or built – negates the need for the building of new facilities, allowing communities to “look to the past for a sustainable future” (Hargrove 2002, 10).

Heritage-related projects and activities (such as the restoration of historic buildings and provision of hotel services in them) impact local community development in a variety of ways: they lay the foundations of long-term orientation and stability, provide employment opportunities, create the need for ancillary goods and services to diversify the heritage site’s original offering, and for the further development or enhancement of local heritage-related activities (Horváth 2013). Depending on the planning considerations and the strategic decisions made in the process, heritage sites’ and projects’ local and regional impacts may be economic, social or ecological, both quantitative and qualitative, and hopefully positive. In some cases, however, owing to poor planning practices or the avoidance of following sustainability principles, the impacts may be detrimental and thus cause serious damage to ecosystems and communities.

First, direct, indirect and induced economic impacts are considered: local community revenue and number of jobs, public sector revenue, and real estate market implications must be taken into account. Developments will have multiplier effects when suppliers (generating indirect multiplier effects) and employees of heritage sites and tourist businesses (generating induced multiplier effects) are locally (regionally) recruited and embedded (Murzyn-Kupisz 2013). Heritage tourism initiatives will have culturally integrated effects, manifesting in local community-based enhancement of cultural

identity and sense of history and place. This will further enhance the revival of value-awareness and realization of commercial potential, benefiting crafts and small entrepreneurship regionally and locally. “For instance, if the local community does not have sufficient knowledge, skills or capital to launch heritage-related tourism businesses, it may benefit to some extent from jobs created in the hospitality sector, but the lion’s share of the profits will go to externally based owners of hospitality establishments. Similarly, tourist shops may be interested in selling locally made, unique souvenirs but unable to do so if they cannot find local producers willing to supply them, or if local craft traditions have been forgotten” (Murzyn-Kupisz 2013, 160).

Heritage tourism’s other externalities such as their contribution to the knowledge economy and the creative sector should also be taken into account. Moreover, built heritage often forms an integral part of local or regional regeneration strategies as a form of inspiration, or even their central component and catalyst. In terms of social dimensions, heritage tourism can directly induce an increase in the quality and standard of life, helping to fulfil local communities’ leisure, cultural and aesthetic needs. Local communities’ social capital can be fostered by the definition or reinforcement of local identity, a sense of pride and belonging, and inter- and intra-generational communication. A newly developed and consolidated image may attract more visitors, as well as offer the potential for new residential projects.

*Castle hotels* belong to the category of themed accommodation that are located in historic buildings and as such constitute one of the most in demand genres of tourist accommodation. These historic buildings once served a different function, were built by aristocratic families, and are nowadays renovated by private investors. Converted castles abound in Europe and have become a preferred form of accommodation for luxury tourists and even business travelers. This unique form of lodging is called the *parador* in Spain and *pousada* in Portugal and signifies a luxury hotel transformed from a formerly aristocratic edifice.

These buildings, due to the special status of the aristocracy, were a marker of social standing and the focal points of the arts during previous centuries – almost all branches of the arts: architecture, design, interior decoration, painting, furniture-making, sculpture, inlay, goldsmith’s work and textiles are represented therein. These residences give an insight into the social stratification of former noble families, their wide range of relationships, habits and lifestyles. Therefore, a castle can be an essence or a symbol of the national cultural heritage from the period in which it was built and decorated (Godsey 1999). Such buildings were also the centre of the period’s theatrical, musical, and scientific life. Moreover, castles became salons of literature, especially in the Reform Era (the latter part of the nineteenth century), when they served as the locales of reading nights.

Services offered by castles also make visits to the area more attractive to tourists who do not use them as hotels but stay in other accommodation. Most castles organize a range of

events that are open to the general public, such as balls, concerts, plays, exhibitions, antiques auctions and seasonal fairs, creating an additional, though rather elite cultural and leisure offering for both local residents and outsiders. Establishments that offer tourist accommodation in the area often refer to palaces as important local cultural assets. Palace owners and managers have also recognized the advantages of visibly grouping similar establishments across the district and the benefits of cooperation, especially for the promotion of an entire area and broader efforts to preserve unique cultural landscapes.

## **5 Case study: comparison of castle hotels in Poland's silesian elysium and in northern Hungary**

### **5.1 Poland**

The Silesian Elysium is the allegorical name for a concentration of castles situated in the Jeleniogórska Valley, close to the Czech-German border in the southwest of Poland, near the industrial city of Wrocław. Eight palaces in Jeleniogórska Valley currently operating as hotels together offer 246 rooms and 502 beds. In 2005, the cultural cluster of castle hotels established the brand the "Valley of Palaces and Gardens," evoking associations with the best-known such clusters in the world such as the Loire Valley. The cluster is currently applying for inclusion on the UNESCO World Heritage Sites list.

The cluster's specific feature is that while its members, innovative in the local context, are competing but also cooperating with each other and with many other local and sub-regional firms, and generating diverse positive effects at different spatial scales. These include strictly economic effects leading to multiplier effects and positive changes to the local economic structure, as well as numerous indirect and non-economic effects on local identity, aesthetics, the cultural calendar and quality of living. The activities of the businesses in these historic residences are respectful of and well inscribed in the area's cultural landscape, appreciating and creatively using its ecological and cultural resources.

Palace owners and managers have initiated a one-of-a-kind gentrification process. They have taken on the role of the "new gentry" in the rural setting. Their arrival in the area and their appreciation of the economic and cultural potential of an existing material heritage has driven the recreation of pre-war relations, links and dependencies between the palaces and their environment in a completely changed post-war social milieu. Like their German predecessors prior to the war, they employ local residents, purchase goods and services from them, and serve as a point of reference in terms of lifestyle, care for property, and the provision of tourist services. They also play a key role as new local stakeholders and leaders, inspiring the rediscovery of both material heritage and immaterial cultural values "dormant" in their localities.

## 5.2 Hungary

The abundance of castles and mansions in the present territory of the Republic of Hungary can be explained by the fact that the nobility, the proprietors of these properties, made up a proportion of the population larger than anywhere else in Europe other than Poland. The majority of Hungarian castles and mansions were built – for reasons of defence against intruders – in mountainous areas such as the northeast of the country during the eighteenth and nineteenth centuries. Once there were 4,500 castles and mansions on the territory of the Kingdom of Hungary, but many of them have been ruined through the tribulations of history. At the end of the twentieth century there were approximately 3,500 historical buildings left standing (National Trust of Monuments for Hungary 2019<sup>9</sup>).

In the area of observation, the NUTS-II statistical unit of Hungary (i.e. the Northern Hungary region), there are currently 38 castles used for government or commercial purposes, of which 16 function as municipal historical heritage museums, and 22 as accommodation. Of the latter, 12 castle hotels proper are in commercial use, operated by business entities; the remaining 10 are managed as various types of accommodation (lower-category tourist bed-and-breakfasts, hunting lodges, etc.). A survey by Horváth (2016) investigated visiting guests' attitudes and perceptions of the services of the castle hotels embedded in the given environment. The general and common characteristics of the hotels included in the survey – although belonging to different categories (four- and five-star commercial accommodation) and with varied room capacity – include the fact that they were built in the same period, have similar architectural characteristics both in terms of exterior and interior design, and possess identical amenities:

- Geographical location: small villages in mountainous areas, number of residents is less than 2,000,<sup>10</sup> except for Tarcsl (2,912 inhabitants).
- Minimum one-hour drive by car from the capital.
- Buildings are older than 100 years, in private ownership.
- Properties are Listed National Heritage Buildings and therefore strictly protected.
- Buildings are surrounded by large, landscaped parks.
- Amenities include wellness and open-air sports facilities.
- Comprehensive information or exhibition about Architect, Builder Family and former utilization of castle on display.
- Availability of cultural, training and leisure programs and events.
- Year-round opening.
- Renovated or extended in the last ten years.

As part of the National Castle Program, 32 Hungarian castles will be renewed by 2020. The Program is embedded in the National Tourism Development Strategy of Hungary 2014–2024, and is supported by the operative objectives of developing heritage tourism product categories that represent outstanding features, authentic values and potential which are also spatially focused and rely on integrated thematic TDM.<sup>11</sup>

## 6 Conclusion

Sustainable destination practices are recognized by UNWTO organizations and institutions as they guarantee adequate stakeholder involvement, thus assuring the long-term viability of tourism projects, whether old or new. Specifically, this chapter sought to explain both conceptually and by concrete examples how Travel and Tourism development is capable of promoting cultural heritage and traditions, in addition to creating extended economic benefits and employment creation.

Furthermore, an attempt has been made to clarify how the wider implications of destination management and sustainable tourism development practices are intricately intertwined. Through the lens of community-based cultural and historic heritage conservation, the practices of two regions in two different countries, Poland and Hungary, were presented to demonstrate their efforts to tackle the issue of destination management. The message to take away from the examples is that:

- Tourism is a growing contributor to national GDP, hence related planning strategies must be carefully developed and delivered,
- Heritage tourism, when planned with the above principles in mind and considering active stakeholder involvement, can effectively drive local development.

### Notes:

<sup>1</sup> Treaty on the Functioning of the European Union.

<sup>2</sup> The UNWTO's Code of Ethics, containing guidance (UNWTO 2019). The organization's mission is to promote the implementation of responsible and sustainable methods of tourism management. Available at: <http://ethics.unwto.org/en/content/global-code-ethics-tourism> (15 March, 2019).

<sup>3</sup> WTTC: World Travel & Tourism Council.

<sup>4</sup> Oxford Economics is a research and analytical consultancy headquartered in Oxford, England.

<sup>5</sup> UNWTO: World Tourism Organization.

<sup>6</sup> The United Nations Conference on Sustainable Development, also known as Rio 2012, Rio+20, or Earth Summit 2012, was the third international conference on sustainable development, aimed at reconciling the economic and environmental goals of the global community.

<sup>7</sup> UNEP: The United Nations Environment Programme is an agency of United Nations and coordinates its environmental activities.

<sup>8</sup> DMO: Destination Management Organisation. A tourism board or visitor bureau responsible for specific management tasks of tourism development, an institution promoting a community as an attractive travel destination.

<sup>9</sup> See: NGM-NTH: National Tourism Development Concept of Hungary 2014–2024.

<sup>10</sup> Based on census of 01.01.2010 (Hungarian Central Statistical Office 2019).

<sup>11</sup> See: NGM-NTH: National Tourism Development Concept of Hungary 2014–2024.

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## Smart and Intelligent Cities

ZSUZSANNA E. HORVÁTH

**Abstract** Societal development is increasingly driven by knowledge, or sets of specialized knowledge, accumulated by communities, efficiently and efficaciously disseminated among its members. At the onset of the fourth industrial revolution, the future of local development, including communities such as cities, depends on how intensively they can rely on state-of-the-art technology. Hence the importance of “Smart Cities,” and “Learning Cities”. The paper taps into the latest developments in the domain and provides conceptual background, definitions, and future insights as driven by key international literature findings. It will demonstrate, by way of achievements/examples/best practices, how key Smart City components in the domain of utilities, transportation, environment, public services and commerce can offer modern solutions to the typical problems encountered by cities. It will also highlight technical solutions such as sensors/actuators and embedded systems, communication networks and protocols, asset/event cataloging and semantics/taxonomies, and finally the use of big data/analysis/mining. The inventory of solutions would not be complete without a description of how citizen involvement and innovations can facilitate progressive city management. Finally, the paper presents a case study that compares typical smart city solutions from Hungary and abroad.

**Keywords:** • smart city • technical solutions • progressive city management • cloud-based initiatives

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## 1 Conceptual framework

In the second decade of the twenty-first century, more than half of the global population live in urban areas, and the share of big cities is predominant. The world's largest metropolitan areas are home to more than one-eighth of the global population. Cities are the core of economic growth, demonstrated by the fact that nearly one-third of global economic output is focused here (Gere 2016). Stemming from their roles as drivers of modern economic growth – involving commerce, innovation, talent and infrastructural relations – global cities play a key role in the governance of the global economy.

The growth rate of the population of large cities is spectacular, and ever rising. The share of the global population is also increasing. It is therefore of fundamental interest from a global perspective to manage cities in a way that is sustainable in all aspects.

The rise in the populations of large cities is coupled with the wake of the fourth industrial revolution, resulting in IT being expanded to all areas of life. In the near future, IT will be inevitably governing people's lives, including the environments people live in. Technical innovations are present in both the private and the public sphere; they facilitate the everyday lives of individuals and also assist governments (national, regional or local) to better manage the lives of communities. More and more activities are being optimized or automated so that time management and the exploitation of resources are maintained at ideal levels. The final state of sophistication in the interconnectedness between people and internet-provided management is called the Internet of Things.

Large cities suffer from a number of problems which are inherent to their development, and often inorganic, forced or unplanned. Such problems, among others, include the high cost of living, congested communities, public health crises, and fossil fuel dependency (Czirjak and Gere 2016). IT companies have realized the potential of innovative technological solutions as remedies for tackling urban issues, and today Microsoft, IBM,<sup>1</sup> CISCO,<sup>2</sup> LG,<sup>3</sup> GE<sup>4</sup> and SIEMENS<sup>5</sup> all use the Internet of Things.

A recent report by PwC<sup>6</sup> Russia (PwC 2017) presented survey findings about the tech-readiness of global cities. The term tech-readiness signifies how ready cities are to adopt technology-driven solutions across sectors from education to security and healthcare. This capacity was gauged across several variables, such as the presence of basic infrastructure, the strategies and regulations that support the adoption and use of new infrastructure, the availability of finished prototypes, and the social readiness of citizens to use new technologies.

The report concludes that the ranking and achievement of the “tech-readiness” of cities is spread among the following candidates:

1. Singapore (64%);
2. London (59%);
3. Shanghai (55%);

4. New York (53%);
5. Moscow (53%) (PwC 2017, 2).

The report, among other issues, also highlighted a few areas of innovation as being indicative of tech-readiness. “In terms of embracing new tech in daily life, London (42%) and Toronto (41%) came in at the bottom. When gauging innovation in culture and tourism, Barcelona (78%), Shanghai (78%) and Singapore (72%), took the lead. In readiness to integrate autonomous transportation, London (72%) was at the top. And in terms of digital economy infrastructure, Singapore (75%) came in first—likely due to its adoption and investment of tech in educational settings” (PwC 2017).

City growth, efficient management, and innovative solutions in IT are today interconnected. The application of smart IT solutions for tackling community or urban issues has been gradually adopted across the world, and this process has given rise to the Smart Cities “movement”. The denomination Smart Cities can be perceived as a parallel to smartphones, which are versatile, programmable, and whose designers and programmers strive to provide personalized solutions. An expansion of the *smart cities* term is smart urbanization, which is seen as key to building safer, healthier, resilient and sustainable cities of tomorrow by utilizing smart growth principles, effective urban planning models, ICTs, and low-carbon energy systems. Smart urbanization, with smart cities nested within, can help create more habitable and efficient urban centres (Horváth 2016). It may also help alleviate pressure on existing natural habitats, resources and biodiversity, thereby reducing the risk of man-made disasters.

In response to UN Sustainable Development Goal (SDG) no. 11, stipulating: “Make cities and human settlements inclusive, safe, resilient and sustainable” (UN General Assembly 2015, 14), ITU<sup>7</sup> and UNECE<sup>8</sup> launched the United for Smart Sustainable Cities (U4SSC) initiative. U4SSC primarily advocates for public policy to encourage the use of ICTs to facilitate and ease the transition to smart sustainable cities worldwide. In order to provide a conceptual framework for the initiative, UNECE and ITU, together with other partner organizations, have developed a common definition of a smart and sustainable city:

*“A smart sustainable city (SSC) is an innovative city that uses information and communication technologies (ICTs) and other means to improve quality of life, efficiency of urban operation and services, and competitiveness, while ensuring that it meets the needs of present and future generations with respect to economic, social, environmental as well as cultural aspects” (ITU 2017, 45).*

## 2 Case studies

In the next section, short case studies illustrating the various components or sub-systems of smart city solutions will be discussed, followed by select Key Performance Indicators (KPIs), pertaining to the domain under discussion.

KPIs are taken from the ISO 37120 – the first international standard<sup>9</sup> about city indicators, which lists a totality of 100 indicators (46 core and 54 supporting) which are structured around the following 17 themes: Economy, Education, Energy, Environment, Finance, Fire and Emergency Response, Governance, Health, Recreation, Safety, Shelter, Solid Waste, Telecommunications, Transportation, Urban Planning, Wastewater and Water & Sanitation (ISO 2014).

### 2.1 Smart economy (Busan, South Korea)

With an economy based on heavy industry, South Korea's second largest city, Busan, confronts challenges similar to those of other large, industrial cities. A primary challenge for Busan is creating job opportunities for its 60,000 annual university graduates and retaining a high-quality workforce. City leaders that face similar issues will be interested in Busan's decision to deploy Cisco's Smart+Connected Communities solution and public cloud infrastructure to stimulate job creation and business growth.

The Busan Metropolitan Government recognized the potential for growing its economic base through the use of information and communication technology (ICT). By connecting citizens, educational institutions, government agencies, and industry, the city has been able to drive sustainable urban development while providing citizens with easy access to city services. A 10GB broadband infrastructure, the Busan Information Highway, has already been deployed and linked to 319 public institutions. This infrastructure gives Busan government a strong foundation for expansion.

Busan Smart+Connected Communities solutions are delivered using a cloud infrastructure based on Cisco UCS™ Unified Computing System™ (UCS®). Today, the cloud connects the Busan Metropolitan Government, the Busan Mobile Application Center (BMAC), and five local universities. Eventually, it will deliver services to citizens through kiosks, citywide digital interactive displays, home-based access, and mobile access (PwC 2017).

One of the first major cloud-based initiatives is designed to create 3500 job opportunities and 300 start-up companies with a focus on mobile application development by 2014. Spearheaded by the Busan IT Industry Promotion Agency (BIPA), the project will create an open innovation ecosystem that fuels the app. economy of Busan. The Busan Metropolitan Government funds ICT development and provides training and education through the BMAC.<sup>10</sup> Software developers, entrepreneurs, and small businesses can register and gain access to tools, training, and testing resources for developing smart

applications and mobile app-based services for citizens. Revenue that is generated is returned to developers through BIPA.<sup>11</sup>

BMAC offers physical workspaces, such as project and meeting rooms, shared application development, cloud platforms for Windows and Mac operating systems, an applications library, a consulting center for start-ups and small office/home office professionals, testing tools, smart devices, application programming interfaces for access to municipal data, an application developer's forum, and marketing resources.

**Figure 1:** KPI indicators in the Smart Economy domain

THEME	CORE INDICATORS	SUPPORTING INDICATORS
Economy	City's unemployment rate	Percentage of persons in full-time employment
	Assessed value of commercial and industrial properties as a percentage of total assessed values of all properties	Youth unemployment rate
	Percentage of city population living in property	Number of businesses per 100,000 population
		Number of new patents per 100,000 population per year

Source: Author's construction adopted from ISO (2014).

## 2.2 Smart mobility (Doha, Qatar)

Like many developed areas, there are traffic jams in Qatar that not only aggravate commuters but can also be costly for companies with fleet vehicles that move goods and services around the region.

Smart Fleet combines sensors with Ooredoo's<sup>12</sup> wireless network to help businesses better direct their fleet vehicles to avoid traffic congestion and reduce operating costs (Smart Cities Council 2018). Council member Ooredoo, the telecommunications company based in the Qatar capital of Doha, has developed a cloud- and sensor-based Smart Fleet solution that deploys GPS<sup>13</sup> and GSM<sup>14</sup> technology to centralize and manage transport-related information. The subscription-based service can be used for any kind of fleet, whether in the services sector, transport and logistics, passenger transportation or construction.

When there is a traffic jam, the system can route a driver around it. This not only saves the driver time, but it can save other drivers time too. By reducing the number of vehicles driving into the congestion, the traffic jam can clear faster.

In addition to reducing the amount of gas wasted in traffic, Smart Fleet can also design fuel-efficient routes for drivers which can save companies money and help reduce

pollution. By keeping track of their assets in real-time, the system also helps the companies that use it reduce loss and theft.

**Figure 2:** Key Performance Indicators in the Smart Mobility domain

THEME	CORE INDICATORS	SUPPORTING INDICATORS
Transportation	Kilometers of high capacity public transportation per 100,000 population	Percentage of commuters using travel mode to work other than a personal vehicle
	Kilometers of light passenger public transportation system per 100,000 population	Number of two-wheel modernized vehicles per capita
	Annual number of public transport trips per capita	Kilometers of bicycle paths and lanes per 100,000 population
	Number of personal automobiles per capita	Commercial air connectivity (number of non-stop commercial air destinations)
		Transportation fatalities per 100,000 population

Source: Author's construction adopted from ISO (2014).

### 2.3 Smart environment (Triangulum, Eindhoven, the Netherlands; Manchester, UK; Stavanger, Norway<sup>15</sup>)

In the Triangulum project, the aim of Lighthouse Cities is to demonstrate that the integration of technologies from the energy, buildings, mobility and ICT sectors within a district can induce significant reductions in energy demand and local GHG<sup>16</sup> emissions and at the same time enhance quality of life and provide a basis for economic growth and development. The project consortium combines the interdisciplinary experience and expertise of twenty-two partners from industry and research and six municipalities which are committed to developing and implementing smart solutions which are planned to be further disseminated and replicated primarily in the three Follower Cities: Leipzig (DE), Prague (CZ), and Sabadell (ES), but also beyond.

As an overarching objective, Triangulum seeks to develop a model for the replication of smart city solutions based on cost and benefit, as well as maximize the dissemination and impact of the knowledge and innovation generated during the project. The replication approach has the following three stages, as shown in the graphic below: demonstration, assessment, and replication. In the demonstration phase, projects such as E-bus lines in public transport are implemented to show how public and private actors can work together to jointly improve the quality of life in cities.

The assessment phase serves to generate robust evidence by describing and quantifying the impacts and benefits. Later, and based on the former, business models that enable



replication in the Follower Cities and beyond are elaborated. To facilitate this process, “on-site assessments” have taken place in the lighthouse cities. These visits took place between late 2015 and early 2016 and were led by researchers from the Institute of Human Factors and Technology Management (IAT) at the University of Stuttgart, the Fraunhofer Institute for Industrial Engineering (IAO),<sup>17</sup> the Fraunhofer Institute for Open Communication Systems (FOKUS),<sup>18</sup> and TÜV Süd.<sup>19</sup> Each of the assessments took place over a period of approximately two weeks and involved 25–40 interviews (political, management and technical), and a creativity workshop. All of this activity was supported by the local Triangulum coordinators in the cities.

**Figure 3:** KPI indicators in the Smart Environment domain

THEME	CORE INDICATORS	SUPPORTING INDICATORS
Environment	Fine particulate matter (PM2.5) concentration	NO2 (nitrogen dioxide) concentration
	Particulate matter (PM2.5) concentration	SO2 (sulphur dioxide) concentration
	Greenhouse gas emissions measured in tonnes per capita	O3 (ozone) concentration
		Noise pollution
		Percentage change in number of native species

Source: Author’s construction adopted from ISO (2014).

## 2.4 Smart governance (G-Cloud framework, New Taipei, Taiwan)

With over 3.9 million citizens and more than 500 administered institutions and schools, New Taipei City Government began constructing and integrating a public cloud and service cloud, not only to strengthen city government operations and those of its subordinate agencies, but also to determine public sentiment regarding government services in order to facilitate a more rapid and effective public service for citizens. The G-Cloud framework is the foundation of the New Taipei City Government and is the cornerstone in terms of operating the public cloud and service cloud (Smart Cities Council 2018).

One of the biggest challenges was that complaints filed by citizens and their subsequent status were processed manually, and saved using various data formats. This meant that it took a lot of time and resources to perform this task. This was a major bottleneck.

Additionally, the user experience left a lot to be desired. The major complaint was the slow response time from the NTPC government regarding their complaints or requests. This was aggravated by the high number of inconsistencies in the responses that the citizens received.

Deputy Director Lin Chunyin at New Taipei City Government Information Center said: “The main objective of the official case is to integrate the two [cloud platforms] more closely and to unify rules, so that both internal colleagues and external users can experience the benefits ... furthermore, we realized it was important to minimize the number of resources required to process their complaints and requests, shorten the response time and finally, strive for 100% accuracy and consistency with regard to replies given to our citizens with regard to their complaints or requests” (Smart Cities Council 2018, 2).

**Figure 4:** Key Performance Indicators in the Smart Governance domain

THEME	CORE INDICATORS	SUPPORTING INDICATORS
Governance	Voter participation in last municipal election (as a percentage of eligible voters)	Percentage of women employed in city government workforce
	Women as percentage of total elected to city-level office	Number of convictions for corruption and/or bribery by city officials per 100,000 population
		Citizen representation: number of local officials elected to office per 100,000 population

Source: Author’s construction adopted from ISO (2014).

This domain measures a city’s civic engagement – particularly for women – as well as the honesty and integrity of its elected officials. Increasing transparency in city governments is a critical step in providing and defending basic rights at the city level. “The advantage of the global standard for measuring and reporting on the performance of city governance – including the role of women in city government, can help city leaders worldwide be more responsive, transparent and more responsible to their citizens” (Smart Cities Council 2018).

## 2.5 Smart education (Cibernàrium, Spain<sup>20</sup>)

Barcelona city government founded the whole digital ecosystem of Barcelona Activa, of which Cibernàrium is a network member. The latter organization governs the training and technological dissemination program of Barcelona Activa – Ajuntament de Barcelona. It offers training for professionals and companies, as well as internet initiation activities for all citizens. The Cibernàrium formula involves a wide range of activities of short duration that are very practical and focused on very specific topics – usually a solution, a concept, or a technological tool that helps participants to develop their technological skills and, therefore, helps with their professional training.

Cibernàrium publishes informative materials in different formats: video courses, activity dossiers, and multimedia content. Cibernàrium hosts days for technological diffusion, along with formative and sectoral events directed at professional sectors. Cibernàrium

develops its activity in different spaces of Barcelona and is headquartered in the Media-TIC Building of 22@.

**Figure 5:** Key Performance Indicators in the Smart Education domain

THEME	CORE INDICATORS	SUPPORTING INDICATORS
Education	Percentage of female school-aged population enrolled in school	Percentage of male school-aged population enrolled in school
	Percentage of students completing primary education	Percentage of school-aged population enrolled in school
	Percentage of students completing secondary education	Number of high-education degrees per 100,000 population
	Primary education student/teacher ratio	

Source: Author's construction adopted from ISO (2014).

### 3 Conclusion

It is especially important to have a good understanding and insight into solutions as modern cities are expected to witness an increase in the number and complexity of problems that must be tackled. Therefore, this chapter had the aim of presenting a few solutions related to the development of Smart and Intelligent Cities. It offered a conceptual background, definitions, and working realizations of principles, followed by future insights as driven by key findings from international literature. We have sought to demonstrate, by way of presenting achievements/examples/best practices, how key Smart City components in the domain of utilities, transportation, the environment, public services, and commerce can efficiently resolve the typical problems encountered by cities.

#### Notes:

<sup>1</sup> International Business Machines Corporation, an American multinational information technology company.

<sup>2</sup> Cisco Systems, Inc., an American multinational technology conglomerate.

<sup>3</sup> LG Corporation, formerly Lucky-Goldstar, a South Korean multinational corporation.

<sup>4</sup> General Electric, an American multinational conglomerate.

<sup>5</sup> Siemens AG, a German conglomerate.

<sup>6</sup> PricewaterhouseCoopers, a multinational professional services network.

<sup>7</sup> International Telecommunication Union (ITU), a specialized agency of the United Nations.

<sup>8</sup> "United Nations Economic Commission for Europe (ECE) is one of the five regional commissions under the jurisdiction of the United Nations Economic and Social Council". (Wikipedia. Available at: [https://en.wikipedia.org/wiki/United\\_Nations\\_Economic\\_Commission\\_for\\_Europe](https://en.wikipedia.org/wiki/United_Nations_Economic_Commission_for_Europe) (15 March, 2019)).

<sup>9</sup> The International Organization for Standardization (ISO) is an international standard-setting body composed of representatives from various national standards organizations.

<sup>10</sup> Busan Mobile Application Center, an innovative center to host a variety of services for its citizens, operating like an app store for developers.

<sup>11</sup> Busan IT Industry Promotion Agency, an establishment to foster and support information and cultural industries.

<sup>12</sup> Ooredoo QSC: an international telecommunications company headquartered in Doha, Qatar.

<sup>13</sup> Global Positioning System (GPS): a satellite-based radionavigation system.

<sup>14</sup> GSM (Global System for Mobile communications): a standard developed by the European Telecommunications Standards Institute (ETSI).

<sup>15</sup> For further information, please check the website of the Triangulum project: <http://triangulum-project.eu/> (15 March, 2019).

<sup>16</sup> Greenhouse gas.

<sup>17</sup> The IAO offers research services to companies and public-sector bodies and institutions.

<sup>18</sup> FOKUS is a non-profit organization, helps the conception and implementation of research and development projects of any size.

<sup>19</sup> A technical service corporation catering to the industry, mobility and certification Segments.

<sup>20</sup> For further information, please check the website of the Cibernàrium programme: <https://cibernarium.barcelonactiva.cat/> (15 March, 2019).

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## **Innovative Policy Interventions, Plans and Initiatives**





## Environmental Cooperation as a Tool for Local Development and Peace-building in Conflict-affected Areas

ŠÁRKA WAIŠOVÁ & LADISLAV CABADA

**Abstract** Since the end of the 1990s, scholars and policy makers have spoken about using environmental cooperation as a tool for local development, conflict transformation and peace-building. Environmental cooperation is believed to internalize norms, form local and regional identities and interests, operationalize routine communication, and marginalize the acceptability of the use of violence. The idea of using environmental cooperation as a tool for local development and peace-building has even been reflected in the agendas of international organizations. UNEP<sup>1</sup> has introduced specific science-based internationally applicable instruments for capturing and evaluating the relations between environmental sustainability, development and peace. In particular, the policy instrument of Post-conflict Environmental Assessment is presently used successfully in conflict-prone and post-conflict areas.

**Keywords:** • environmental cooperation • local development • peace-building • environmental peace-building • environmental scarcity

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## 1 Introduction

Environmental cooperation as a political issue has a short but rich history. Environmental issues penetrated the political agenda in the mid-1960s in various forms and have since stayed on the agenda of international and national politics. One of the newest ideas is that of using environmental cooperation as a tool for peace-building and development, particularly in post-conflict or conflict-prone areas. This idea arose in the 1990s in connection with efforts to seek more effective tools for fostering sustainable development and conflict resolution. Analyses of environmental cooperation in underdeveloped and conflict-affected areas were first conducted in the first half of the 1990s. The first proponents (e.g., A. Westing) often worked as environmental experts and propagated the idea of so-called natural peace parks. These conservation areas were established with the aim of protecting local ecosystems from the impacts of armed conflict. During the last decade, several peace parks have been established, such as the Sierra del Condor Park between Peru and Ecuador, the Kashmiri Siachen Glacier Park between India and Pakistan, and the Demilitarized Zone between North and South Korea.

The idea of peace parks was elaborated in connection with the resolution of conflicts caused by disputes about natural resources and raw materials. Particular attention has been paid to conflicts over water, diamonds, coltan,<sup>1</sup> and tropical timber (Le Billon 2009; Matthew *et al.* 2002). Later, some authors (for example, Conca and Dabelko 2002; Wallace and Conca 2012) and consequently policy-makers (e.g. within the World Bank, UNDP and UNEP; Westing 2010) began to consider the possibility of using environmental cooperation as a tool for local development, conflict transformation and peace-building.

This deliberation is based on the presumption that conflict and cooperation can coexist and that a cooperative approach to planning, management, and the use of environmental resources can boost development, confidence, communication, and interactions between conflict parties and contribute to the transformation of threats and uncertainties (see Box 1). According to supporters of the idea, environmental cooperation helps to internalize norms, form local and regional identities and interests, operationalize routine communication, and marginalize the acceptability of the use of violence (Brock 1991). In other words, environmental cooperation is perceived as a tool for (local) development, conflict transformation and resolution because it enables institutional and behavioral transformations and changes in the approaches of the affected actors.

**Box 1:** Dominican Republic and Haiti<sup>2</sup>

*UNEP and UNDP accompanied the Governments of Haiti and the Dominican Republic in undertaking a detailed assessment of their border area. Economic and resource inequalities between the two countries are the cause of many of the transboundary problems that have been identified in the border zone. Several of the identified issues related to the environment and the use of natural resources also raise the short-term but significant risk of instability and conflict regarding the relations between the two countries. Fourteen related recommendations were developed with and accepted by the two governments. The recommendations are expected to reduce chronic poverty and hunger in the border zone while promoting more sustainable livelihood practices and enhancing the resilience of the population to shocks and stresses. They also contribute to preserving peaceful relations between the two countries through increased national and local level bilateral cooperation that will reduce tension and the risk of conflict over border zone issues.*

Ideas about the positive effects of environmental cooperation on local development, confidence building and conflict transformation proceed from the fact that there exists a relationship between environmental cooperation and other forms of cooperation, or, better said, that environmental issues can hardly be separated from other problems that local communities are challenged by. Many scholars and policy-makers believe that ecological interdependencies create social relationships upon which local communities can capitalize and that these interdependencies can create win-win circumstances. Environmental issues are closely related to the other areas of life of local communities such as the level of development, the structure of the economy, the culture of the community, human rights policy and the security situation (see Table 1).

For example, we have evidence that involuntary migration flows such as the flights that occur before violence or famine have significant negative environmental effects: people who leave their homes without funds and property often loot the localities they move into; they may also cut down trees for fuel and hunt the local animal population for food. In a short time this can lead to the widespread environmental degradation of the hosting area. This was experienced in the Virunga national park on the border between Rwanda and The Democratic Republic of the Congo (DRC); Rwandese fleeing before the 1994 genocide found shelter in the region and within a few months decimated the population of mountain gorillas and cut down a large area of rainforest. Concurrently, the high level of insecurity in the region caused mainly by the ongoing attacks of small militia groups made the protection of the natural park and of the rainforest impossible.

**Table 1:** Examples of the relationship between environmental issues and other thematic areas

	<b>Climate change and global warming</b>	<b>Deforestation and land degradation</b>	<b>Water scarcity</b>
<b>Environment and ecosystems</b>	Change in ecosystems, droughts, floods, loss of animal species	Loss of endemic species, local water scarcity	Change in local climate, droughts, loss of natural environment and endemic species (wetlands)
<b>Security and threats</b>	Rise in ocean level and loss of territory and agricultural land, lack of food	Landslides and torrential rains endanger settlements and infrastructure	Water conflicts
<b>Development and poverty</b>	Hits poorest countries and poor people hardest	Rise in environmental refugees, loss of natural environment	Loss of agricultural land, lower yield, rise in number of environmental refugees
<b>Trade and economics</b>	Change in trade routes, unstable weather conditions	Regional and local resettlement, rise in poverty over long term	Increases in water prices, need to rebuild water and sewage infrastructure

Source: Authors' construction.

As it is evident from Box 1, the idea of using environmental cooperation as a tool for local development, conflict transformation and peace-building has intrigued not only researchers, but also international institutions. It appears on the agenda of the OSCE<sup>3</sup> (under the term “environmental confidence building”), UNEP (under the term “environmental peacebuilding”), and at the World Bank, the Asian Development Bank, the European Union, NATO,<sup>4</sup> international environmental agencies, and many non-governmental organizations (for example, the World Wildlife Fund and MacArthur Foundation) (ADB<sup>5</sup> 2019 and GMS CEP<sup>6</sup> 2019; Van Dijck 2012; IUCN<sup>7</sup> 2013; MacArthur Foundation 2019; OSCE 2012; UNEP 2009).

Despite the growing number of projects that involve the use of environmental cooperation as a tool for local development and peace-building and growing interest among scholars about the issue, the assumptions about the conditions for the establishment of environmental cooperation and its operation in underdeveloped conflict-prone or conflict-affected areas are quite unclear. Little is also known about how the idea of using environmental cooperation as a tool for local development and peace-building developed, and how it is used in practice today. This gap is filled by this chapter. We first present the development of the approach of “environmental cooperation as a tool for local

development and peacebuilding” and offer a critical analysis of the literature on the issue. Second, attention is paid to “environmental assessments” and to “post-conflict environmental impact assessment,” which are the basic practical instruments of UNEP for identifying the links and interdependencies between environment, security and development in specific areas.

## **2 Environmental cooperation as a tool for local development and peace-building: history and criticism of the approach**

In this chapter we will proceed chronologically, analysing how considerations of the relationship between environment, security, conflict and underdevelopment have evolved over time. We cover the most relevant academic texts and documents of international governmental and nongovernmental organizations, as well as those of think tanks and national responsible bodies.

Environmental issues became a part of security studies during the 1950s and part of the agenda of international politics during the 1960s. During this period authors such as Harrison Brown (1954) studied the relationship between environmental changes and security, but without the explicit use of this terminology. Development studies incorporated environmental issues a decade later, at the beginning of the 1970s. In development assistance and policy-making, both issues have been strongly linked since the 1990s when Finland suggested adding to the existing Official Development Assistance concept a broader concept of concessional resource flows for development, humanitarian and environmental purposes, and when scholars and practitioners started to talk about the environmental assessment of development projects and the “greening of development assistance”.

One of the first pieces of work to connect the environment with development and security was a book published in 1972 by Donella H. Meadows, Dennis L. Meadows, Jørgen Randers and William W. Behrens called *the Limits to Growth*, which predicted that the options for the development of human populations are limited by the amount of resources that are available. The oil crisis of 1973 proved some of Meadows’ theses to be correct and the matter of the relationship between security, resource availability, development, and the state of the environment became a subject of political debate and academic research.

At the turn of the 1970s, the issue of security began to penetrate the debates of ecologists and environment experts. After experiencing the Vietnam War, the world started to pay attention to the negative impact of warfare on the environment. During the 1970s and 1980s environmental topics became a common part of the international agenda. The first Earth Summit took place in 1972; in 1973 the United Nations Environment Programme was established; the United Nations Conference on Human Settlements HABITAT took place in 1975; and in 1982 the UN General Assembly adopted the World Charter for

Nature. In 1980, the UN Commission led by W. Brandt published the report *North-South: A Program for Survival* (ICIDI<sup>8</sup> 1980), which discussed the necessity of connecting development-related considerations with the protection of the environment and natural resources. In 1987, G.H. Brundtland's commission published the report *Our Common Future*, in which the necessity for the protection of the environment and natural resources was articulated in connection with the term "sustainable development" (WCED<sup>9</sup> 1987).

These events, changes, and developments led to the rise of so-called new political ideologies, such as environmentalism, including deep ecology and ecofeminism, and paved the way for debates about the environment and natural resources in security and development studies, as well as policy-making. Since the end of the 1980s the idea of the relationship between the environment, (in)security and (under)development was further developed and resulted in a new approach called environmental security. As noted by Dabelko, "environmental security has emerged as a transnational idea, the core of which was the assumption that environmental degradation and the depletion of non-renewable resources can become a source of threat to the security of individuals, groups, corporations, states, ecosystems and the international system" (Dabelko in Rønnfeldt 1997, 474).

Individual pieces of work devoted to the analysis of the relationship between the environment, security, peace-building and conflict resolution are not presented here in detail; only the approaches which have been gradually generated are summarized. The first wave of researchers (e.g., Mathews 1989; Levy 1995; Buzan *et al.* 1998) focused on researching the relationship between the environment and national security. These authors considered environmental degradation and the lack of natural resources a threat to national interests and values. The second wave of scholars (e.g., Granzeier 1997; Barnett 2001) considered the environment as an independent referent object. They also considered ecosystems, ecological processes and ecological balance to be the same. The third wave of researchers (Gleick 1991; Gleick 1993; Homer-Dixon 1991; Homer-Dixon 1994; Le Billon 2009) claimed that environmental degradation and environmental change and a deficiency of natural resources (so-called environmental scarcity) can become the cause of outbreaks of violence and/or that raw materials can become a driving force behind violent conflict.

It is worth mentioning – from the perspective of our topic – that a numerically smaller critical stream of scientists (e.g., Dudley 1997; Gleditsch 1998) have doubted the causal chain that was postulated; namely: high resource consumption – environmental degradation – deepening of scarcity – higher competition – greater risk of the outbreak of violence. For example, Dudley (1997) and later also other scholars (Borrini-Feyerabend *et al.* 2007; Luzi 2007; Young 2009) argued that environmental degradation and scarcity can lead to the emergence of joint interests and a shared approach to facing environmental problems.

Reflections on environmental scarcity and so-called conflict resources since the mid-1990s have increasingly been influenced by the debate about development – economic as well as sustainable- (see Collier *et al.* 2003; World Bank 2011). This development approach has been called the security–development nexus and is directly associated with the establishment of the human security concept at the UN. It was mainly the UNDP which advocated the concept of human security, including so-called “Freedom from Fear” (protection of the individual against political threats) and “Freedom from Want”. Freedom from Want is outlined in UNDP documents as the interconnection of individual security and the chance for individual sustainable development, which also includes environmental security (UNDP 1994, 25). Environmental security is defined as the protection of the individual against the degradation of local ecosystems and global ecological changes (UNDP 1994, 28–29). The importance and relevance of these themes in practice have been advocated by those who have pointed out the increase in environmental migration and the number of environmental refugees (for example, Westing 1992).

In the mid-1990s, it was not only the academic world that was engaged with the issue of the rise in environmental problems and the need to jointly manage degradation/environmental change, underdevelopment and insecurities. At least five important initiatives emerged with a focus on the environment, development and security nexus: 1. Reducing Emissions from Deforestation and Forest Degradation (REDD+); 2. the Clean Development Mechanism (CDM); 3. the Global Environmental Facility (GEF); 4. the Green Climate Fund (GCF); and, 5. UNEP’s Crisis Management Branch. REDD+ seeks to compensate countries for making emission reductions through reducing deforestation. The CDM allows agents in developed countries to purchase emission reductions in developing countries in the hope of simultaneously reducing emissions and spurring sustainable development. GEF, the World Bank framework, is a more traditional aid vehicle that provides a package of grant funding and technical assistance. The GCF emerged as a major initiative for facilitating financial flows from developed to developing countries to meet climate-related challenges (Arndt and Tarp 2017). UNEP’s Crisis Management Branch conducts field-based assessments, works to reduce the risk of disaster, and promotes environmental cooperation for peace-building, among other activities (UN Environment 2019).

During the following decade, researchers engaged in the study of conflict elaborated the relationship between the environment and natural resources on the one hand, and the causes, courses and conflict resolution on the other, into a multidimensional and complex field, in which four wide streams can be identified. The first stream (for example, Homer-Dixon 1991 and 1994) has worked further with the concept of environmental scarcity and enriched it with ideas about demographic growth, climate change and water wars, claiming that environmental degradation and a deficiency of natural resources and raw materials reduces the adaptive capacity of societies and encourages outbreaks of violence.

The second stream believes that natural resources and raw materials can serve to prolong conflicts as they enable combatants to obtain resources for warfare (compare with the debate about so-called blood diamonds; de Koning 2008). Representatives of the third stream argue that unequal access to resources, denial of access to resources, or insufficient compensation to local communities whose resources are consumed can cause a sense of grievance that becomes the root of violence (Collier and Hoeffler 2004).

The above-mentioned streams gave rise to the fourth one (Brock 1991; Conca and Dabelko 2002; Dabelko 2006; Rustad *et al.* 2012), which comes to the conclusion that the transformation and resolution of conflicts, post-conflict reconstruction and development assistance must take into consideration environmental changes and natural resources.

Some scholars and policy-makers go even further, stating that environmental issues go beyond politics; that it is apparent that unilateral approaches to environmental protection or environmental change solve nothing and that environmental matters have the potential to catalyse cooperation. Significant optimism is created by studies undertaken by Aaron Wolf (1997) who presents evidence that states that share water resources tend to cooperate rather than come into conflict.

The fourth stream consolidated around the year 2000, when a number of studies were published (Matthew *et al.* 2002; Conca and Dabelko 2002) that described the peace-building and development impact of environmental cooperation, and it was also at this time that this idea became established in important international organizations – in particular, the UNEP (see above), OSCE, UNDP and World Bank. It was also at this time when UNEP introduced a new framework for the evaluation of the environmental situation of particular countries or regions to grasp the nexus between environmental sustainability, natural resources, development and security, and to enable the prioritization of needs and the adjustment of policies. Consequently, terms like “greening development assistance,” “environmental governance,” and “greening the blue helmets” emerged.

### **3 Environmental assessment: The nexus between environmental sustainability, development and peace-building**

A rise in the importance of environmental issues in politics and security was evident during the late 1980s, strengthened by several international events in the first half of the 1990s. The Chernobyl nuclear power plant accident, a series of chemical-related incidents in East European countries, rising water scarcity in Central Asia, and several oil tanker collisions and the related contamination of extensive areas of ocean by oil – to name a few incidents only – confirmed that environmental degradation and sustainability should be the top international priorities and require a coordinated international approach.



It was also crystal clear that environmental degradation progresses faster in poor and developing countries which do not have sufficient resources, technical skills and human capital to face such problems. A number of weak, poor, or post-conflict countries have not been able to conduct environmental assessments at all or to implement systematic environmental policy; either the national authorities lack the scientific expertise or operational capacity to conduct environmental assessments, or there have been serious security problems in the region and the necessary conditions for conducting field research and collecting evidence for environmental assessments have been lacking.

In response, several international bodies have accepted a new approach in an effort to assist countries to cope with environmental problems. The UNDP,<sup>10</sup> UNEP, European Union, World Bank, OSCE and even NATO have introduced new environmental frameworks and initiatives. A series of internationally coordinated programs and platforms have progressively integrated environmental issues into development projects and security topics. As an example, the programme “Environmental-Security Initiative” (ENVSEC) reflects on the interrelated challenges of environmental sustainability, development and security in Central Asia and Eastern post-soviet Europe. ENVSEC has been supported since 2010 by the Regional Environmental Center, NATO, UNDP, UNEP and OSCE.<sup>11</sup> While this initiative is only of regional scope, other international initiatives and support mechanisms have been established (such as the Global Environmental Facility, as mentioned above).

The most problematic issue was how to approach the multi-disciplinarity of the nexus between environmental sustainability, underdevelopment and security, and how to translate these issues into practical policies. Based on these problems and needs, UNEP introduced a framework called “Environmental Impact Assessment” which developed into “the process by which the consequences and effects of natural processes and human activities upon the environment are estimated, evaluated or predicted” in less than one decade (UNEP 2015, 4). In reality, Environmental Impact Assessment (hereafter, EIA) is a toolbox that enables the scrutiny and evaluation of a plethora of interconnected issues and problems, and offers an opportunity to suggest priorities and solutions. It is science-based approach to collecting evidence for improving policy making.

Based on the experiences, lessons learned, and needs of the affected countries, UNEP has developed many different types of environmental assessment methodologies. These include Integrated Environmental Assessment, Ecosystem Assessment, Environmental Valuation Assessments, Flash Environmental Assessment and Post-conflict Environmental Assessment, to name just a few. The particular assessments differ in terms of the scale of evaluation and according to the trends, processes and issues under evaluation (see Table 2). While this chapter particularly concentrates on the possibility of using environmental cooperation as a tool for development and peace-building, the primary focus here is Post-conflict Environmental Assessment.

**Table 2:** Types of UNEP environmental assessments (random sample)

Type	Scale assessment	General information
<b>Integrated Environmental Assessment</b>	Global Regional National Local	Interdisciplinary; aims to identify, analyse and appraise all relevant natural and human processes and their interactions which determine both the current and future state of environmental quality and resources; integrates social, economic and environmental issues.
<b>Ecosystem Assessment</b>	Global Regional National Local	Evaluates the consequences of ecosystem change on human well-being, which provides the scientific basis for the actions needed to enhance the conservation and sustainable use of those systems and their contribution to human well-being.
<b>Risk Assessment</b>	Global Regional National Local	Intended to calculate or estimate the risk to a given target system, region, state or population, including the identification of attendant uncertainties or particular agents; involves steps to determine needs and gaps, hazards, and vulnerability.
<b>Vulnerability Assessment – climate change and disasters</b>	Global Local	Focuses on climate change and disasters; aimed at fostering understanding of the impacts, risks, and hazards associated with adverse effects brought about by climate change, natural hazards, and disasters, combined with economic, social and environmental factors that increase or decrease vulnerability.
<b>Post-conflict Environmental Assessment</b>	National Local	Aims to identify, evaluate, and respond to critical environmental issues to identify environmental risks, during or immediately following conflict situation; provides information on social and economic impacts associated with the use of natural resources.
<b>Thematic Assessment</b>	Global Regional National Local	Focuses on a specific theme, e.g. water, air, biodiversity, cities, land, etc.
<b>Environmental Impact Assessment</b>	National Local	Seeks to identify and evaluate the potential environmental consequences, impacts and effects of a proposed development project in order to minimize, mitigate or eliminate any adverse potential impacts.

Source: Authors' construction based on UNEP (2004; 2015).

#### 4 Post-conflict environmental assessment

Natural resources are key to the peace process and development because they often underpin other peace-building and development sectors. From water for drinking and agriculture to forests and wetlands that support livelihoods to high-value natural resources such as timber, coltan and copper that can kick-start economic growth and become an engine for recovery and development, how natural resources are used and how environmental degradation or protection are approached influence development and peace-building endeavors. As evidence from the field shows (e.g. from South Sudan, Darfur, Virunga National Park in the DRC or the Emerald Triangle between Laos, Cambodia and Thailand; more see Waisová 2017), deficiencies in the management of natural resources and in environmental governance and the absence of environmental cooperation are some of the most common sources of underdevelopment and of local unrest and conflict (see also Chart1).

Since 1999, UNEP has offered tailored technical expertise for conducting post-conflict environmental assessments in response to increasing civilian conflict and the environmental degradation and looting of resources that is interconnected with these conflicts. The goal of this activity has been to detect and analyse the environmental drivers of conflicts and the impact of such conflicts on the environment and to suggest solutions for stopping environmental issues becoming conflict drivers or creating victims in the future. UNEP's initiatives in this area of issues and their efforts to intervene in policy making to mitigate environmental degradation, environmental threats such as deforestation or acid rains and the underdevelopment nexus are based on wide-ranging cooperation with academia.<sup>12</sup>

The first Post-conflict Environmental Assessments (hereafter, PCNA) were carried out in 1999 shortly after the Serbia–Kosovo conflict, when the bombing of industrial sites, military bases and public infrastructure raised concern about a potential environmental catastrophe (particularly water and air pollution) resulting from the release of toxic chemicals. UNEP's Crisis Management Branch was officially established in 1999, followed by, in 2001, the UNEP's Post-conflict Environmental Assessment Unit. Since then, more than twenty PCNAs have been written and introduced: e.g. for Lebanon, Iraq, Afghanistan, Sudan and Liberia. PCNAs represent the vision of the nexus between environmental sustainability, development and security, whose goal is to help with collecting scientific evidence about the nexus of these three areas of issues in the field, evaluating data, and suggesting solutions with the aim of supporting environmental sustainability. Moreover, they are designed to enable a form of local development that is also based on the use of local and regional environmental resources, and all this by maintaining peace and security in the long-term.

Development efforts and economic growth such as the rapid (re)construction of infrastructure or booms in the extraction industry and efforts to strengthen food security

for a rising population can sharply contrast with the goals of environmental protection and sustainability. This has been experienced in many countries and regions (e.g., coastal China, Romania, Nigeria and Angola). PCNAs are designed to responsibly evaluate the nexus between environmental sustainability and the chance for development and security, and to propose appropriate strategies for enabling long-term development and the positive interplay of all three sectors.

Scrutiny of the existing PCNAs (e.g. Afghanistan (UNEP 2003), Albania (UNEP 2000), Sudan (UNEP 2007), Côte d'Ivoire (UNEP 2015)) shows that the PCNAs aim to develop the whole-of-government approach based on transparent and good governance, to make all three goals – environmental sustainability, security and development – compatible, and to capitalize on the linkages between environment, peace-building and conflict prevention. All assessments also clearly indicate that adequately reacting to the interdependence between environmental sustainability, security and development requires the coordinated and integrated approach of domestic and international bodies, including non-governmental organizations and development agencies.

## 5 Summary and conclusions

Scientific knowledge, as well as lessons learned from the field, offer evidence that interdependence exists between the state of the environment, underdevelopment and poverty, and the security situation. Rash projects that take into consideration only one area of issues may have extensive and irreversible effects on other areas, and in some cases might even create local unrest and conflict. Although development projects such as large dams, hydroelectric power stations and high-voltage power networks increase the production of electricity, reduce the number of blackouts and enable industrial development, they may also irretrievably change the landscape (e.g. annihilate wetlands and destroy rain forests), eradicate endemic species, increase CO<sub>2</sub> emissions and also force the resettlement of local populations, changing not only the lifestyles of local communities, but also ethnic and religious maps.

The rise of knowledge about the interdependence between the state of the environment, access to natural resources and the development and security situation have resulted in innovative approaches in science as well as policy making. Numerous scientists have suggested that environmental scarcity and the need for sustainability should not be a source of conflict but rather a source of cooperation, arguing that environmental issues must be dealt with in coordinated ways; in other words, a unilateral approach has only negligible effects. Environmental cooperation is thus needed. Environmental cooperation may be the bridge between conflict communities and the way to strengthen development, as well as security. These ideas have been widely reflected in international politics. Since the end of the 1990s an increasing number of frameworks, initiatives and projects have been implemented that have operationalized the nexus between environment, development and security. Environmental assessment has emerged as a practical

methodology and practice of evaluating this nexus and its effects in particular issue areas and policies.

The pioneer of this approach has been UNEP, which, based on needs and on lessons learned, has established several types of assessment mechanisms. Post-Conflict Environmental Assessment is the mechanism specifically designed for use in parallel with peace-building, development and environmental sustainability efforts. This mechanism has already been used in more than twenty countries; assessments have been introduced for Sudan, Afghanistan, Bosnia and Lebanon, to name just a few. These assessments indicated that good and transparent environmental governance and cooperation about environmental issues are prerequisites for development as well as security in the long-term, and that there will be no environmental sustainability without a sensitive approach to development and the careful maintenance of peace.

#### Notes:

<sup>1</sup> UNEP (the United Nations Environment Programme) is an agency of the United Nations which coordinates the organization's environmental activities and assists developing countries to implement environmentally sound policies and practice.

<sup>2</sup> Coltan is a metallic ore, the base material of tantalum which is widely used in the manufacture of batteries for electric cars, capacitors, and other electronic products.

<sup>3</sup> UNEP (2019): "Environmental Cooperation for Peacebuilding". Available at: <http://web.unep.org/regions/rolac/environmental-cooperation-peacebuilding> (15 March, 2019).

<sup>4</sup> OSCE: The Organization for Security and Co-operation in Europe is the world's largest security-oriented intergovernmental organization. Its mandate includes issues such as arms control, the promotion of human rights, freedom of the press, and fair elections.

<sup>5</sup> NATO: The North Atlantic Treaty Organization, also called the North Atlantic Alliance, is an intergovernmental military alliance between 29 North American and European countries.

<sup>6</sup> ADB: The African Development Bank Group or *Banque Africaine de Développement* is a multilateral development finance institution.

<sup>7</sup> GMS CEP: The Greater Mekong Subregion Core Environment Program.

<sup>8</sup> IUCN: International Union for Conservation of Nature.

<sup>9</sup> ICIDI: Independent Commission on International Development Issues.

<sup>10</sup> WCED: World Commission on Environment and Development.

<sup>11</sup> UNDP: United Nations Development Programme.

<sup>12</sup> For more, see <http://www.envsec.org> (15 March, 2019).

<sup>13</sup> See above, and also <https://environmentalpeacebuilding.org/about/> (15 March, 2019).

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## Local Development Projects and Security Strategy: The Security-development Nexus in the Post-9/11 Period

ŠÁRKA WAISOVÁ & LADISLAV CABADA

**Abstract** Since the 1990s, security as well as development experts have been accentuating the links and relations between security and development. The security-development nexus is a policy framework that combines the need for security with striving for development, and there are a variety of interpretations of the interdependence between the two concepts. The security-development nexus has also found its application in practice, and has led to profound changes in the military as well as development strategies and practice at the national as well as international level. There are an increasing number of projects and programs in which security and development are closely connected. Consequently, the agents and stakeholders in charge of security and development have to implement institutional, organizational and managerial changes, and the budgeting of security and development policy has to be transformed.

**Keywords:** • security • development • security-development nexus • development projects as security strategy • counterinsurgency

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## 1 Introduction

As with many other countries, Canada is engaged in the reconstruction of Afghanistan. In particular, the Canadian Provincial Reconstruction Team is engaged in Kandahar province, where several projects are being carried out. One of the largest and most expensive of these was the reconstruction of the Dahla dam<sup>1</sup> and irrigation system in the region. The project was organized and financed by the Canadian International Development Agency (hereafter, CIDA).<sup>2</sup> The aim of the project was to improve the chances of the local population in sustainable agriculture by reducing their dependence on the vagaries of the weather. The dam was also intended to support many new jobs and decrease the frequency of blackouts, which in turn would increase economic activity. These efforts were also aimed at decreasing the number of people who grow opium poppies and cooperate with insurgents, who are often the only economic partners of local communities (GoC<sup>3</sup> 2009).

After 2008, dam reconstruction work slowed down when the security situation in the region deteriorated. The number of insurgency-related attacks increased and several participants of the dam building project were killed. Even after the dam and irrigation system were finished, the situation in the region did not change very much. The Afghani company contracted by Canadian government and responsible for the security of the dam attacked in 2010 the CIDA's employees, engineers as well as humanitarian workers. Consequently, the Canadian government decided to withdraw all CIDA's people. The dam is currently being patrolled by international forces as well as Afghani soldiers, but the risk of terrorist attacks on the facility is high. The dam and the connected irrigation system represent a potential source of profit for the local population which could increase their economic independence, creating a "perfect target" for the Taliban (GoC 2009; Potter 2010).

To sum up and evaluate the case, the reconstruction of the dam was aimed at assisting the local population and making the lives of local people easier and more independent of the insurgency. During the reconstruction work the environment was so insecure that civilian workers had to be closely guarded by soldiers and by private security companies. Later, the opening of the dam and the commissioning of the irrigation system became the source of a new concern: that the dam could become the target of a terrorist attack. Furthermore, the destruction of the dam could cause a devastating flood in neighboring villages. The Dahla dam case clearly shows how closely development and security issues are connected. However, the idea that development and security, are interconnected, or even interdependent, is relatively new. It first emerged at the end of the 1980s in several reports (e.g. in the report of the Brandt Commission<sup>4</sup> and in a report by a commission led by O. Palme<sup>5</sup>). However, it was not until the middle of the 1990s that this was reflected in practical policies.

In the 1990s numerous humanitarian crises, genocides and civilian conflicts erupted and the international community was challenged with the question of how to effectively deal with such crises and assist the affected population. Operations in Haiti, in Somalia, in Bosnia and Herzegovina, and Rwanda – to name just a few – opened up a debate about reconstruction and stabilization efforts and created the first experiences and lessons about the integration of security and development issues, and also about how to use armed forces in humanitarian reconstruction operations. Underdevelopment was accented as being one of the top sources of stress and unrest, and since the 1990s underdevelopment has been listed as among the threats to security (UNDP 1994). Awareness about the nexus of security and development was first raised within the UN<sup>6</sup> (such as in the UN Secretary General report “An Agenda for Peace” and in the Human Development Report (1994) published by UNDP<sup>7</sup>); later, it emerged in the policies of the main donors and on the agendas of international organizations (e.g., IMF,<sup>8</sup> the World Bank, the OECD<sup>9</sup> and the EU<sup>10</sup>) (Hughes 2009; Lambach 2006; Picciotto 2010; World Bank 2011).

The re-formulation of the security-development nexus is still not complete. Since 9/11<sup>11</sup> more and more has been said about the need to continue implementing development projects even in insecure environments because underdeveloped and poor communities are prone to insecurity and to collaboration with terrorists and insurgents who are often the only “employers” in an area. The reconstruction of Afghanistan and Iraq, and particularly the conception of Provincial Reconstruction Teams, has confirmed that the security-development nexus is a reality. The struggle for justice, prosperity and security has started to be understood as one activity, and the separation of development from security has become less likely after experiences from Afghanistan and Iraq (Picciotto 2010). As a consequence, development has become a security strategy. Development projects are used in insecure areas to win the hearts and minds of local population and have become an integral part of counterinsurgency and counterterrorism activity (USJFC 2010).

As demonstrated, the security-development nexus has been on the international agenda for more than two decades, but the topic is still not well analysed and understood. This fact is demonstrated well by the meeting of a World Bank expert panel in April 2018.<sup>12</sup> The panel was designed “to improve the understanding of the relationship between security and development and enhance collaboration across the humanitarian, development, peace and security sectors” (World Bank 2018).

Considerations and reflections about the security-development nexus include a variety of ideas, concepts, approaches and interpretations that have very different practical implications. The present paper has three parts. The first part offers a state-of-the-art review of the literature on the security-development nexus, while the second part pays attention to the different practical implementations of the security-development nexus. The third part contains reflections and thoughts about the evidence surrounding (and

changes in) the security-development nexus, and presents ideas about its future development.

## 2 Reflections on the security-development nexus in the contemporary literature

The security-development nexus is a policy framework that combines the need for security with striving for development (Brinkeštam 2012). The major contemporary considerations about the security-development nexus are based on the assumption of the interdependence of development and security: the fact that security enables development, and that development is a prerequisite of security. Furthermore, we can also identify a dominant interpretation that underdevelopment, poverty, fragility and instability in the Global South<sup>13</sup> may constitute a threat to the security of the Global North.<sup>14</sup> Even though the security-development nexus is a rather widely accepted perspective today, scholars, experts and policy-makers differ about which of these (i.e. security or development) comes first, and how to tackle the problem on the ground. Scrutiny of the contemporary literature and policy documents makes it evident that there exist at least three interpretations of the relationship between security and development:

- *Security first.* This attitude originates in the idea that the existence of a secure environment is a prerequisite for development; i.e. that insecurity and a dangerous environment negatively influence economic-, political-, social- as well as human development, and reproduce poverty. Any form of development needs a safe, working environment. In other words, security is a component of governability. Representatives of this attitude include Etzioni (2007) and Dobbins (2008), and in politics the European Commission (2018) and OECD DAC<sup>15</sup> (2004) – to name just a few.
- *Development first.* This attitude originates in the idea that development decreases stress and the risk of conflict. Development is a prerequisite of security, while poverty and underdevelopment are sources of insecurity and conflict, and development policy is the instrument for strengthening security. Development assistance is thus aimed not only at supporting development, but preventing conflict and violence. In other words, development is a technique of governability, and security is one of the aspects and consequences of development. Among representatives of this attitude we can identify, for example, the World Bank (2011), the European Union (2017), and scholars such as Brainard and Chollet (2007) and Collier *et al.* (2003).
- *Development and security go hand in hand.* This attitude does not prioritize either development or security, but understands both as interdependent. Development and security must be supported jointly and may affect each other positively as well as negatively. This approach is represented by human security advocates such as the UNDP (1994), for example, and in academia by Duffield (2001), among others.

These three interpretations are equally often present in the security-development debate and fundamentally influence the conceptualization and implementation of the security-development nexus in practice.

### **3 Various implementations of the security-development nexus in practice**

Awareness of the security-development nexus appeared in international politics more than two decades ago and has since then been translated into numerous documents, projects and practical policies. These practical steps and activities in the field reflect the variety of understandings of the interdependence between development and security. Scrutiny of the practical implementations of the security-development nexus can provide useful hints for better understanding the different facets of the interdependence between security and development and also the potential critical points in situations when development and security are linked. In the next section the various practical implications and consequences of the security-development nexus will be introduced and scrutinized.

#### **3.1 The emergence of stabilization and reconstruction operations**

Security and development policies are interdependent, as increasingly demonstrated by the increasing awareness of the security-development nexus in a wide range of projects. Many states, policy makers, experts, bureaucrats and armed forces have been engaged in international humanitarian, reconstruction and peacebuilding missions in recent years in the form of operations undertaken in weak, underdeveloped and risky areas. The crucial moment seems to have been the international engagement in Iraq and Afghanistan. Each country that has Provincial Reconstruction Teams in each of the respective countries has to take a stance on the security-development nexus and has been challenged when debating the topics of foreign security and engagement with development at home. A number of policy makers and state representatives have agreed that “in this world it is impossible to draw neat, clear lines between security interests, (our) development efforts and democratic ideals ... Diplomacy must integrate and advance all of these goals together” (Rice 2006). Experiences from the reconstruction of Iraq and Afghanistan, but also the Solomon Islands, Haiti, Somalia and Bosnia and Herzegovina, have shown that military security (or generally, the establishment of security) goes hand in hand with social and economic reconstruction, democratization and good governance. All the lessons learned from post-conflict operations originate in so-called stabilization and reconstruction politics. Stabilization and reconstruction politics as a new approach have emerged in many states, including the United States, United Kingdom and Germany, but also in smaller countries with limited international engagement (e.g. the Czech Republic, which had its own Provincial Reconstruction Team in Logar/Afghanistan).

What stabilization and reconstruction policy consist of, and how this policy area is connected with security and development policy, will be demonstrated and analysed using the case of the United States. The US model of stabilization and reconstruction

policy, including counterinsurgency and counterterrorism strategies, has become the model for many other countries and thus may be considered a representative case.

The United States established stabilization policy as a reaction to robust counterinsurgency interventions in Iraq and Afghanistan, and the lessons learned from these two countries were used to build a model stabilization policy. The US model is based on a merger of diplomacy, security and development policy which was followed by institutional and organizational changes in all three policy sectors. The reform included the transformation of relations and processes of cooperation between the Department of Defense (hereafter DOD), the State Department,<sup>16</sup> the National Security Council, and the US Agency for International Development (hereafter, USAID). Changes in the tasks of the US army and the emergence of a new conception of civil-military relations have been reflected in changes of the tasks of USAID, followed also by changes in the USAID budget and later by changes in the law on development assistance.

The peak of the reforms – that also demonstrated the merger of all sectors and coordination requirements – was the establishment of the post of Coordinator for Reconstruction and Stabilization Operations in 2004, which in 2009 evolved into the Bureau of Conflict and Stabilization Operations (hereafter, CSO). The goal of the Bureau is “to help U.S. diplomats prevent, respond to, and recover from conflict which disrupts and undermines long-term development and capacity building ... [and] brings partners and State Department capabilities together to assist, identify, and implement policy ...” (CSO 2017). The Bureau works as an inter-departmental group which connects people and projects from the State Department, DOD,<sup>17</sup> USAID,<sup>18</sup> the Ministry of Justice, the Ministry of Trade, and the Department of Homeland Security. People from the Bureau of Conflict and Stabilization Operations plan projects in the framework of the security-development nexus, advise when stabilization and reconstruction teams are needed and how they should be localized, and also track the situation in different parts of the world to identify potential threats to the United States and when to engage in stabilization operations.

In cooperation with the National Security Council, the Bureau has created the Inter-agency Management System for Reconstruction and Stabilization, and all departments and governmental agencies are obliged to co-operate with this institution. In order to support stabilization and reconstruction activities, a special budget for stabilization operations has been created. The budget has been managed by USAID and used to finance quick-response projects such as the operations of provincial reconstruction teams in Iraq and Afghanistan, counterinsurgency operations that include projects to win hearts and minds of local populations, and projects for training the Afghani national army.

In 2016, impact assessments of stabilization initiatives were made public and in 2018 the first ever Stabilization Assistance Review<sup>19</sup> was published together by the State Department, USAID, and the Department of Defense. When USAID introduced the

review it stated that “stabilization includes restoring basic services such as water and electricity ... in certain situations, none of [the former] can be accomplished without help from the military ... DOD also helps USAID and State get into areas it would not be able to go into without additional security” (Welsh 2018). As is evident from the information above, DOD, the State Department and USAID have been the key players by concurrently DOD participating in civilian and development projects, and USAID in counterinsurgency and counterterrorism operations.

The connection of security and development in stabilization and reconstruction policy has influenced the work and organizational structure of USAID and the US Army. Under stabilization and reconstruction operations the intensity of civil-military cooperation has increased (e.g. joint action with USAID or cooperation with non-governmental organizations that are implementing USAID projects) and new military training which has enabled the integration of civilians into military structures was introduced. The US Army received the new task of participating in critical infrastructure building, supporting good governance, elections, free media, and the rule of law and security sector reform. The growing number of stabilization and reconstruction operations and the lessons thereby learned have also been reflected in strategic documents. In particular, the National Defense Strategy of 2005 explicitly speaks about the importance of civil-military cooperation in the fight against the enemy. Civil-military cooperation has become the cornerstone of the counterterrorism and counterinsurgency operations of the US Army.

Not only has the US Army been transformed, but profound changes have been made to the organizational and institutional structure of USAID and the relationship between USAID, the US Army and other governmental departments. Within USAID, an Office of Civil-Military Cooperation was established and USAID officers now sit in US unified combatant commands planning and coordinating cooperation between DOD and USAID. These changes have been framed by the National Security Strategy 2002, in which development is thought of as one of three pillars of US national security. Consequently, USAID issued the report *Foreign Aid in the National Interest. Promoting Freedom, Security, and Opportunity*. The report declared development assistance to be a strategic instrument of US foreign policy which facilitates the maintenance of US national security and international peace (USAID 2002). The changes have also affected the system of cooperation with third parties, and of grant giving. USAID, based on the Acquisition and Assistance Policy Directive<sup>20</sup> (also called Anti-Terrorism Certification), primarily prefers to collaborate with and to support organizations and states that fight against terrorism (Moss *et al.* 2005).

To sum up, there presently exist collaborative relations in the triangle of organizations the State Department, USAID and DOD; moreover, there also exists close cooperation between the US Army and USAID framed as civil-military operations. The US Army and USAID carry out local development projects with the aim of assisting local communities

to establish good and transparent governance and build relations between the population and political representatives, and to win the hearts and minds of local people; i.e. to decrease support for insurgency and related economic activity. In implementing local development projects, USAID needs military assistance to protect civilian employees, and the US Army hopes to use USAID's projects, money and expertise as part of a complex counter-insurgency and counter-terrorism strategy.

### **3.2 The pooling of resources and the use of development budgets for security goals**

As indicated in the case of the United States, the security-development nexus has affected not only the organizational and institutional structure of the branch of development and security, but has also had a deep impact on budgeting. This transformation in budgeting has been called the “pooling of resources”. It includes the merging of budgets into one “bag” and using development – traditionally civilian – budgets for security and military purposes, typically in stabilization and reconstruction operations.

The pooling of resources takes place not only in the US but has also occurred in Canada, Great Britain and in the Czech Republic, to name just a few examples (DFAIT<sup>21</sup> 2006; DFID<sup>22</sup>, FCO<sup>23</sup> and MOD<sup>24</sup> 2003). The pioneer of the pooling of resources based on the security-development nexus was actually Canada. The first integrated Canadian budget was introduced in 1991 and called the International Assistance Envelope. This budget merged all development projects and resources of all governmental agencies with the aim of improving human security. During that time, human security was Ottawa's key foreign policy goal (Waisová 2009). The construction of the integrated development budget continued even when Canada abandoned a human-security-focused policy. The basis for the further pooling of resources was the need to meet the demands of the OECD Development Assistance Committee concerning the effective use of resources and to implement a so-called “whole-of-government approach” (CIDA<sup>25</sup> 2007, 2008 and 2009).

For our analysis, it is important to trace and evaluate the security-development nexus as a framework for pooling resources. In the case of Canada, the main transformations may be observed in the development budget after Canada became engaged in Afghanistan. Since Fiscal Year 2004–2005 the ministry of defense has been the first governmental body with permission to use funds from the Integrated Assistance Envelope, and since then initiatives such as Disaster Assistance Response Teams, provincial reconstruction teams, rapid response teams, stabilization and reconstruction operations and counterinsurgency and counterterrorism operations have been covered from it (CIDA 2007, 2008 and 2009). Since 2006 the Global Peace and Security Fund, a part of the Integrated Assistance Envelope, has been working to collect financial resources for operations in weak and failing states where the Department of Defense does not have a presence, and which are not beneficiaries of Canadian development assistance. This fund is managed by the Stabilization and Reconstruction Task Force and is used to finance –



among other things – demining, demilitarization, transitional justice, and reconciliation tasks (DFAIT 2006). The purpose of the Stabilization and Reconstruction Task Force is to advance Canadian peace and security priorities in complex political-security crisis situations in fragile and conflict-affected states (GPSF<sup>26</sup> 2018).

Not only in Canada has the pooling of resources – particularly the use of development budgets for security and military purposes, and the opening up of development budgets for the armed forces – become the norm rather than the exception. As will be demonstrated and analysed below, the door for such transformations was clearly opened by OECD DAC<sup>27</sup> when it changed the definition and guidelines of development assistance in 2007.

#### **4 The new security role of international financial institutions**

The security-development nexus has not only had an impact on foreign policy and domestic policymaking. The linking of security with development – or rather insecurity with underdevelopment – occurred within the United Nations, as well as on the agendas of international financial institutions, particularly the World Bank. While the UN is and always was the primary body with security issues on its agenda, the World Bank has always been the first and foremost financial body. In the World Bank's documents, development has traditionally been defined in socioeconomic terms and security issues have tended to be ignored. The condition for countries to receive World Bank assistance was that there should be no war and violence in the country. However, since the beginning of the 1990s World Bank policy has started to change, and issues such as governance and the impact of development projects on the security situation have risen on its agenda.

The decisive moment was the Middle East Peace Process and war in Former Yugoslavia. Based on the Oslo Peace Accords, the World Bank administered financial resources for the reconstruction and development of the Gaza Strip and of the West Bank. When war in Former Yugoslavia erupted, the European Commission asked the World Bank to participate in the post-conflict reconstruction of Bosnia and Herzegovina. In 1995, the Bank led a joint mission (with the IMF, the European Commission and USAID) to finally meet the reconstruction needs of Bosnia, while later it managed the Trust Fund for the country. In both cases, the bank found itself in an unusual position; it developed special relations on the ground, received excellent information about the situation, and was challenged by security and post-conflict issues (Schiavo-Campo 2003).

In the 1990s, the number of conflict or post-conflict countries where the Bank had projects increased (Rwanda, Sierra Leone, Angola, Croatia and Cambodia, to name a few) (Holtzman *et al.* 1998). These experiences profoundly changed the Bank's role in security issues and led to transformation of the Bank's agenda. Institutional changes such as the establishment of the special Post-Conflict Unit, of the Framework for World Bank Re-engagement in Post-Conflict Reconstruction, and a special fund for post-conflict

countries were introduced. The Bank's resources were used to finance the demobilization and reintegration of child soldiers, demining and the rehabilitation of community life, to name a few initiatives (Van Houten 2007).

At the beginning of 2001, the Bank accepted an operational policy called "Development cooperation and conflict" as the guiding principle for future programs. The basic idea embedded in this policy was that underdevelopment may be a source of insecurity and conflict, and that via development assistance peace and security may be supported. Consequently, the post-conflict reconstruction unit was expanded with a bigger budget and greater human capacities and awarded a mandate to participate in conflict prevention and resolution (Bannon 2005). The Bank started to engage with countries which were not eligible to receive standard development assistance because they were undergoing conflict. Significant impact on the change in the Banks' motivation for development assistance and also in the implementation of development projects originated in the findings of the World Bank's research team led by P. Collier. Collier and his colleagues formulated the concept of the so-called "conflict trap". This term describes the pattern of repeating civil wars; Collier and his team also assumed that civil wars are associated with economic problems and mistakes in development policy, and when such mistakes are eliminated and problems solved, a path out of the conflict trap may emerge (Collier *et al.* 2003).

A milestone in the acceptance of the security-development nexus was the 9/11 terrorist attacks and the consequent World Bank engagement in Iraq and Afghanistan. The Bank's representatives argued that it is not poverty that leads to terrorism, but rather weak governance and failing state institutions that create a haven for terrorists (Bannon 2005). By the end of 2001, the Bank had created so-called LICUS initiative (Low Income Countries Under Stress) and framed the initiative with the motto "[the] eradication of poverty is the way to global security" (Bourguignon 2005). In 2004, LICUS was awarded a special budget, not for classical development assistance, but to finance project-supporting good governance, the rule of law, social services and peacebuilding, including security sector reform and the demobilization of soldiers.

The symbolical peak of the security-development nexus transformations in World Bank's agenda was the annual report from 2011 entitled "Conflict, Security, and Development". The Report concludes that 90 per cent of the civil wars which have started since the end of the 1990s have emerged in countries with previous experience with civil war or violence (the conflict trap) and the biggest challenges for development are avoiding this conflict trap and new forms of violence such as insurgency and civil wars. The first step in fostering development is the provision of security – without security there can be no development, but security can hardly be improved without development, which is why development projects also need to be implemented in countries in conflict (World Bank 2011, 2, 5 and 41). The report declares that it is necessary "to apply security-development linkages in all areas struggling to prevent large-scale political or criminal violence"

(World Bank 2011, 28). The subsequent World Bank projects respected the trend created by the 2011 Bank report.

To sum up, the penetration of the security-development nexus into politics and on the agendas of international bodies has gone global, and even organizations with no security goals on their agendas have accepted it as the basic framework for their projects. How far the security-development nexus has changed international financial institutions is clearly demonstrated in the case of the World Bank. In less than one decade, the Bank became an important and qualified partner of the UN, NATO,<sup>28</sup> the EU and several states in conflict-affected and post-conflict areas using development assistance and particularly local development projects to prevent violence and to bridge the conflict trap. In several conflict-affected areas it would hardly be possible to engage in reconstruction and to build a peaceful working domestic system without the World Bank's engagement (Schiavo-Campo 2003).

#### **4.1 A new definition of development assistance**

As indicated above, the implementation of the idea of the security-development nexus has brought about the transformation of security policy, as well as of development assistance. The cases of the World Bank, Canada, and the United States also demonstrate the fact that donors have profoundly changed their approaches over the last two decades. While shortly after the end of the Cold War the criteria for receiving development assistance was poverty or humanitarian need and the absence of violent conflict, at the beginning of the new millennium the biggest donors were stressing the need to use development assistance for various security purposes, while a situation of peace in the country was not required (Brzoska 2008). These developments even caused several representatives of the least developed countries to become skeptical; they complained that to qualify for development assistance or international loans their countries had to be undergoing violence. In other words, the international post-9/11 discourse led to a disadvantage for poor but peaceful countries, because the chance of countries in conflict receiving assistance was much greater (World Bank 2011). These transformations were not only reflected in projects on the ground, but started to be reflected in the basic framework that regulated the provision of development assistance.

The key role in the transformation of the framework regulating development assistance was played by the OECD Development Assistance Committee, the body that gathers together the biggest donors. The DAC member countries have been debating the security-development nexus since the middle of the 1990s when human security entered international politics as an issue. Human security was discussed as the possible framework for the Millennium Development Goals, and the future guiding principle for DAC activities (OECD 1997, 2001 and 2004). Although the concept of human security did not become the final principle of development assistance, the debate made it clear that DAC accepted the claim to a link between development and security.

The debate involving the security-development nexus in development assistance principles continued in the post-9/11 period when several big donors were operating provincial reconstruction teams in Iraq and Afghanistan and wanted to use development budgets for their activities. The DAC member countries articulated that the big problem was weak and failing states. While in the 1990s weak and failing states were understood as a problem for their citizens and as a barrier to local development, in the post-9/11 period weak and failing states were considered to be a haven for terrorists and insurgents, and as a threat to international security (Duffield 2006; Brzoska 2008). Consequently, within DAC security was interpreted as a prerequisite for development (OECD 2004). Changes in understanding development and development assistance were completed in 2007 when a new directive defining what could be financed from the development budget (i.e. what may be understood as development assistance) was issued by OECD DAC. Since 2007, budgets for development assistance may be used, for example, for the management of security expenditure, for an increase in the role of civil society in the democratic control of military forces, for assistance to child soldiers, for security sector reform, for demining and also for the activities of provincial reconstruction teams (OECD 2007) (Box 1).

**Box 1:** Official Development Assistance Reporting Rules – what donors may report as development assistance

*Technical co-operation provided to parliament, government ministries, law enforcement agencies and the judiciary to assist review and reform of the security system to improve democratic governance and civilian control ... Participation in the post-conflict peace-building phase of United Nations peace operations (activities such as human rights and elections monitoring, rehabilitation of demobilized soldiers, rehabilitation of basic national infrastructure, monitoring or retraining of civil administrators and police forces, training in customs and border control procedures, advice or training in fiscal or macroeconomic stabilization policy, repatriation and demobilization of armed factions, and disposal of their weapons; support for landmine removal) ... Reintegration of demobilized military personnel into the economy; conversion of production facilities from military to civilian outputs; technical co-operation to control, prevent and/or reduce the proliferation of small arms and light weapons.*

Source: OECD (DCD/DAC) (2007).

The changes in development assistance principles and guidelines and budgeting clearly demonstrate the penetration of the security-development nexus into policy-making frameworks, norms and rules. Consequently, they have led to the spread of the security-development nexus within DAC member states, and also beyond. Reflections about the security-development nexus on the formal, normative level indicate that the changes have not been ad hoc, short term and situation specific, but rather deep, based on long-term political interests and the consensus of the biggest donors.

## 4.2 Armies as agents of development

Armed forces have usually been not the agents of development assistance, but the participation of militaries in development projects is not entirely new. In several countries (Sri Lanka, Nepal, India and Ghana) military forces have traditionally been vehicles for development and innovation diffusion at home. Armed forces may build infrastructure, offer education and health care, and transfer skills and knowledge. However, use of the army as an agent of development is rather uncommon at the international level.

One of the first experiences of military forces as agents of development assistance entered world politics in the 1990s. Several international peace operations (Bosnia and Herzegovina, Rwanda, and Sierra Leone to name a few) undertook local humanitarian and development activities and assisted when local development projects were created. Soldiers engaged in UN operations participated in the building of hospitals, demining, demobilization, and the social reintegration of former combatants, the reconstruction of basic infrastructure and healthcare systems, etc. However, the milestone was international engagement in Iraq and Afghanistan. As Duffield (2006, 30) comments:

*... during the 1990s, the military doctrine among leading states was to support civilian humanitarian agencies and to only become directly involved in humanitarian activities as a last resort. Since Kosovo, and especially Afghanistan, this situation has changed. Humanitarian assistance ... has increasingly been colored by political considerations. In Afghanistan as well as Iraq, humanitarian assistance, development and social reconstruction have been redrafted as a legitimating support for transitional state entities and their transformation into show-case examples of regional stability. This places tremendous responsibilities upon cooperating aid agencies and draws them directly into an ex-posed political process. At the same time, due to widespread insecurity and insurgency violence, the military has moved beyond protection and become directly involved in activities it labels as 'humanitarian'.*

The developmental role of the military forces was for many military representatives very new and in many cases the military structures did not have time to prepare for it; when international forces came to Iraq and Afghanistan, local bureaucrats and policy makers from ministries disappeared overnight (Interview with Petr Voznica,<sup>29</sup> 20 May, 2011, Ljubljana/Slovenia) and international forces, wanting to maintain the operation of state structures and a minimal rule of law, had to at least temporarily carry out civilian tasks. In several cases international forces were the only actors with the human resources, skills and infrastructure to deliver social services, including transferring money (salaries for civil servants) into remote areas (Box 2).

**Box 2:** The US Army's tasks in Afghanistan

*KUNAR PROVINCE, Afghanistan, September 22, 2011 Approximately 60 Soldiers from across Illinois, as well as two Soldiers from Michigan and South Dakota respectively, have been deployed to Kunar province since June with the Illinois Army National Guard's 1–14<sup>th</sup> Agribusiness Development Team.*

*The Agribusiness Development Team, or ADT ... have been assisting the Government of the Islamic Republic of Afghanistan in revitalizing and establishing a strong, growing and sustainable agriculture industry.*

*The Illinois team's mission is part of a broad effort that involves multiple National Guard ADTs from several states, each operating within its own province. The teams typically come from mid-western states, such as Missouri, Nebraska, Indiana and Iowa, which are known for agriculture production ... The Illinois soldiers have educations and backgrounds in agronomy, plant and soil science, forestry, engineering, pest management, zoology and hydrology ... All this expertise is critical for ADTs to operate in a country where the agricultural sector has suffered setbacks in the form of a Soviet military occupation, a civil war and devastating droughts over the past 30 years. While training is one key element of the ADT mission, the team also promotes sustainability by providing aid to Afghan entrepreneurs who wish to start or expand agribusinesses that have a positive impact on the local economy.*

Source: US Army (2019).<sup>30</sup>

The change in the role and activities that military forces have experienced during the last two decades have resulted in transformations at the strategic, organizational, and conceptual level; strategic military documents have been penetrated by the security-development nexus, civil-military units and civil-military rapid response teams have been created, and several armies (the US and Canadian Army, to name a few) have adopted a three-block model of war which seeks to combine the delivery of humanitarian aid with peace support operations and high-intensity fighting (Dorn and Varey 2008).

Changes in military operations and tasks have not been without criticism. The local development engagement of armed forces has been criticized because soldiers may not be trained for such activities, or as a waste of military money and capacity. Proponents of the developmental engagement of armed forces have argued that when the military is the only agent that is able to support local development projects, then it has to do it, and when support for local development seems to be the way to win the hearts and minds of the local population and to decrease support for insurgent and terrorist groups, it is also necessary to pursue this option. Irrespective of the position, the transformation of the role of the military forces according to the security-development nexus is the reality in many countries today.

## 5 The security-development nexus: conclusions

Development and security, underdevelopment, poverty and insecurity, security policy and development assistance – all these topics were traditionally understood as independent areas of issues. Similarly, the actors engaged in development assistance and in security policies were rarely linked. Development agencies and humanitarian/development non-governmental organizations supported education, health care, or construction-based infrastructure projects such as dams, irrigation systems or rails and roads. Armed forces trained for military operations, defended countries, or fought in wars.

The situation has changed since the beginning of the 1990s, and security as well as development experts have accentuated the links and relations between security and development. A focus on the security-development nexus is no exception today; it is rather part of the mainstream in terms of security as well as development studies. However, there are variety of interpretations of the nature of the interdependence between development and security, or underdevelopment, poverty and insecurities respectively: different actors use different approaches and interpretations which consequently influence the penetration of the security-development nexus into politics and its implementation on the ground. As demonstrated and analysed above, there are at least three approaches to the security-development nexus: “security first,” “development first,” and “security and development hand in hand”.

All three approaches have found their application in practice and have led to profound changes in the military, as well as in development strategies and practice at the national as well as international level, and have deeply influenced the institutional, organizational and managerial background of security as well as development assistance. As is evident from the data and information presented above, there are some trends in the application of the security-development nexus. While a few decades ago countries in conflict did not meet the criteria for development assistance, today violence and conflict may even contribute to the fact that states qualify for development assistance. Development assistance, particularly local development projects, are not only tools for supporting local communities, but are used as counterinsurgency and counterterrorism tools. In other words, local development projects have turned into components of security strategy.

Last but not least, security and development assistance agents have also experienced these profound changes and transformations. Development agencies and bodies work in insecure and conflict-ridden areas in cooperation with military forces, while military forces carry out civilian tasks that were traditionally outside their area of responsibility. All the evidence and changes indicate that the security-development nexus has become the norm rather than the exception, and is now the approach for managing global challenges and local insecurities. In all probability, the next decade will not bring any

revolutions in the security-development nexus, nor a divorce between security and development.

### Notes:

<sup>1</sup> The Dahla Dam is the second largest in Afghanistan, built in 1952 on the Arghandab River. It was rehabilitated between 2008 and 2012 with assistance provided by the Government of Canada.

<sup>2</sup> CIDA does not exist anymore as an independent body. In 2013, the government of S. Harper decided to incorporate the independent agency into the ministry of foreign affairs, arguing that this was necessary to improve the coordination and efficiency of Canadian foreign policy. CIDA was also renamed – today it is the Department of Foreign Affairs, Trade and Development.

<sup>3</sup> GoC: Government of Canada.

<sup>4</sup> The Brandt Report was written by the Independent Commission, first chaired by Willy Brandt (the former German Chancellor) in 1980, as a review of international development issues.

<sup>5</sup> UN Independent Commission on Disarmament and Security Issues. The aforementioned report was published in 1982.

<sup>6</sup> UN: United Nations.

<sup>7</sup> UNDP: United Nations Development Programme.

<sup>8</sup> International Monetary Fund.

<sup>9</sup> Organisation for Economic Co-operation and Development.

<sup>10</sup> European Union.

<sup>11</sup> 9/11: The September 11 attacks (also referred to as 9/11) were a series of four coordinated terrorist attacks by the Islamic terrorist group al-Qaeda against the United States on the morning of Tuesday, September 11, 2001.

<sup>12</sup> A panel discussion held on April 20, 2018 at the World Bank Group Headquarters about the relationship between security and development and enhancing collaboration across the humanitarian, development, peace and security sectors to deliver more efficiently and effectively in fragile and conflict-affected settings. Participants: World Bank Group President Jim Yong Kim, General John Allen (Ret.), President of the Brookings Institution, and a panel of high-level guests.

<sup>13</sup> The "Global South" is a term that has been emerging in transnational and postcolonial studies to refer to what may also be called the "Developing World" (i.e., Africa, Latin America, and developing countries in Asia), or "developing countries," "less developed countries," and "less developed regions".

<sup>14</sup> The North–South divide is broadly considered to be a socioeconomic and political divide. Generally, definitions of the Global North include the United States, Canada, Europe, developed parts of Asia (the Four Asian Tigers, Hong Kong, Singapore, South Korea and Taiwan) as well as Australia and New Zealand.

<sup>15</sup> The OECD Development Assistance Committee became part of the OECD following Ministerial Resolution on 23 July 1961. It is a unique international forum of many of the largest donors of aid, including 30 DAC Members. The Asian Development Bank, African Development Bank, Inter-American Development Bank, International Monetary Fund, United Nations Development Programme and the World Bank participate as observers.

<sup>16</sup> The United States Department of State (DOS), often referred to as the State Department, is the United States' federal executive department. This body has the role of advising the president and represents the country in international affairs and foreign policy issues. It is equivalent to the foreign ministry of other countries.

<sup>17</sup> The Department of Defense (DoD, USDOD, or DOD) is an executive branch department of the federal government of the United States charged with coordinating and supervising all agencies



and functions of the government concerned directly with national security and the United States Armed Forces.

<sup>18</sup> The United States Agency for International Development (USAID) is an independent agency of the United States federal government that is primarily responsible for administering civilian foreign aid and development assistance.

<sup>19</sup> The review is available from the website of the US Department of State: <https://www.state.gov/r/pa/prs/ps/2018/06/283334.htm> (15 March, 2019).

<sup>20</sup> Acquisition & Assistance Policy Directive (AAPD) issued by USAID on September 24, 2004. Certification Regarding Terrorist Financing. Implementing Executive Order 13224. Accordingly, entities associated with terrorism are not eligible to funding from USAID.

<sup>21</sup> DFAIT: Department of Foreign Affairs and International Trade (Canada).

<sup>22</sup> DFID: Department for International Development (UK).

<sup>23</sup> FCO: Foreign and Commonwealth Office (UK).

<sup>24</sup> MoD: Ministry of Defence (UK).

<sup>25</sup> CIDA: Canadian International Development Agency.

<sup>26</sup> GPSF: Global Peace and Security Fund (Canada).

<sup>27</sup> OECD DAC: OECD Development Assistance Committee.

<sup>28</sup> The North Atlantic Treaty Organization (NATO), also called the North Atlantic Alliance, is an intergovernmental military alliance of 29 (North American and European) countries.

<sup>29</sup> Petr Voznica, retired Major General of Armed Forces of the Czech Republic, served as the Ambassador of the Czech Republic in Lithuania (2001–2005), Iraq (2005–2009), and Slovenia (2009–2014).

<sup>30</sup> Available at:

[https://www.army.mil/article/66004/agribusiness\\_soldiers\\_focused\\_on\\_afghanistan\\_mission](https://www.army.mil/article/66004/agribusiness_soldiers_focused_on_afghanistan_mission) (15 March, 2019)

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## **Re-thinking Development after Disaster – Notes on Post-earthquake Reconstruction Planning in the Central Himalayas, Nepal**

DIPAK RAJ PANT

**Abstract** This essay is based on a field survey in the central Himalayan highlands, Nepal, badly hit by earthquakes in spring 2015. The affected remote communities have always been constrained by spatial and economic marginality and have suffered not only from the earthquakes but also a number of geophysical hazards and economic problems, including the inexorable outbound migration of young and adult workforce in recent decades. Accordingly, they are one of the most vulnerable communities in Asia. Post-earthquake reconstruction represents an opportunity to reduce their vulnerability, to foster collective resilience, to stop (and reverse) outbound migratory movement by employing local workforce in recovery and reconstruction projects, and to develop a sustainable economy through use of well-targeted economic and fiscal policies and encouragement of entrepreneurial activism. Reducing human vulnerability is key to fostering sustainable economic development after disaster.

**Keywords:** • development • disaster • hazard • resilience • sustainability  
• vulnerability

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## 1 The Himalayan disaster: Nepal earthquake, 2015

Nepal was hit by two strong earthquakes in 2015: the first on Saturday 25<sup>th</sup> April when a very strong tremor (7.8 Richter scale) hit Gorkha district; and a second one (7.3 Richter scale) on Tuesday 12<sup>th</sup> May with an epicenter near the district of Sindhupalchok bordering Dolakha, on the same fault-line, probably as a result of a strong after-shock. The central-eastern highlands and valleys of Nepal were hit, including the capital, Kathmandu. This caused destruction on an enormous scale, affecting the lives and livelihood of millions, and disseminating widespread distress. The earthquake killed and injured thousands of humans and animals. Settlements, infrastructure, geo-hydraulics and ecosystems in the central Himalayas received serious jolts, causing a long trail of destruction and despair. A major natural incident (the earthquake) soon turned into a human tragedy on a massive scale. This disaster re-affirmed the fragility of human habitats in the central Himalayas and underscored the vulnerability of its inhabitants. Two devastating quakes were followed by hundreds of aftershocks and tremors. Tremors continued for months, frightening the already battered population.

**Figure 1:** The epicentres of 2015 earthquakes in the central Himalayas



Source: Pant (2016, 8).

According to Nepalese government records, there were 8,790 human casualties (deaths) and many more (22,300) severely injured. More than half-a-million houses were destroyed, leaving the owners and tenants homeless and internally displaced. It is estimated that the lives of eight million people, a little less than one-third of the total population of Nepal, have been badly affected. Thirty-one of Nepal's 75 districts were struck, out of which 14 high-altitude rural districts were the worst-hit (NPC 2015). In some areas, settlements and croplands were swept away by avalanches and landslides triggered by earthquakes and tremors. It was the worst natural disaster to strike Nepal since the big earthquake of 1934.

## 2 Vulnerability exposure

The 2015 earthquake has exposed the vulnerability of Nepalese people. The magnitude of damage caused by the earthquake is largely a result of pre-existing vulnerabilities. Had these vulnerable conditions been properly addressed long before the earthquake, then the extent of destruction and loss could have been significantly lessened. Vulnerability is a combination of institutional, infrastructural and socioeconomic conditions that limits the ability of people living in hazard-prone areas to withstand, cope with and mitigate the effects of a hazardous event (Blaikie *et al.* 1994).

Emergency relief work and immediate (post-emergency) support systems involve transitional action which is, understandably, carried out speedily, without in-depth analysis. Nepal's emergency response was admirable in the immediate aftermath of the earthquake of 2015. Rescue missions were conducted in every place of distress. Relief materials were distributed. Health crisis (starvation, epidemics) and breakdown in law and order (chaos, anarchy) were avoided. Nepal's security forces worked hard and performed quite well, despite being under-resourced and overstretched in terrain that is very rugged and difficult to work in.

Post-disaster reconstruction is very different from emergency management. In terms of local characteristics, every place has unique post-disaster features, thus effective recovery solutions must be calibrated as per the local circumstances and an assessment of local vulnerability and capability. Post-disaster management demands well-informed policy-making and careful planning. Before committing huge amounts of resources and deploying a wide range of skills for recovery and reconstruction, four sets of knowledge have to be obtained:

- Scientific understanding of all potential hazards.
- Historical memory of previous disasters, and lessons learned from previous post-disaster management.
- Periodical technical assessment of the geophysical, environmental and infrastructural vulnerabilities; and their post-disaster evolution in the disaster-hit habitats.
- Anthropological comprehension of the preexisting institutional and socioeconomic vulnerabilities and capabilities of people affected by the disaster, and of the new risks and uncertainties contributed by the disaster.

Post-disaster recovery is a complex process that involves almost all social spheres and economic sectors and requires close collaboration between public institutions and private actors as well as other agencies (NGOs and international bodies). Close collaboration among all stakeholders helps to grasp local vulnerability. Local communities should be helped through the provision of scientific and technical support to define and manage their own vulnerabilities and capabilities. Aided by technical support from external

agencies, a community-based, contextual and proactive approach to vulnerability is perhaps the best approach (Wisner 2008).

In the aftermath of 2015 earthquake, Nepal's vulnerability due to institutional deficiencies was exposed. The absence of locally elected governing bodies at municipal and district levels proved to be a serious handicap to a timely and systematic reconnaissance of the impact of disaster and for accurate information and data collection. Non-elected state-government teams, charities, security forces, etc. were limited in terms of grasping the details and peculiarities of the local reality. They had difficulty in reaching the grass-roots level. The mobilization of government workers becomes effective only if there is a valid and well-representative local institutional counterpart. The decentralization of the institutional framework is key to delivering relief and reconstruction programs, as well as to ensuring full recovery and economic development after the disaster (Lyons *et al.* 2010).

The void in local governance was a direct result of a long period of political instability caused by bargaining, brokering and bickering among the contenders for power, even after the end of a decade-long (1996–2006) Maoist insurgency. An active institutional counterpart, representing the local community, was not available to coordinate recovery until recently.<sup>1</sup> Even non-elected administrative officers (municipal secretaries) were absent in many villages when the earthquake struck.<sup>2</sup> This was one of the serious limits faced by relief workers in the immediate aftermath of the earthquake. Later, this also caused delays and confusion in terms of fact-finding, planning and providing reimbursement to victims by the newly instituted National Reconstruction Authority (NRA), besides the political bickering and bargaining (i.e., delay) over the composition and nomination of the NRA itself.<sup>3</sup>

In Nepal, the vulnerability of already vulnerable people such as those with physical disabilities, the sick and under-treated, pregnant women, young children, very old persons and single-parent households became worse compared to the pre-earthquake period. Women were particularly hit hard as they were most likely to be busy indoors performing household work when the quake struck. The active adult workforce in Nepal's rural highlands consists mainly of women and the elderly; both suffered badly (many young adults had left their villages long before the earthquake). Political instability combined with poverty and the lack of off-farm opportunities drove away waves of able-bodied natives from the rural highlands to work in the towns and roadside trading posts (*bazars*) of the largest urban conglomerate (Kathmandu valley), and to the urban areas of southern lowlands. A majority ended up in sub-standard periphery (and often unauthorized) settlements. Many have gone abroad to earn money that they can send money back to their families.<sup>4</sup> The absence of the able-bodied during the relief action in the immediate aftermath of the disaster proved a serious problem. Political instability and rural poverty caused widespread socioeconomic vulnerability which has caused the massive exodus of able-bodied youngsters and adults in the recent past. The absence of the able-bodied



rendered the remaining people (mostly women, children and the elderly) even more vulnerable; it added another layer of vulnerability. As a result, the destructive effects of earthquake became disastrous. After the earthquake many more left as the reconstruction process slowed down due to politicking and bureaucratic procedures. The state's offers of compensation and technical delivery proved to be far below the quantity and quality required.

Those most affected by the disaster are farming and herding communities concentrated in the mountainous districts of central-eastern Nepal. Smiths, craft-workers and retail traders have been hit hard. The earthquake has affected people engaged in farming and herding, retail trading, crafts and services, with their fewer properties and lower incomes and with very little means of reconstructing their shelters and livelihood-related structures. Large business structures, usually constructed in reinforced concrete, suffered less physical damage. Small home-based businesses (cottage enterprises) suffered badly, crippling the ability of many to make a livelihood, and making them vulnerable to financial bankruptcy, physical and mental health problems. The 2015 earthquake devastated relatively neglected (marginal) socio-spatial contexts such as the scattered rural hamlets of high-altitude regions and was a disaster for the poor rural folk of mountain districts who already had few material resources and very difficult logistical conditions.

The aftereffects of the earthquake manifested as formidable risks and challenges: more outbound migration of the able-bodied, an increase in pressure on existing facilities and services in urban areas (more slums and shanty-towns), health and safety problems, public security concerns, illicit trade, and further burdens on the shoulders of police and criminal justice offices. Disasters trigger multiple disruptions in civic and economic life. Later, these effects are amplified by further secondary disruptions of livelihoods, critical infrastructure, the supply system, and law and order. Disastrous events involve a long causal chain of crisis and hardship, generating secondary and tertiary disasters from the interaction between anthropogenic and natural elements as “cascading” effects. Careful analysis of such cascading risk is essential to identifying solutions for recovery and resilience-enhancement (UNISDR 2017).

Post-disaster disruption and dysfunctionalities are particularly difficult for vulnerable categories of society, and even more so in politically unsettled and economically weak countries like Nepal. The after-effects of large-scale disasters unfold as a myriad of problems for society, and can trap already vulnerable sections of society in chronic poverty and perpetual vulnerability. Disaster hits hard those who are already vulnerable, and those who are hard hit become even more vulnerable.

“Vulnerability” is the key term for understanding the long-term effects of disasters. Some sectors of society are more vulnerable compared to others, and more exposed to harm and loss in the case of a hazardous event. Socioeconomic processes related to economic

inequality and the hierarchical power structures of a country are said to be responsible for the unequal exposure of individuals to risks in society (Bankoff and Hillhorst 2008). In the case of Nepal, we should also mention spatial disadvantages; i.e. the geographical marginality of the rural highlanders.

### 3 Understanding human vulnerability in Nepal

Nepal is one of the poorest and least developed countries in the world. Among 179 nations surveyed, it is ranked 30<sup>th</sup> from the bottom according to the World Bank (2018).<sup>5</sup> Vulnerability has generally been associated with poverty. Poverty exacerbates the negative effects of hazards and accidents and thus contributes to further vulnerability. Poverty certainly represents a deficiency in terms of facing risks, but poverty is not vulnerability in itself (Cardona 2008). Some wealthy and developed places may be exposed to high levels of risk (e.g. Japan and Taiwan in Asia to earthquakes and typhoons, California in the USA to drought and earthquake, The Netherlands in the EU to floods). However, such countries may be less vulnerable due to their capacity to cope with risks. There are many other factors involved in vulnerability such as demographic factors (i.e. population density, composition, proportions, trends etc.), infrastructural predisposition, institutional preparedness, public awareness, social cohesion (solidarity), etc. Many less developed countries may not be exposed to high risks of hazard, but may have some in-built deficiencies (including massive poverty) that increase the difficulty of facing risks.

As far as vulnerability is concerned, risks and poverty are important factors, but not all of them. From the point of view of vulnerability, more important are geophysical features, demographic parameters (number, concentration, density), infrastructure, settlements and buildings, as well as public awareness and the institutional mechanisms to respond quickly. The risk of a natural hazard or an accident turning into a tragic disaster depends only partly on poverty or on the force of the event itself. The conventional classification of countries – “least developed,” “developing,” “developed,” “low income,” “middle income,” “high income,” etc. – is not sufficiently applicable for assessing vulnerability and helping define risk-reduction strategies. It is better to consider the geophysical and environmental situation, demography, housing and settlement patterns, infrastructure, social cohesion and institutional realities of a place – of a town, a village area or a district. These place-systems should be assessed in terms of their susceptibility, short-term coping capacity, and long-term adaptation strategy (Welle *et al.* 2013).

Scholars and policy-makers have discussed different approaches to assessing vulnerability. There seems to be some agreement that the best way is to combine the demographic and taxonomic approaches of technical experts and professional planners with situational and contextual assessment conducted through local community participation (Wisner 2008). The updated guidelines (the “Sendai Framework”) issued by the United Nations for disaster risk reduction define a priority order: **a)** understanding disaster risk; **b)** strengthening disaster risk governance to manage the risk; **c)** investing in

disaster risk reduction for resilience; **d**) enhancing disaster preparedness for effective response and for recovery, rehabilitation and reconstruction (UNISDR 2015). The critical issues of human vulnerability are included in the third priority (i.e. investing in disaster risk reduction for resilience).

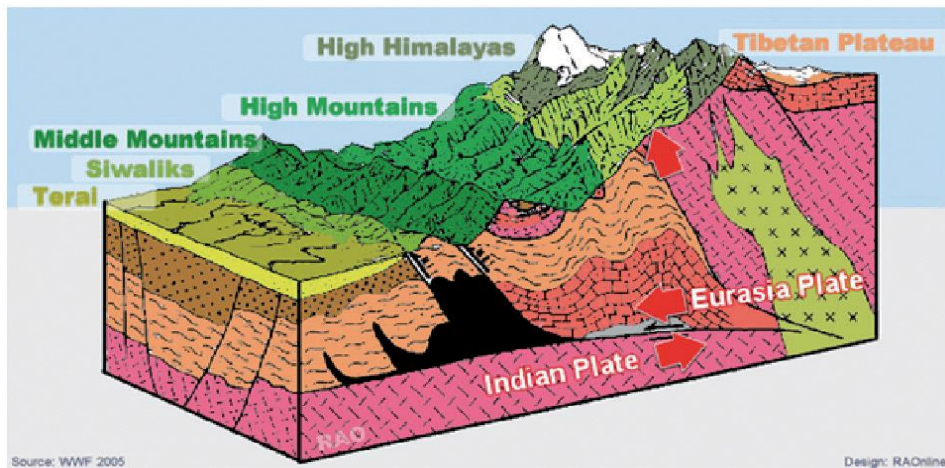
The government of Nepal has announced its commitment to UNISDR's Sendai Framework. It has declared it will increase investment in disaster risk prevention and risk reduction through all those measures which are essential to enhancing the resilience of communities as well as their environment and assets. According to the special agency of the Nepalese government for emergencies (NEOC 2018), the major sources of human vulnerability in Nepal, in order of damage and distress, are: first of all, road accidents; then epidemic outbreaks, earthquakes, landslides, floods, heavy snowfall and snowstorms, and drought.

Our studies and field surveys have revealed that vulnerabilities are exacerbated by poverty, and that poverty is perpetuated by vulnerabilities; a vicious cycle indeed. We have identified some key vulnerabilities in Nepal that are responsible for frequent disruptions and setbacks in people's lives and livelihoods and which expose them continually to mortal risks. In identifying the key vulnerabilities, we have taken into consideration the *level* and frequency of risk to normal people's lives and livelihoods. We have identified four key vulnerabilities in Nepal:

- Geophysical vulnerability;
- Human habitat vulnerability;
- Road traffic vulnerability;
- Environmental vulnerability.

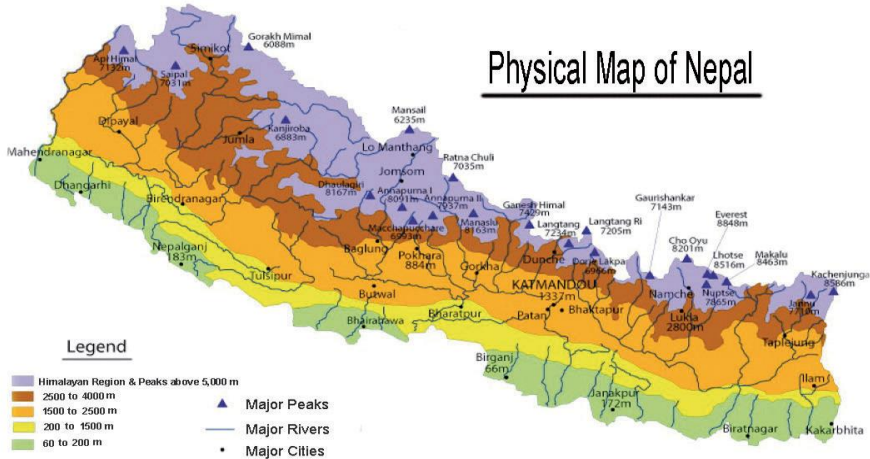
#### **4 Geophysical vulnerability and risk-reduction measures**

For centuries, earthquakes have hit Nepal, which lies between the trans-Himalayan outskirts of the arid and cold Tibet-Qinghai high plateau in the north (bordering China) and the *cis*-Himalayan fringes of the Gangetic plains with a warm sub-tropical climate in the south (bordering India). Around 85% of the entire national territory of Nepal is made up of mountains and hills, where human settlements are located mostly on steep slopes that merge into the relatively flatter and wider bottoms of V-shaped river valleys located between 200 and 4000 meters above sea-level. Everywhere in Nepal, from the flat lowlands to the high slopes, human habitats are vulnerable to seismic activity due to the fact that Nepal sits on the boundary of two massive tectonic plates that are in a perennial process of adjustment after millions of years of collision.

**Figure 2:** The Himalayan faultline

Source: Pant (2016, 17).

Land safety is problematic across the Himalayan region and surrounding, because the entire region sits on the fault lines of the Indian and the Eurasian tectonic plates. Nepal is located in the central and the highest portion of the Himalayan region, thus is the most exposed to the tremors and upheaval of the fault lines. These two massive tectonic plates collided to build the great Himalayan range millions of years ago. The ever-going convergence of these tectonic plates means relatively frequent earthquakes. More frequent than the earthquakes are the geohydraulic hazards. Landslides are frequent on the steep slopes all over Nepal. The threat of glacial lake bursts in the upper Himalayas is quite serious. In the summer monsoon period, heavy rainfall triggers excessive surface run-off and landslides on the mountain slopes, and flash floods in the steep catchments. Deforestation and land degradation have increased the risk of floods and soil erosion – not only in the mountains but also in the flat and wide southern lowlands (the northern fringe of the Gangetic plains).

**Figure 3:** Physical map of Nepal

Source: Pant (2016, 17).

Nepal needs an integrated environmental strategy centered on watersheds and eco/bio-regions that encompasses both highlands and lowlands. The newly established seven large administrative regions (*Pradesh*)<sup>6</sup> do not match the scientific criteria for watershed and eco/bio regionalism, but are constructed according to quite vague (politically compromised) criteria concerning ethno-linguistic and demographic patterns. Consequently, environmental protection, land-use policies and land safety measures are going to be quite problematic in the coming years.

**Figure 4:** Nepal's new administrative regions

Source: Wikimedia Commons (2019).<sup>7</sup>

Damage from quakes and aftershocks has not been uniform even within the same area. As highlighted by many studies in the aftermath of the 2015 earthquake, a significantly higher number of structures collapsed, causing deaths and injuries in the new settlements that had been established only in the last few decades (SGEB 2015). This was due to surface run-off on terrain susceptible to water pressures and sub-soil conditions (Okamura *et al.* 2015). Geo-technology experts recommend proper identification of sub-soil conditions, cracked river embankments, rocks, and destabilized slopes, because these all pose dangers in the case of excessive snowfall and rainfall, as well as in the case of later tremors (Chiaro *et al.* 2015).

In Nepal there are not enough good experts in the scientific and technical disciplines related to land safety. The scientific and technical education related to land safety must be expanded and improved as quickly as possible. More urgently needed are local (grassroots) level land-safety campaigns, basic training and local empowerment programs. Land safety work must begin with surface run-off management, not only of permanent natural streams (which swell during the summer monsoon rains) and all other rainfall-induced random temporary flows, but also of the water discharged from cultivated terraces and human settlements. The multitude of small surface run-offs must be well managed through a proper system of coordinated drainage at all levels, from tiny

hamlets and cultivated terraces to large watersheds formed by torrents on slopes and by major streams at the bottoms of valleys. Besides the management of surface run-off conveyance and protection of settlements and infrastructure, some other permanent measures are necessary:

- Constant monitoring of the geo-hydro configuration and trends at a local level;
- Local (municipal)-level institutionalization of risk assessment and early warning systems;
- Training for local people and administrators;
- Well-organized and continuous public awareness/notification campaigns regarding hydro-geological risks, locally manageable solutions for prevention, care and control;
- Implementation of well-targeted local, community-led re-forestation programs;
- Improvement of forestry practices in the existing woodlands;
- Expansive re-greening activities in private compounds, company premises, premises of public buildings, side-spaces of infrastructure;
- Public and communal spaces should be used, as much as is technically feasible, for re-greening by using land-stabilizing plantations (e.g. bamboo or *pipal*<sup>8</sup>);
- Haphazard locally initiated activities aimed at carving out vehicle tracks in the mountains should be restricted, because such invasive activities have increased the vulnerability of already fragile slopes.

All this implies that the role of the local community as “ecological sentinel” must be strengthened. The active involvement of communities in terms of mapping their vulnerabilities and assessing them is a key element in reducing geophysical vulnerability. The capability of vulnerable people to reduce their own vulnerability should be developed (Delica 2001; Delica-Willison and Willison 2004).

## **5 Habitat vulnerability and risk-reduction in housing and settlement planning**

Earthquakes occur infrequently, but they are unpredictable, inevitable, and sometimes extreme. Their effects can be mitigated by improving the quality of buildings and infrastructure, and by well-rehearsed and well-resourced emergency planning, but only up to a certain point. In contrast, more frequent risks (e.g. flooding, landslides, road accidents, etc.) can and should be substantially prevented through early warning systems, land-use planning, design practices, building methods and regulations, as well as social and economic policies that target vulnerability reduction. Strong political will is needed to ensure that adequate financial and technical support is provided by the government to people in order to reduce their vulnerability related to housing and settlements. We suggest applying the following basic financial and technical assistance measures to reduce habitat vulnerability in Nepal:

- Offering full financial grants and free technical assistance for a family's first shelter and livelihood-related structures to all who have been hit by earthquakes or landslides.
- Providing partial financial grants (proportionate to the damage) and free technical support for the first shelter (home) and livelihood-related structures.
- Strictly enforcing scientific codes – not only for buildings, but also for surface run-off water management, waste management, hygiene and sanitation facilities.
- Offering financial grants and technical help only to those who adhere to the codes of "basic habitability" (Gesto and Perea 2012).
- For tenants and other non-owners, providing soft (low-interest, long-term) loans for acquiring land-plots, but free technical assistance and full financial grants for building family shelters and livelihood-related structures.
- Giving only technical advisory help and no financial grants in the case of secondary purpose buildings (vacation homes, property for rent, recreational structures).

Post-disaster recovery represents an opportunity to rationalize local development plans that address public safety, service delivery and critical infrastructure. Critical infrastructure and basic services should be as accessible as possible to existing households: this should be a major priority, rather than building new buildings in new settlements.

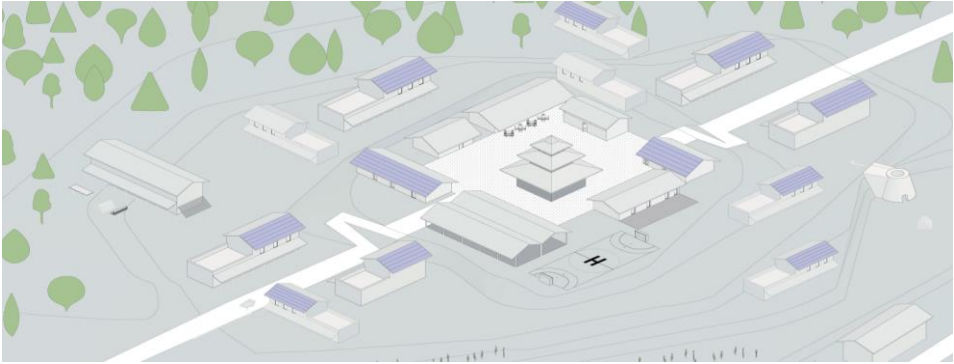
In Nepal, private houses in traditional rural settlements in the mountains are generally scattered and located close to cultivated land-plots, water sources, relatives, and kinsfolk; and often in proximity to a place of cult, worship or memory that has a cultural (and spiritual) meaning to the community. The location of private houses reflects livelihood-related needs as well as family bonds, community relations, and cultural traditions. The traditional scattered rural settlements in the central Himalayan highlands represent a coherent place system of functional, affectionate and symbolic interactions among inhabitants, as well as between inhabitants and their environment. The scattered location of private households makes people self-reliant in terms of basic necessities. It enables them to keep their animals and herds under constant supervision, and to manage (compost) domestic biodegradable waste in their own backyards. The scattered rural setting prevents the quick spread of contagious diseases and safeguards family privacy.

The idea of creating new integrated and compact settlements (*ekikrita basti*) by relocating and concentrating private households in a new safe spot may increase human vulnerability. Instead of making people safer and the delivery of services more cost-effective, the new compact settlements may create new problems, extra burdens and increase cost. They may also diminish villagers' self-reliance and create serious difficulties with managing waste and community hygiene. Therefore, people should be left freely to build their houses and livelihood-related structures wherever they choose within the boundaries of their land property once land safety conditions are ascertained. Except for the criteria of land safety and safeguarding of protected areas, there should be



no interference in people's choice of location for their shelters and livelihood-related structures. The government should, instead, create a common strategic space for people in all rural municipalities. The administrative and commercial centers of the rural municipal headquarters should be designed and built as strong and resilient fortified citadels; the common fortresses of the local community (*Sāmudāyika Durga*).

**Figure 5:** Rural municipal centre as the community fortress



Source: Pant (2016, 42).

Municipal centers should be developed as the safest nucleus of a territory, as community fortresses and as the permanent logistic hubs where all public and commercial facilities are based and from where all services are coordinated. They should serve as the base camps from where squads of government and security personnel, health workers, teachers and trainers, technicians, maintenance workers, service-providers, traders, volunteers etc. can go to outlying villages as required by the situation; both for ordinary routine tasks and trades, as well as for emergency missions. In normal times they should function as business hubs, while in the case of emergencies they should be a readily available safe haven. In the past, fortified citadels served as the permanent centers of local governance or as defensive structures or emergency shelters for the community.<sup>9</sup> In places like Nepal's mountain districts, these concepts are very relevant today. Municipal centers in ideal cases are symbols of local identity.

## 6 Vulnerability reduction as the guiding principle for transportation planning

The 2015 earthquakes damaged many roads and bridges. However, floods and landslides do even more damage, and more frequently. Nepal's roads are sub-standard. Far from being affordable to ordinary citizens, motor vehicles have become a status symbol for Nepal's consumerist middle- and upper-class, and motorable roads are synonymous with "development". National and local politicians from all ideological groupings totally agree to accord highest priority to construct motorable roads. As a result, expansive

motorization has led to land degradation, congestion, pollution, accidents (death and injuries), and a foreign trade imbalance (import of vehicles, spare parts, and fossil fuel). Nepal's main roads are frequently clogged because of narrow lanes (due to the constraints of the terrain). Poor maintenance and reckless driving create additional risks. A road trip in Nepal is quite troublesome and often dangerous; accidents are frequent. Road safety has become a serious issue, increasing people's vulnerability. Even before the earthquake, vehicle-related accidents ranked as the number one cause of health burdens in Nepal.<sup>10</sup> According to Nepalese police, road accidents constitute one of the top ten public security concerns and are one of the ten most numerous causes of criminal justice cases (NP 2017). The vast majority of victims of traffic accidents are pedestrians, passengers and cyclists (and animals). Nepal's policy-makers and planners seem eager to build more motorable roads and to widen existing roads to make room for more vehicles, while ignoring the need for walkable lanes and spaces for the free movement of people. Nepal's urban areas have become polluted and unwalkable. Similarly, the rural areas of Nepal are increasingly polluted and less walkable. As a consequence, human vulnerability has increased everywhere. As post-earthquake reconstruction of transport infrastructure is proceeding, new planning based on "vulnerability reduction" is needed. Considering people's daily needs, geophysical conditions, socioeconomic realities and local business development prospects (including tourism), Nepal's transportation infrastructure planning should be based on the following priorities, in descending order:

- **Walkability<sup>11</sup> as the top priority:** Nepal already has trekking trails with suspension bridges that are used by pedestrian travelers, traders, herders and animals. After the introduction of motor vehicles many are in disuse, and many need repair. It is time to restore, refurbish and maintain all of the pedestrian trails and bridges. Appropriate signal systems are needed for the pedestrian trails, bicycle routes and other non-motorized traffic paths. Why should only motorable roads have public information signposts and milestones? Non-motorized networks should be considered equally important as an alternative and complement to motorable roads. Non-motorized networks should intersect and converge with motorized ones. Each and every stop/junction of motorable roads and ferry-boats must serve as the starting point/terminal of non-motorized trails.
- **Pedestrians first on motorable roads:** every existing road must be retrofitted to include non-motorable lanes and easy and safe crossings for non-motorized traffickers (humans on foot, bicycles, animals); this must be mandatory for all roads. Existing roads should be made safer and completed (retrofitted, re-adjusted) with foot-paths, non-motorized lanes, safe crossings, and intermodal intersections.
- **New roads, better roads:** in building new and safer motorable roads, non-motorized lanes (for pedestrians, cyclists and animals) should be planned and designed right from the beginning. Priority must be accorded to pedestrians, animals and cyclists. Revisions may be necessary in terms of the legal liability of road builders, maintainers and drivers. Additional points should be added to the penal codes for cases of vehicle-caused death and injury to non-motorized movers; i.e. pedestrians, cyclists and animals.

- **Upgrade public motorized transportation:** strict enforcement of road safety and environmental rules, and training for public transport workers.
- **Proper management, regular maintenance and additional security measures:** for existing helipads, STOL (short take-off and landing) runways and flight routes; each airport/helipad must function as the starting point/terminal of motorized as well as non-motorized trails and roads.
- **Electric ropeways:** for goods (also for persons) wherever possible: each ropeway terminal should serve as the starting point/terminal of trails and roads.
- **Railroads:** eventually, Nepal will have to develop railways that connect with the Indian railway network in the south which already reaches Nepal's borders, and with China's railway network that is expanding in the Tibetan plateau. Rail connections with India and China could be immensely beneficial for Nepal's trade and tourism. Each railway station should be designed to serve as the starting point/terminal of motorized roads as well as non-motorized trails.

A multi-form inter-modal mobility system, with high priority for non-motorized modes (pedestrian/bicycles/animals), is what Nepal needs to create affordable, cost-effective and ecologically sound transportation while reducing human (and animal) vulnerability. Human and animal-powered mobility has always been a salient feature (and a great tourist attraction) of the whole Himalayan region. It can and should be harmonized with new, better and safer modalities of motorized mobility. This is important not just for cutting fuel costs and controlling pollution, but also for developing Nepal's economy (local trade, trekking and tourism). This multi-form intermodal mobility is, above all, necessary for reducing the vulnerability of all living and sentient beings in Nepal.

## 7 Environmental vulnerability, energy supply and waste management

Post-earthquake Nepal is facing many socioeconomic challenges related to environmental degradation and climate uncertainties. To address the environmental vulnerability in Nepal, two major issues must be seriously dealt with: energy and waste.

In Nepal, energy demand has been outpacing supply for many years. Fuel shortages are frequent, and high cost is a constant problem.<sup>12</sup> Demand for fossil fuels and electrical energy for private homes, transportation, business/livelihood structures and public facilities in Nepal is growing exponentially. Due to this shortage and high costs, many self-employed workers and small entrepreneurs are struggling to run their businesses. They are vulnerable to economic downturns as well as to other hazards. The obvious response from Nepal's government to the ever-increasing energy demand is to develop more hydropower because Nepal is rich in water resources.<sup>13</sup> To deal with the current shortage and increasing future demand of energy, Nepal has stepped forward to implement big hydropower projects.

One particular dream is quite popular in Nepal: making a lucrative revenue by selling electricity to neighbors (mainly India) where massive industrial development and expanding consumerism have generated a huge demand for energy. The dream of selling surplus electricity to neighbouring countries by generating a lot of energy from big hydropower plants is not sustainable at all. Large hydropower projects demand huge financial investment that does not come easily, is never free of conditions and interference, and takes a long time to implement. Large hydropower facilities and power transmission grids are complex to manage and expensive to maintain. Bigger facilities imply more risks from natural hazards (earthquakes, floods, landslides ...) and security threats (terrorism, sabotage). Big hydropower plants are invasive and are likely to alter local ecosystems. In the case that Nepal successfully harnessed electricity from big plants, it would be compelled to sell most of its surplus only to India or China (the two countries that encircle Nepal) on their own terms because there are not enough market options to sell electricity to a variety of buyers. Therefore, big hydropower projects aimed at producing surplus electricity do not make economic sense. It would be better to develop a multitude of locally manageable mini-grids and small-scale plants all over the country to satisfy local needs at affordable price. Nepal also needs to prioritize the use of renewables (rather solar than wind<sup>14</sup>) and human/animal power solutions (for walking, working, riding, and traction), combined with better management and operational efficiency through the entire energy supply chain. People's energy-deprivation and related vulnerability should be addressed through decentralization (micro/mini plants catering to local needs) and de-massification (stand-alone solar panels). Energy de-massification and de-centralization make end-users more responsible, and empower local communities.

The cleanest unit of energy is the one which is not consumed. Deliberate rationalization to reduce energy demand is the best way of saving energy (and cost) and cutting pollution. Reducing energy demand can be achieved through improving lamps, installing efficient and smoke-free kitchen stoves, biogas plants in rural farming households with animals, proper insulation and ventilation of buildings, use of locally available natural building materials (e.g. limestone, hemp, wood, bamboo etc.) Walkability, bicycle lanes, animal-power, etc. can drastically reduce the demand for energy, particularly of highly polluting imported fossil fuels. A relentless drive to reduce energy demand is likely to trigger many improvements in eco-efficiency and a new wave of entrepreneurial activities. Practical training for the population to reduce energy demand should be an integral part of a civic environmental awareness campaign that uses all possible means: local community-based training sessions, media (print, radio, television) and web. Fiscal incentives for decreasing energy consumption should be made available to households, businesses and all private and public organizations. Demand reduction must be the main goal of Nepal's energy strategy. This will encourage economic savings and ecological innovation. Nepal will be lighter and leaner, greener and cleaner; and, above all, people and all other living beings will be less vulnerable. A deliberate and determined drive to contain and decrease "volume" (i.e., the cumulative quantity of energy that is produced) should be combined

with an equally strong drive to increase “value” (i.e. need satisfaction, reliability, cost-effectiveness). The de-coupling of “value” and “volume” is a strategic imperative for sustainable economic development everywhere, not only in Nepal.

Along with the issue of energy, waste is a critical issue for Nepal’s environment. The 2015 Earthquake turned a lot of man-made structures into debris in Nepal’s towns and villages, where non-biodegradable waste was already an increasing burden. The impact of waste is related to the pollution of soil, water and air; but also includes space consumption, bad smells and aesthetic degradation – detrimental to the environment, public health and tourism. Nepalese people are vulnerable to many risks related to the ever-increasing and accumulating volume of waste littered around and dumped at many sites, most of them unauthorized and carelessly managed.<sup>15</sup> Three decades ago, waste was not a problem because consumption and material flows were limited within the confines of a subsistence economy based on the resources available within a close range, mostly related to the primary sector (agriculture, livestock, forestry). Rural activities generated very little waste, which was almost entirely biodegradable, and that waste was re-distributed within a narrow area and dissipated into the environment (decomposition and re-cycling in Nature). In the past three decades, the situation has drastically changed. Non-biodegradable waste has increased enormously even in remote rural areas due to urbanization and urban-like consumerism with the steady circulation of industrial products, mostly imported from outside Nepal. Non-biodegradable waste is increasing everywhere in Nepal, including the high crests and peaks where leftovers from trekking and climbing expeditions are scattered.

There is an important sociocultural dimension to waste management in Nepal: the very low social status of waste-management workers. This is not only a legacy of the old caste mentality. It is more due to the negative perceptions of ordinary people all over the world (not only in Nepal) about any work that involves the handling of waste (filth, dirt, discarded materials). In Nepal, as in many parts of the so-called “Third World,” ground-level waste-handlers are neither properly trained nor well paid. There are many informal waste-pickers who are self-employed and organized in small bands. Their working conditions are even worse. Inevitably, this creates low self-esteem among all waste handlers, with adverse effects on their morale and quality of work. For any society to be clean and healthy, waste handling must be among the well-paid jobs. Training programs and better pay would certainly help to raise the social profile of waste-handlers and make it easier for them to obtain better economic treatment. Improvements in the socioeconomic conditions of waste-handlers means reducing, first of all, the vulnerability of an already vulnerable and marginalized social category (i.e., waste-handlers). A reduction in their vulnerability would lead to a drastic reduction in the vulnerability of the entire community, which in turn would then be less exposed to health and environmental risks posed by waste.

Waste minimization should become the highest priority. Lessening demand and diminishing circulation implies an extended life-cycle for products, more re-use/recycling, better quality of environment, less burden (and cost) for waste management; and, above all, a reduction in the vulnerability of all living and sentient beings. The following list describes measures for waste minimization:

- Re-qualification of waste-handlers through selective recruitment, solid training and good remuneration as “workers with special skills”, and “public officers” (i.e. environmental operators).
- Reduction of the length of supply chains for all commodities and products (towards “zero km”).
- Increasing the durability of end-products, artificial plants and installations, infrastructures.
- Enhancing the versatility, re-use and recycling of materials and products already in circulation.
- Implementation of new fiscal measures (tax and incentives) for curbing waste.
- Enforcement of strict regulation on waste disposal.
- Increasing wealth creation through non-material and cultural resources (services, arts, literary and scientific productions, brand value ...).

## 8 Economic policy for vulnerability reduction and sustainable development

From the perspective of the conventional economy, which is obsessed with quantitative “growth,” the macro-economic indicators of the past decade generally show slow and moderate growth in the gross domestic product (GDP)<sup>16</sup> of Nepal. As per Nepalese government sources (MF), GDP per capita is estimated to be around 853 US \$ now; a slight increase on previous years. In the current fiscal year (FY 2017–2018), GDP is projected to increase robustly (around 6.94%) while inflation is expected to rise only modestly (around 3.4%); total government revenues are predicted to grow spectacularly (around 33%), while foreign loan and grants are liable to remain at the same level as the previous year.

The picture provided by international organizations is entirely different. According to the Asian Development Bank, the growth of Nepal’s economy is slowing down to 4.7% in FY 2017–2018. This growth forecast has been revised down from an earlier estimate in the wake of severe floods and landslides that affected agricultural output (ADB 2017). According to the World Bank, economic growth is expected to slow down because of the contraction in agricultural output and exports, higher interest rates, inflation (between 5% and 9%) and a tightening of credit. Government expenditure is expected to rise further and widen the fiscal deficit, and the decrease in remittances is resulting in current account deficits. The growth of deposits has slowed faster than that of credits, resulting in the diminished ability of banks to lend to entrepreneurs (World Bank 2018).

For the last six decades, the general picture of Nepal has been that of a weak and backward country. As per the “multi-dimensional poverty index” (MPI)<sup>17</sup> Nepal is a backward and weak country, despite some noticeable growth in national output and government revenue. According to the estimates of Nepal’s National Planning Commission (NPC 2018) and the United Nations Development Programme (UNDP/Nepal Office 2018), 28.6% of Nepal’s total population<sup>18</sup> suffers deprivation, and Nepal’s score on the Human Development Index (HDI) is very low – 144<sup>th</sup> among 188 countries. Outbound migration and the under-reporting of seasonal intra-regional migratory movements have falsified data about unemployment (officially around 3.2%). Under-employment, the informal (“black”) job market and poor remuneration (i.e., exploitation) are widespread. The economic freedom needed for entrepreneurial activities is moderately below the regional average (Asia-Pacific), well below the global average, and far below the average enjoyed by entrepreneurs in developed countries.<sup>19</sup>

The revenue of the government in relation to GDP was around 21.45% in the recently concluded fiscal year (FY 2016–2017). Of all government revenues, 93.18% was from taxes; non-tax revenue was 6.82%. Revenue in previous FY (2015–2016) in relation to GDP was around 20.5% (tax revenue 18.4%, non-tax revenue 2.1%). In FY 2014–2015, it was 19.1% of GDP (tax 16.8, non-tax 2.4%). In 2013–2014, the FY preceding the earthquake, it was 18.2% of GDP (tax 15.9%, non-tax 2.2%). Since FY 2006–2007, when total revenue was 12.1% of GDP, the government’s tax revenues have continued to increase (MF 2016a and 2017).

Public finance does not seem to be in very bad shape for now. But the national economy is lopsided (non-productive) and externally dependent (remittance, foreign aid); society is backward, and people are vulnerable. There is ample space for the Nepal government to adjust public finances in order to invest more into human vulnerability reduction as well as in human resource development (i.e. education/training, business incubators, support for entrepreneurial start-ups). This demands sustained financing from state coffers which should be continually replenished by revenues. A reduction in human vulnerability and enhanced human resources would lead to the widespread development of entrepreneurship and self-employment which, in turn, would lead to more private and corporate income, thus multiplying sources of tax revenue. In any case, initially, consistent financial investment is needed; this means an increase in government expenditure. Therefore, two sets of policy measures are necessary to make Nepal’s post-disaster development financially viable and economically sustainable: **cuts** and **taxes**.

We suggest starting with the “cuts” by reducing drastically the perks and privileges of politicians<sup>20</sup> which are disproportionately costly for a poor and backward country like Nepal. Cuts should also be made to many ceremonies and celebrations.<sup>21</sup> Cuts in perks, privileges and ceremonies may not be quantitatively significant in terms of making savings from public finances, but they are certainly helpful in terms of resource efficiency and are politically and socially meaningful as a strong symbolic gesture of the moral

legitimacy of rulers and the system. The moral legitimacy of the political system is one of the fundamental requisites for sustainable development. For the moral legitimacy of a system to be sustained, downtrodden and common citizens should be protected and provided with the essentials they need to live well, and the highest echelons of the establishment of power should represent living examples of parsimony, sobriety and efficiency to lead effectively. Without the moral legitimacy of rulers and system, it is difficult for a government to lead; and it is hard to obtain compliance from citizens who struggle to live. When the moral legitimacy of rulers and system is in doubt then the private sector feels justified in dodging taxes, non-governmental organizations tend to be self-serving, corruption in public administration and in business management becomes rampant, common citizens suffer, and the economy languishes. Austerity is a very efficacious economic policy provided that it is applied first and foremost to rulers and elites.

There is a wide range of subsidies and discounts that Nepal government offers to organizations, sectors and companies. The government should periodically scrutinize all subsidies and concessions. The government should periodically make a balanced score-card for each subsidy or concession awarded to any person, firm or organization. Cuts in unproductive subsidies and unnecessary concessions may not quickly produce a big difference in the government coffers, but cumulatively and ultimately, they become incisive for rationalizing the system and allocating resources where they are worth allocating.

Every year, an independent, critical “spending review” of all expenditure should be published in order to single out potential areas in which to apply cuts. The spending review should set out where and how government money can be saved from expenditures that are morally untenable (disproportionate perks and privileges), superfluous (non-essential, like pompous ceremonies), or socioeconomically unproductive (certain subsidies). Once singled out, the public must be informed about the results of the spending review, and the cuts must be executed quickly. The cuts will certainly help with saving, with re-deploying resources productively, and with creating the moral ground and social consensus on which the government can impose taxes.

Nepal’s government should work towards building a broad formal tax base (Pyakurel *et al.* 2013; SLRC 2016). Nepal does not tax citizens a lot, but it delivers too little. It should tax a little more, but must deliver a lot better. Taxation must be limited and well-targeted, based on socioeconomic goals.<sup>22</sup> A steady stream of tax revenue is needed now and in the future to reduce the vulnerability of Nepalese people and for human capital development (i.e. health, education, skills, training, capacity building, business incubators, support for entrepreneurial start-ups). While the expenses of vulnerability reduction and human capital development justify some increases in tax, there may also be some areas where the decrease or elimination of tax is beneficial to people. Taxes on business and labour inhibit the entrepreneurial spirit and work ethic. Progressive taxation



on corporate profit and private income is justified. It is acceptable to tax heavily various forms of speculative investments (stock market gains, capital gains, currency trades, etc.). It is also acceptable to tax non-productive forms of earning such as rent, inheritance, discounts, commissions, etc. as well as certain forms of consumption.

Value Added Tax (VAT) is a general consumption tax and is added to goods at each step of the production and distribution process. VAT was introduced in Nepal in 1997. The current general rate is 13%. Some items such as agricultural items and inputs, medical supplies, educational materials, literary and cultural items, public transport for passengers, etc. are exempt. Nepal should review its VAT policy in the light of domestic needs. The VAT situation is different from country to country. VAT is the most commonly applied consumption tax in the world (applied in more than 160 countries). Leaving aside exemptions and reductions, according to the socioeconomic policy goals of each country, the global average general VAT rate is around 15.80% (KPMG 2015). Nepal's general VAT rate is quite low (13%). It could be raised a little higher, to a general rate of 16%. This would help public finance and would allow government spending on welfare, human vulnerability reduction, environmental protection, human capital development through education, public awareness campaigns, capacity-building, entrepreneurship-facilitating services (training, business incubators, cheap credit, market info), etc. Some more items should be included on the list for exemption or rebate; for example: medical and educational supplies, the building materials produced in Nepal that include components of Nepalese origin, technical instruments and essential items related to land safety, clean water supply, pollution control, wireless telecommunications and internet services, renewable and clean energy, waste management, etc. The government can continue adjusting VAT exemptions and rebates for specific items or sectors in order to improve sustainability, to cool an overheating business sector, or to boost an ailing one. In the long term, the general VAT rate should be stable and well within the tolerable range (between 15% and 18%) in order to prevent the expansion of a VAT-dodging, under-ground ("black") economy.

Nepal needs to introduce "extended producer liability"<sup>23</sup> to tax all product's end-of-life phase because that phase creates environmental and public health burden and waste management cost. It is designed to offset the environmental cost of goods. It is incorporated into the price of products by making the manufacturer of the product responsible for the entire lifecycle including the post-consumption (after-use/end-state) phase for take-back, recycling and final disposal. In Western Europe<sup>24</sup> many countries have adopted some form of such targeted taxation, either directly as a pre-tax fee paid by companies to the specific consortia that handle the post-consumption (end-of-life) phase of that specific product, or as a part of direct tax, or a mixture of both. This concept was first introduced in Sweden in 1990. Later, the European Union issued a waste directive mandating all member states to recycle non-biodegradable waste and use fiscal and regulatory means to make this happen. In the case of Nepal, the extent of such a tax should be proportionally correlated to the volume of waste generated by a product and its

packaging material, with the risks (hazardous/non-hazardous) incurred by the after-use phase, with the environmental burden (biodegradable/non-biodegradable), and with the cost of waste handling and final safe disposal.

In the case of products imported from other countries (i.e. most of the consumer products in Nepal), there should be an “extended importer/trader liability” tax for products as well as for packaging materials whose end-of-life/after-use ultimately becomes a burden to society, the environment and public finances (i.e. the cost of waste management). Imposing an outright ban on non-biodegradable materials without some viable alternative makes little sense. The former would be unenforceable, thus would only create illegal traffic and unauthorized dumping. It is better to vigorously tax non-biodegradable materials right at the beginning of their entry into the socioeconomic cycle in order to prevent waste. The tax collected by extended producer and trader liability should be invested in the research and development of locally available biodegradable substitutes and used to provide an incentive to local entrepreneurs who produce items from locally available biodegradable materials and re-use and recycle materials already in circulation.

In addition, substantial taxation should be imposed on items associated with an unhealthy lifestyle such as drugs, tobacco, alcohol, junk food, and drinks. Since 2016, the United Kingdom has imposed an extra tax burden on sugar-containing bottled and canned drinks. In response to growing concerns over obesity, UK imposed a levy on soft drinks like Coca Cola, Pepsi Cola, Red Bull, 7Up, etc.<sup>25</sup> Many other countries are either already implementing or seriously considering similar options for a variety of unhealthy items.

After imposing fiscal pressure on unhealthy items, on the end-of-life/after-use stage of all products, and on non-biodegradable materials, the cost will be very high for certain types of industrial products. A hefty tax on non-biodegradable and unhealthy items, containers and packaging will generate noticeable costs for producers and importers. Producers and importers will discharge the accumulated tax pressure down to retailers and consumers in order to maintain their profit margins. Ultimately, end-consumers will have to pay more. This will discourage the consumption of certain products. Less non-biodegradable materials in circulation means a reduction in the waste management burden. Less consumption of junk foods/drinks means a positive gain for people’s health and purses. Less importation will stimulate local entrepreneurship and improve the trade balance. The demand for local biodegradable substitutes will certainly increase. Local producers may venture into the production and trade of local alternatives that are less exposed to taxation (i.e. environment-friendly, healthy, biodegradable). Harnessing domestic resources through such progressive taxation for local development is far better than depending on foreign aid (loans and grants).

After the 2015 earthquake, foreign governments and international organizations pledged (but have not effectively delivered) a little more than four billion US\$ to help Nepal – nearly half of the entire total estimate of aid required for the five-year period of

rehabilitation and reconstruction. Aid from foreign governments and from international institutions is called “Official Development Assistance” (ODA). In Nepal ODA is spent on infrastructure, drinking water, health, education, energy, agriculture, and also for “peace and rehabilitation” projects after the end of Maoist insurgency. ODA comes to Nepal in different forms (outright grants, commodities or cash or specific services, soft loans, disbursements for ongoing or completed projects, direct payments to providers such as NGOs or firms, etc.). Foreign aid is used to support development programs, national budgets, and for humanitarian assistance. Nepal also receives direct help from large international non-governmental organizations (INGOs). The combination of all foreign grants, loans and contribution has represented on average one-fifth of the national budget over the last decade.

Nepal has been receiving foreign aid and “advice” for the past six decades. Six decades of such foreign aid and advice have not produced better governance in Nepal. The country remains one of the poorest, worst governed,<sup>26</sup> and perceived as one of the most corrupt<sup>27</sup> in the world. All this seems to suggest that foreign aid to Nepal is ineffective, misused or wasted. Serious doubts have been raised by scholars and observers, both Nepalese and foreigners, about foreign aid to Nepal, from early periods until recent times (Mihaly 1965; Pyakuryal *et al.* 2008; Panday 2011). Frequently, observers question foreign donors’ terms, conditions and “advice” (interference in internal affairs). More questions are being raised about many unintended consequences (e.g. corruption, the rise of a foreign-connected new professional elite, rent-seekers, too many aid-seeking NGOs, proselytism for converting locals to followers of alien religions, distortion of market, inflation, aid-dependency, loss of national prestige, etc.). Foreign aid is a very controversial issue in Nepal; but not only in Nepal.

Ultimately, reliance on foreign aid is not a definitive solution for any country. A country that is dependent on foreign aid will never be free of foreign interference in its internal affairs, and will never be held high in the opinions of its own people nor in global public opinion. Now, starting from the efforts related to post-earthquake reconstruction, Nepal’s economic goal should be to pay back its foreign debt and phase out dependency on foreign aid. Nepal should build a self-reliant and debt-free economy based on sound public finances, targeted taxation, government efficiency and, above all, private sector productivity and expansion (local entrepreneurship-driven development). The best form of foreign aid that Nepal needs, and which can be highly effective, is that of selected and essential technical help: experts, trainers and essential equipment from abroad.

## **9 Concluding remarks: a little note from the past, an important lesson for the future**

After the big earthquake of 1934, which killed more than 12000 and destroyed most of Kathmandu valley’s houses and infrastructures, Nepal’s rulers of that period (hereditary monarchy, regents and coteries, none democratically elected), politely declined the

generous offers of financial help for reconstruction by the global super-power of that time (i.e. the British empire, present as colonial administrator in neighbouring India). But the Nepalese rulers were successful at mobilizing and managing internal resources, helping the needy, punishing the greedy, and in re-building better. In the aftermath of the 1934 earthquake, free donations from individuals and charities from outside Nepal (mostly from India, Britain and Japan) were accepted only for immediate emergency relief. Not a single penny was accepted for reconstruction. Reconstruction was done entirely by harnessing internal resources (Sharma 1951). It is also noteworthy that, in the end of a seven years-long recovery and reconstruction process, loans provided by government to commoners for rebuilding their family shelters were totally pardoned (Shamsher [1936] 2015). Is it not possible for today's democratically elected Nepalese rulers to do something similar (or better) now, instead of begging for money from foreign donors and delaying the reconstruction process?

#### Notes:

<sup>1</sup> After a two-decade hiatus, local (municipal and regional) elections were held in Nepal in three phases on 14 May, 28 June and 18 September 2017. These were the first local-level elections to be held since the promulgation of the new 2015 constitution. The previous local elections were held in February 2006 under the old monarchical constitution, which were boycotted by the major political parties, and saw low voter turnout. Prior to 2006, local elections were held in 1997. Elections were supposed to be held in 2002 but were delayed due to decade-long (1996–2006) violent political turmoil caused by the so-called “people’s war” launched by the Maoist communist party of Nepal.

<sup>2</sup> Sindhupalchok, one of the mountain districts worst affected by the earthquake (one of our field survey sites), is a case in point; out of 68 municipal bodies known as “Village Development Committees” (VDC), as many as 25 VDC offices were without secretaries when the disaster happened.

<sup>3</sup> In less than three years following its formation, the chief executive officer and members of the executive board of the National Reconstruction Authority (NRA) were changed four times following changes in the government coalition and due to the political bargaining among the coalition partners.

<sup>4</sup> It appears that, since 2006, more than four million able-bodied Nepali citizens have left the country to work abroad. According to Nepal’s government foreign employment regulatory offices, each year around half-a-million Nepalese citizens legally go abroad for work. There are no estimates about those who have left illegally (through human-trafficking channels).

<sup>5</sup> World Development Indicators from the World Bank, gross domestic product (GDP) per capita based on purchasing power parity (PPP); data last updated on 01/03/18.

<sup>6</sup> Nepal’s new constitution came into effect on Sept 20, 2015, replacing the interim constitution of 2007 which, in turn, was established after the abolition of the monarchy. According to the new constitution, Nepal is composed of seven large administrative regions which are supposed to be responsible for local development, some fiscal policy matters, environmental measures and social provisions.

<sup>7</sup> Source and license: [https://commons.wikimedia.org/wiki/File:Nepal\\_adm\\_location\\_map.svg](https://commons.wikimedia.org/wiki/File:Nepal_adm_location_map.svg) (15 March, 2019).

<sup>8</sup> *Pipal* or *Peepul* (*Ficus religiosa*) is a species of semi-evergreen fig tree with a very long lifespan.

<sup>9</sup> Their remains are found in many parts of the Indian subcontinent and Himalayan region where they are known as *Gadh*, *Gadhi* or *Kot*. Such public structures were also common in Europe during the Middle Ages. Many medieval European villages and towns were developed around a central fortified structure (*Receptum* in Latin) which served as a temporary retreat to protect the population in times of insecurity and emergency. Usually, the fortified citadels (*Ricetto* o *città murata* in Italy, *Kremlin* in Russia, *château* in France, similar structures all over Europe) contained the governor's residence, a military post, market square, chapel, lodging and storage facilities. *Receptum* also served as the places in which to deposit the treasures of the community, venues for gatherings of public interest and celebrations, and as the site of local government. The best preserved example of a large *receptum* in Western Europe is to be found in Candelo (*Ricetto di Candelo*, built in the 11<sup>th</sup> century A.D.) in the province of Biella in the region of Piedmont, north-western Italy.

<sup>10</sup> "Road accidents are the leading cause of death of young adults between 18–29 years of age. Those getting killed are therefore often the able-bodied, the best of the workforce, and often the breadwinners for their family," (c.f. *Nepali Times*, 26 July–1 August, 2013).

<sup>11</sup> "Walkability" is a measure of how safe and easy an area is for a pedestrian. Walkability means that the public space and built environment are benevolent to the presence of people living, working, doing their necessary tasks, going to school, shopping, visiting, enjoying or spending time in any area – on foot. Walkability decreases human vulnerability; it encourages safe and free movement of individuals and groups, social interaction and the getting-together of friends and relatives. Walkability provides the much-needed "eyes on the street" that reduce petty crime because more people walking around means more eyes watching over neighborhoods and streets. Walkability has become an important concept in land-use and environmental planning. Factors influencing walkability include the quantity and quality of sidewalks and walking lanes, pedestrian rights-of-way, land use patterns and, above all, a drastic decrease in the volume and pressure of motorized traffic. Automobile-focused street design and town planning are detrimental to walkability. In Asian cities, only areas of interest to tourists are walkable to some (limited) extent; the case of Nepal is one of the worst in Asia (Leather *et al.* 2011).

<sup>12</sup> According to a projection from the Nepal Electricity Authority (NEA), demand will triple in the next decade, reaching 3,600MW by 2027. Nepal's installed hydropower capacity is around 800 MW. Electricity demand has already exceeded 1300MW. According to the latest official estimates, fossil fuels are used mostly for transportation, while firewood still contributes more than 75% of household energy needs (in rural areas, perhaps 99%); fossil fuels account for more than 8% of domestic needs, electricity for only 2%, and solar around 0.5% (Water and Energy Commission Secretariat, Government of Nepal, 2015).

<sup>13</sup> Nepal is rich in water resources: glaciers, snow-melt, rainfall, falls and springs, surface and underground water. There are more than 5000 rivers, including rivulets and tributaries, totaling about 45000 km in length. Moreover, there are hundreds of lakes and thousands of natural ponds of various sizes. Nepal contains 2.2% of the world's inland water resources. This is significant considering that the country is a relatively tiny, landlocked spot on the world map. Nepal's potential capacity for producing energy from hydropower projects is estimated to be above 80000 MW.

<sup>14</sup> Nepal's geophysical characteristics (between 30.43° and 26.36° latitude north of the Equator, elevated position) and climatic conditions (around 300 days of sunshine annually) create highly suitable conditions for harnessing solar energy for heating as well as for electricity generation. Solar and photovoltaic (PV) plants do not pollute the air; they can be added or fitted into existing structures (usually on rooftops) without occupying extra space and without being visually invasive.

Covering natural spaces and green fields with solar/PV must (and can) be avoided; solar/PV should be fitted onto the built structures without eroding virgin surfaces. In contrast, wind power turbines have a significant impact. A large number of turbines and supporting structures and a lot of materials and artifacts are needed to harness energy from wind. Such invasive structures can have a degrading effect on landscape quality (landscape is Nepal's main resource for tourism). The availability of wind is irregular and uneven from place to place, and highly unpredictable. Wind power facilities (turbines) interfere with the normal movement of birds and insects (e.g. honeybees, butterflies, glow-worms ...) directly, and as act as physical barriers indirectly through disturbances in bioacoustics and vibrations. It may be possible to harness energy from small individual turbines in the form of power co-generators by using a "stand-alone" (off-grid) system in some windy places (e.g. northwestern high mountain districts). In general, for the public grid and on a medium-large scale, this solution is not suitable for Nepal.

<sup>15</sup> Nepal's waste management needs survey submitted to the "Global Partnership on Waste Management". The United Nations Environment Programme (GPWM/UNEP) and the Nepal-based NGO Society for Environment and Economic Development (SEED) suggests that Nepal's waste management is very inefficient and, above all, the country needs to address the problem of specific and potentially hazardous wastes such as industrial and non-biodegradable waste, healthcare waste (used and discarded bio-medical items) and e-waste (electronic and electrical trash). In Nepal, potentially hazardous wastes are often discharged carelessly, or disposed alongside general municipal waste, or informally recycled with little attention to health and environment (UNEP 2019; available at:

<http://www.unep.org/gpwm/InformationPlatform/org/gpwm/CountryNeedsAssessmentAnalysis/Nepal/tabid/106535/> (15 March, 2019).

<sup>16</sup> For the fiscal year (FY) 2015–2016, Nepal's real GDP at basic prices (adjusted with inflation) was estimated to be around NPR 6 952 billion (around 66 billion US\$, provisional estimate, first semester of current FY), with an annual inflation rate of around 9–10%. The annual average percentage change of real GDP at basic prices has swung between 2.8% in FY 2006–2007 to 5.7% in FY 2013–2014. A sharp decline occurred in fiscal year 2014–2015 (2.3%) and in FY 2015–2016 (0.77%), certainly due to the economic slowdown following the earthquake, unrest in the southern lowlands, and the Nepal-India border blockade between late 2015 and early-2016. Per capita GDP was 410 US Dollars in FY 2006–2007; it reached 762 US\$ in FY 2014–2015 and was expected to decline slightly (752 US\$) in FY 2015–2016. Nepal's moderate increase in GDP has not been well distributed; the rich-poor gap remains a serious problem.

<sup>17</sup> The global "Multi-dimensional Poverty Index" (MPI) was developed by Alkire and Santos (2010; see also Alkire *et al.* 2015) and first appeared in the UNDP's 2010 Human Development Report. The MPI takes into account three dimensions of deprivation: health, education, and living standard. In each of the three dimensions several specific indicators (e.g. households with running water or proper roofing and flooring) can be included as per the local context. The Sustainable Development Goals (SDG) promoted by UN recognize and seek to end poverty in all its forms and dimensions. The multidimensional concept of poverty is now embedded in the SDGs.

<sup>18</sup> The total population of Nepal is 29 million.

<sup>19</sup> According to the Heritage Foundation's calculations, Nepal's economic freedom score is 54.1, making its economy 133<sup>rd</sup> out of 180, putting it among the "mostly unfree" countries. The "Economic Freedom Index" is calculated by taking into account judicial effectiveness, property rights, monetary freedom and labor freedom.

<sup>20</sup> "... Former dignitaries, including heads of state, prime ministers, ministers, chiefs of commissions and security bodies, justices and secretaries are using excessive ... facilities worth millions of rupees from taxpayers' money", stated the sub-panel of a parliamentary committee after

nearly three months of study. The sub-panel was headed by parliament member Janak Raj Joshi. ... “Rented or government residences, deployment of personal and residence security and other facilities such as vehicles, drivers, fuel, maintenance, secretariat, staff, helpers and medical facilities are the types of conveniences provided to former dignitaries. In Nepal there are 8 former prime ministers, 9 former deputy prime ministers, 11 former chief justices and 17 former home ministers using the facilities,” stated the report. “The state has to bear from Nepalese Rupees [sic] (NPR) 3.6 million to NPR 4 million every year just for one former high-ranking dignitary ...” (see Prakash Acharya, “Security, facilities for former VIPs unjustifiable: House panel” in the Himalayan times, daily, Kathmandu, Nepal, 21st June 2016).

<sup>21</sup> Every time Nepal’s head of state (president) or government (prime minister) travels abroad on an official visit, a big, colourful ceremony is organized with five virgins (*Pancha-Kanya*), decorations and garlands, guard of honour and so on at the airport to see-off and to welcome back; this is unnecessary, expensive, even ridiculous.

<sup>22</sup> From reading the 253-page-long report of Nepal’s tax advisory committee (Rajaswa Paramarsha Samiti-ko Prativedan 2067, Ministry of Finance, Government of Nepal (2010)), we get the impression that there are enough details but not enough clarity about economic and social policy goals for targeted taxation.

<sup>23</sup> According to the Organization for Economic Co-operation and Development (OECD 2019), “Extended Producer Responsibility” places a significant responsibility – financial and physical – for products’ post-consumption phase. Assigning such responsibility could in principle provide incentives to prevent wastes at the source, promote product design for the environment and support the achievement of public recycling and materials management goals. Within the OECD the trend is towards the extension of EPR to new products, product groups and waste streams such as electrical appliances and electronics Available at: <http://www.oecd.org/env/tools-evaluation/extendedproducerresponsibility.htm> (15 March, 2019).

<sup>24</sup> In Germany, after the adoption of “extended producer liability”, between 1991 and 1998, per capita consumption of packaging material was said to have come down from 94.7 kg to 82 kg. In the USA, 40 such laws have been enacted in various states since 2008 and the results are positive. *Auto Recycling Nederland* (ARN) is a producer liability organization that makes arrangements for vehicle component recycling charging an advanced recycling fee to those who purchase a new vehicle; that fee is used to fund recycling. *Consorzio Nazionale per la Raccolta, il Riciclaggio ed il Recupero degli Imballaggi in Plastica* (COREPLA) in Italy is a mandatory consortium for companies that produce plastic materials; it was established to charge producers a fee and to handle collection, recycling and re-utilization. There are similar mandatory consortia for other non-biodegradable wastes across Europe. Outside the EU, other western countries such as Norway, Iceland and Switzerland have also adopted similar measures. The Swiss Association for Information, Communication and Organizational Technology (SWICO), an ICT industry organization, addresses the problem of electronic waste.

<sup>25</sup> In the UK there is a so-called “sugar tax” on bottled and canned drinks with more than 5g of sugar per 100ml. There is also a higher rate for those with more than 8g per 100ml. Natural fruit juice and milk-based drinks are exempt. The measure will raise an estimated 520 million pounds (around 673 million US\$) a year, and will be spent on doubling funding for sports facilities in primary schools of Britain.

<sup>26</sup> The ‘Bertelsmann Transformation Index’ (BTI) prepared by Bertelsmann Stiftung (an international NGO dedicated to research and documentation on socio-economic and political transformation in the world, based in Germany), a governance assessment tool covering 129 countries, rates Nepal as very low (around 3 on a 1-10 scale) in the “resource efficiency” (effective use of available resources) and “steering capability” (political leadership and strategic

coordination) criteria. According to BTI, Nepal clearly lacks a coordinated long-term approach for economic development.

<sup>27</sup> According to Transparency International's Corruption Perception Index, Nepal is located in 122<sup>nd</sup> position among 180 countries surveyed in 2017. Available at: [https://www.transparency.org/news/feature/corruption\\_perceptions\\_index\\_2017](https://www.transparency.org/news/feature/corruption_perceptions_index_2017) (15 March, 2019).

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## Social and Cultural Innovation in Sustainable Urban Development

ANNAMÁRIA ORBÁN

**Abstract** Social and cultural innovations have unfortunately received less attention than technical-architectural innovations in sustainable and creative urban development, rehabilitation and regeneration programs. Moreover, the quarter century since the fall of communism in Central Eastern Europe has seen a blossoming of original, grass-roots, bottom-up and spontaneous social and cultural innovations, creative ideas, products, places and services. Since these initiatives and their role in sustainable and creative urban development are rather under-investigated in Hungary and Budapest, this paper takes some steps to fill this research gap. The first part provides an overview of the on-going scholarly debate about the notions of social (and cultural) innovations and their relation to sustainable urban development. The second part describes empirical evidence for the impact – be it positive or negative – of these types of innovations on citizens' quality of life based on documentary and field research.

**Keywords:** • social innovation • cultural innovation • creativity • sustainable urban development

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## 1 Introduction

Cities and the development of human civilizations are, were, and always will be intertwined. Cities have been the cradles of great civilizations and cultures for thousands years, from Uruk in the Fertile Crescent through the Inca Machu Picchu to the European Venice. Cities host more people (54%) today than rural areas, and according to the world population prognosis of the UN, will be the home of the majority of people (66%) globally by 2050 (UN 2014). Cities are complex systems both in a physical and material and metaphysical and immaterial sense. They concentrate economic and political power and breed new, innovative and creative ideas. As Landry puts it, “the city provides a critical mass. It is an accelerator of opportunities and a generator of problems. It is a laboratory for what is good and bad about living together” (Landry 2012, 126). Creativity is the lifeblood of cities, with creative people and organizations at the centre. When individuals come together in one area, they establish a creative milieu, but the real question is how such a milieu comes about and enables cities to become innovative hubs (Landry 2000). As for the development of the creative milieu, Florida (2002) emphasizes the importance of how the physical space itself provides culture-related facilities, meeting places, restaurants, cafes and bars that attract the creative class of workers. While acknowledging the importance of the physical place and space – as we will see in the second empirical case study –, our interpretation is closer to Landry’s “metaphysical” understanding of the creative milieu and cities, with the people, organizations and capacities at the centre establishing creative and innovative places. Thus, accepting his perspective, cities can be considered permanent laboratories of creativity and innovations, and, as this paper will emphasize, social and cultural innovation. Without such developments, we assume, cities could not have arisen, nor could they survive, since the multifaceted problems they generate demand innovative solutions. Moreover, we assume that culture and cultural innovations are the quintessential elements and basis of sustainable and creative cities, present and future.

Cities can be mediating innovation hubs, and/or perfect laboratories – quantitatively and qualitatively large enough for the testing of what is good or bad for communities, being located in-between the macro/national and micro/individual level. From another perspective, it is very important what kind of negotiation and mediation takes place in the urban development policy process to successfully meld “bottom-up,” spontaneous and decentralized social and cultural innovation initiatives with “top-down,” centralized urban development planning and policy.

The first part of this paper attempts to clarify the term social innovation as extended to the field of cultural innovation by describing the results of a literature review which paid special attention to the relationship of the former with sustainable urban development. To support our argumentation, it then seeks to operationalize – to translate into down-to-earth, everyday life – these notions in the form of case studies with the help of qualitative empirical research based on document analysis, field research and structured interviews.

## 2 The conceptualization of social innovation

At the beginning, we should consider the ongoing theoretical and scholarly debate about the concept of social and cultural innovation – whether this is a useful, enduring and theoretically clarified term, or just another trendy but ambiguous buzzword (Pol and Ville 2009; Jenson and Harrisson 2013<sup>1</sup>). The term – and the idea behind it – are not new, since Max Weber in the early 1900s first mentioned "social invention" when examining the relationship between social order and innovation. Later in the 1930s another well-known social theoretician, Joseph Schumpeter, considered social innovation as structural change in the organization of society, or as a change within the network of organizational forms of enterprise (Moulaert 2009; Moulaert *et al.* 2013).

Despite its widespread use in contemporary social science literature, however, the scientific conceptualization and operational definition of social innovation is still under elaboration (Jenson and Harrisson 2013; Moulaert *et al.* 2005 and 2013; Mumford 2002; Pol and Ville 2009). Some authors have acknowledged that social innovation is a "quasi-concept" (Jenson and Harrisson 2013, 15), while others honestly admit that reading and talking about social innovation "do not necessarily make its scientific meaning unambiguously clear" (Moulaert *et al.* 2013, 13).

In the last decade there has undoubtedly been a rise in the number of theoretical overviews of social innovation, many of which were related to social economy, sustainable development and creative cities (Cameron *et al.* 2004; Cohendet *et al.* 2010 and 2011; Deakin and Allwinkle 2007; Landorf 2011; Landry 2000 and 2012; Laville *et al.*, 2007; MacCallum *et al.* 2009; Mieg 2012; Moulaert and Ailenei 2005; Moulaert *et al.* 2005 and 2013; Mumford 2002; Pol and Ville 2009; Rydin 2010). We can also witness an increase in empirical research in the form of a growing number of initiatives and projects funded by national/federal governments: for example, in Canada (Laville *et al.* 2007; Wolfe 2009) and the EU (see, for example, Jenson and Harrisson (2013), or Pisano *et al.* (2015),<sup>2</sup> in addition to some of the latest EU FP7 projects such as SI-DRIVE, TRANSIT, TEPSIE and WILCO).<sup>3</sup>

Nonetheless, the author still continues to observe a "technological bias," both in the interpretation and application of innovation among university scholars and professional experts generally, and in the field of urban development particularly. Both social innovation and what may be termed cultural innovation have unfortunately received less attention than technical innovation, despite their essential role in integrated and sustainable urban development, rehabilitation and regeneration programs. However, cities can be the starting points for sustainable urban development and policy implementation both in a technological and social sense, since they link technological and social innovation, including institutional innovation. When Mieg (2012) links sustainability and innovation in urban planning and development, he stresses both the challenge and potential of urban development for preserving local identity as a major retention factor and resource. To reconcile the seemingly controversial characteristics of

sustainability (preservation) and innovation (radical change in and/or re-combination of resources) he differentiates based on other theoretical concepts two kinds of resources: "core" resources for preserving, and "growth" resources (potential "services") which may be radically changed through urban development. Another concern – also important in later argumentation – is to distinguish between "pure" and "hybrid" types of social innovation, the first having pure public good characteristics – many of them found in civil society and the social economy sector –, and the latter being located in between public and private goods, mostly represented by private/business sector social innovation. When business innovations and social innovations overlap, they can be called "bifocal innovations" (Pol and Ville 2009).

Mumford (2002), when trying to explain this problematic issue through conceptualization, identified several – essentially methodological – factors: social innovations are quite rare and they are typically diffuse, involving multiple partners over rather a long period of time. As such, it is difficult to identify a definite creative act in the end as an outcome. Perhaps one part of this explanation is too general, since it covers changes in social institutions, the creation of new forms of government, social movements and ideological-theoretical revolutions at the macro social level at one end of the social innovation continuum. At the other end of the continuum, however, are micro-level social innovations such as the creation of new processes and procedures for structuring collaborative work, the introduction of new social practices in groups, and the development of new business practices. This perspective is more relevant to this research, focusing as it does on examples of micro-level, practice-oriented social innovation in Hungarian case studies.

There are, however, certain features and characteristics common to scholars' interpretations in the social innovation literature which may serve as a starting point for further discussion. One characteristic approach is to relate the appearance of social innovation in a society (and economy) to unsatisfied needs or dissatisfaction with the present state of the art of social (political and economic) relations, institutions and ideas, often in times of crisis from a historic perspective. Many interpretations associate social innovation with issues of social justice, social integration, the fostering of (local) development and combating social exclusion, alienation, deprivation, or a lack of well-being (Gerometta *et al.* 2005; Moulaert and Ailenei 2005; Moulaert *et al.* 2005 and 2013). Social innovation is often a phenomenon concomitant with the social economy, as social innovation is viewed as a re-introduction of the values of social justice (such as solidarity) into the economy (see for example, Laville *et al.* 2007; Primavera 2013).

### 3 Social innovation and sustainable urban development

Some authors claim that many cities today suffer from various socioeconomic problems due to the crisis of the welfare state and the post-Fordist transformation processes. They also hope that these problems may be addressed by changes in governance structure – an important component of social innovation in the dimension of process – and by increasing



socio-political capabilities and access to resources (the empowerment dimension) with the help of civil initiatives and organizations (Gerometta *et al.* 2005; Lafferty 2004; Moulaert *et al.* 2005; Taylor 2000). It is clear by now that social innovation is an important element of the social economy, and that both are strongly related to the third sector or civil society as they aim at increasing social integration and strengthening social-economic solidarity. In this paper, we treat civil society as an umbrella term, embracing both non-profit and not-for-profit organizations, among the other important initiatives in the "political community" that supplement and "counterbalance" the state and the market. Without exaggeration we can say that the re-appearance of civil society and the revitalization of various non-governmental organizations (NGOs) in the late 1980s changed the course of history, triggering – directly or indirectly – enormous political-economic regime change and the process of democratization of the countries of the Central-Eastern European region, including Hungary.

Turning back to social innovations in an urban context, Taylor (2000) argues that financial capital alone is not enough; human, social and institutional capital are also needed for successful urban regeneration, along with more inclusive urban governance programs. Furthermore, extending the research question to the "happiness of cities," quantifiable empirical evidence has recently come to light (Florida *et al.* 2013) that human capital plays a significant, crucial role at the metropolitan-level of well-being and the happiness of communities: more so than income or other variables (housing, density, climate, commute time, age, etc.).

Employing another perspective, some authors treat civil initiatives, civic engagement, local communities and networks – even "ICT-enabled" ones – as primary elements of alternative or sustainable local and/or urban development (Deakin and Allwinkle 2007; Moulaert *et al.* 2005), placing special emphasis on innovation and creativity in knowledge-based urban economies and urban regeneration programs (Deakin and Allwinkle 2007; Wolfe 2009). Authors also claim that there is a need for a more horizontal, network-based, multiscalar and multi-actor, participatory, inclusive and sustainable process of urban governance and policymaking (Gerometta *et al.* 2005; Lafferty 2004; Rydin 2010), a finding also relevant from the perspective of the present research and its policy implications.

#### **4 Cultural innovation and creativity**

This paper adds two further areas for consideration and analysis. As the title indicates, we included cultural innovation in our empirical research. To clarify the notion itself, we consider the former to be comprised of creative and innovative new ideas, practices, processes and/or changes in the vast field of culture, be they among the normative, cognitive or material, human-made artifacts and elements of culture. In the case studies we emphasize those material and immaterial – or rather, normative and cognitive – elements which enhance the life and well-being of urban social communities. Creativity, on the other hand, is a complex psychological phenomenon involving intuition and reason

(Richards 2010) which may be classified in various ways, such as the "C's and P's" of creativity (ranging from the "Big C" – the eminent and unambiguous creativity of well-known artists and scientists – to the "little C"; the everyday creativity of ordinary people). Depending on which aspect of creativity is being emphasized, four or six P's can theoretically be identified, focusing on *process*, *product*, *person (or personality)* or *place*, – extended by *persuasion* and *potential* (Kozbelt *et al.* 2010). The social context and environment a creative person operates in may be highly important. In social or business environments where grass-roots, everyday creativity can be found everywhere, creativity is a norm and culture in which there may be found many so-called "cultural creatives" (Richards 2010).

Finally, the *place* perspective leads us toward the creative place phenomenon, where "you can feel and sense the buzz" (Landry 2012, 123) which can occur either at the micro-level (a pub, for example) or the meso/macro level (a whole city). We assume that culture and cultural innovation are quintessential elements of any creative city, present and future. We suppose – as a concluding remark associated with a theoretical overview based on Roberts' (2006) findings about the British night-time economy does – that creative places, milieu and cities are not equivalent to "party cities" with youth-based, night-time, dominantly alcohol-related forms of entertainment and "no-go areas"; places that create more negative than positive externalities for local communities and lead to calls for a clearer vision of the creative city and effective policies from various layers of urban/local government.

As mentioned before, the second part of this paper – employing the theoretical findings described above – describes an examination of empirical evidence for the impact of social and cultural innovation on citizens' welfare and quality of life in various sectors. The first case study is an example of "pure" social innovation – with strong public good characteristics – coupled with cultural innovations realized in a civic-public and/or "CPP" (civic-public-private) partnership that unquestionably serves to improve local community welfare. We describe some hindering as well as fostering factors in the diffusion of this innovation, thereby enriching the findings of the earlier mentioned EU WILCO project. The second example is dominantly a cultural innovation with much "little C" creativity, which at the same time represents hybrid or bifocal social innovation in the private sector replicated very rapidly by new cultural creatives and entrepreneurs. Paradoxically, this second example exemplifies both public good and "public bad" characteristics, the latter in the form of negative externalities that affect the life of a close, local community.

In this way, the two case studies mirror each other: the first relating to sociocultural innovation, and the second to cultural-social innovation, but each have their own explanatory power to confirm our initial assumptions. However, both of them can be considered creative urban laboratory products that emerged "from below" that are – directly or indirectly – related to sustainable urban development. Moreover, they are successful socioeconomic and cultural experiments, validated – and replicated – by society and the economy.

## 5 Social and cultural innovation serving the well-being of families with kids

### 5.1 Maltese playgrounds<sup>4</sup>

Our first case study, initiated by a Hungarian civil organization, the Hungarian Charity Service of the Order of Malta, or the Hungarian Maltese Charity Service for short (HMCS), involves "pure" social innovation and has the characteristics of a public good coupled with cultural innovation. At this point, however, it is essential that we extend the historical scope, geographic space and time dimension to include an observation about the 1989–1990 political and economic regime change in Central-Eastern Europe. The re-appearance of civil society, and the foundation and revitalization of various non-governmental organizations (NGOs) in the late 1980s played an essential role in the political-economic regime change and democratization process of the region's countries, including Hungary. Without exaggeration we can say that some of these initiatives changed the course of history, having – directly or indirectly – enormous political impacts on the regime change process. One of the actors was the Hungarian Maltese Charity Service (HMCS), whose foundation and early activities are strongly intertwined with the political-economic changes of the late 1980s in Hungary.

Today, one of HMCS's programs represents a social and cultural innovation, providing empirical evidence for the earlier-mentioned theoretical foundations: it satisfies a social need, fosters social integration, forms part of sustainable urban development and provides the kind of social welfare, as well as cultural services, which are essential for promoting the well-being of many local communities. Basically, it is a pure social innovation with public good characteristics that was founded by a civil organization, relying on both "core" and "growth" resources, the former represented by a preserved urban infrastructure, and the latter socio-educational services.

In 1998 the HMCS initiated a program called "Prevention with playing" and opened (through a "civic-public" partnership) the first of its *Maltese Playgrounds* in a high-rise estate in Óbuda in Budapest's Third District, supported by funding from the government as well as other non-profit organizations. The creative idea of a new type of playground came to the founding fathers' (the President and Vice President of HMCS) minds when they visited a Dutch town in the late 1990s and saw a fenced-in playground with a little house occupied by an elderly female guard. Nevertheless, from the very beginning the initiators wanted to do more. From working in the schools of the district, they were both aware of all the socioeconomic problems and needs of local families. An additional important aspect was that they had (and still have) good relations with the local government (from our perspective this represents positive social capital), which can be regarded as a fostering factor, yielding more Maltese playgrounds in the Third District than in any other in Budapest.

One the most important socio-educational innovations of these playgrounds is the service they provide to the families of the high-rise apartment buildings: social pedagogue

professionals, accompanied by volunteers, offer free-of-charge, cultural-educational day-care activities both for families with small children and for older teenagers. These playgrounds are rather large, fenced off, about 100 m<sup>2</sup> in size, and are open every day – but closed at night – with a covered playhouse shelter where activities and events can be held even on rainy days. They are also equipped with other service facilities, including toilets with a changing table, a first-aid kit and a telephone for emergencies. It is also important to mention that the various youth cohorts have separate places to play peacefully within the grounds, but everybody has to conform to the ethical norms and formal and informal behavioral rules of the Maltese playground, which serve their own interests. Thus, supported by this form of normative cultural innovation, the Maltese playgrounds have a very good reputation in the district as meeting and orientation points for families, mothers and children, who “like them and come, because there are rules”.

It is fair to say that these Maltese playgrounds are most helpful in social terms for local families and sustainable for the whole (prefabricated) housing estate community during school holidays. This is especially true during the long summer vacation when schools are closed and many children wander unattended in the streets, as their parents are working and cannot afford to pay for summer camps or other activities that are offered by the private sector. Many former “Maltese kids” help the social workers as young volunteers with their own programs, such as teaching folk dancing. There are also other social-educational and cultural innovation programs such as the “Playground library stop” where second-hand kids’ books can be exchanged free of charge, and a “Puppy adoption market”.

Beyond the physical existence of these playgrounds, it is primarily the professional expertise and free cultural-educational and community building programs that they offer that help prevent both youth crime and vandalism, and also contribute to the well-being of the people living in the huge high-rise, concrete panel-block estates in the area. Nonetheless, building and especially maintaining these Maltese playgrounds represents a public good: someone has to pay the bill, which is unfortunately a problematic issue, and a hindering factor in terms of their successful diffusion. The annual costs of maintenance are 10–12 million HUF, which may be a – relatively – large portion of the total budgets of certain local governments who are thus unable to engage in such initiatives. This may also be an explanation for their slow diffusion both in Budapest and in the countryside. However, we have witnessed some progressive, bifocal, “CPP” (civic-public-private) social innovations based on social capital in smaller cities, where everyone knows everyone. Creative local governments have found patriotic local businessmen to sponsor the maintenance of these Maltese Playgrounds, primarily for the well-being of the whole community, including themselves and their own kids.

## 6 Creative urban regeneration, reuse and "Cultural creatives"

### 6.1 The success story of Budapest's ruin pub culture<sup>5</sup>

Our second case study focuses on a real mixture of social and cultural innovation, cultural creatives and urban regeneration and represents a successful model of bifocal sociocultural innovation in the private sector. The phenomenon under investigation is a "Hungaricum" (a Hungarian speciality), a well-known, image-building tourist attraction in Budapest and among the top five destinations for foreign visitors, especially for the young people from all over the world who come to Budapest.

This example involves the "ruin pubs" of Budapest and the interrelated and alternative "ruin pub culture" which has been developing for more than fifteen years. Today there are many such establishments around the city concentrated mostly on the Pest side of Budapest, especially in the more run-down parts of the seventh district of Budapest (called Elizabeth-town), full of decaying old apartment houses and courtyards, the original birthplace of this type of innovative cultural and entertainment venue. Since the early 2000s the seventh district has undergone an intensive process of urban rehabilitation and regeneration – although interrupted by the economic crisis of 2008–2009 – which was partly planned and controlled by the local government through (for example) the granting of "re-use" licenses. It was also partly initiated by bottom-up, spontaneous cultural creatives and entrepreneurs who occupied run-down apartment houses otherwise destined to be demolished. The "top-down-bottom-up" interrelationship, however, has not been without conflict since the mid-2000s. Following this time the local government could no longer stand to see the spontaneous mushrooming of ruin pubs and either demolished the decaying houses, or terminated licenses to use them (Csizmady and Olt 2014). The only survivor was our case study example which moved to a privately owned – but also run-down – house and widened its scope of activities to include arts and culture by opening an open-air movie theatre. Hospitality – or as some researchers call it, "guerrilla hospitality," – played a significant role in the establishment of these ruin pubs, but they were more than simple providers of hospitality from the very beginning, becoming cultural focal points and attractions in their own right (Lugosi *et al.* 2010).

For our field research we selected and focused on an analysis of the very first flagship ruin pub, *Szimpla Kert* (Simple Garden) on Kazinczy street, which opened its doors in 2001 and which still exists and thrives to this day, and which is a model for many other cultural innovators and an initiator of this new sub-cultural trend. One piece of empirical evidence for the successful diffusion of this cultural innovation is the rapidly increasing number of ruin pubs on Kazinczy street: twenty-nine have opened in the last fourteen years. Furthermore, this bifocal sociocultural innovation ruin-pub model has been internationally replicated and exported to Berlin where two Szimpla-like venues (under the same ownership) have been opened recently.

Some university students in the early years of the new Millennium wanted to found an alternative, non-consumerist type of underground entertainment venue in which young people could meet, talk and feel a sense of community. The first *Szimpla Kávészó* (Simple Café) was – both in its physical and metaphysical meaning – a real underground place located on Kertész street, in a stuffy basement with little furniture but always full of enthusiastic young people. The first creative insight by the Szimpla founding fathers to start a business was partly spontaneous and partly planned at a very opportune moment because in 2001 there was a temporary vacuum in the underground nightlife scene caused by the closure of two popular youth clubs in the city. At the very beginning it only involved a "let's-see, one-off, spontaneous adventure" of the founding friends, but very soon they realized that they had created something unique and attractive where "you can feel and sense the buzz". Nonetheless – according to one of the founding fathers, still among the most innovative and active owners of *Szimpla* – it was always more than a simple pub: the owners wanted to build a cultural and community centre with a variety of new and innovative cultural and community-building programs (e.g. cultural street festivals), some of them belonging to the field of the social economy (e.g. *Szimpla* Farmers' Market). One of the present owners also founded a civil organization named *Azért* <sup>76</sup> to represent both the interests of the creative entrepreneurs and ruin-pub owners that could mediate between them, the local government, and local inhabitants, and also for the purpose of discussing and settling any conflicts, as well as to somehow formalize their spontaneous participation in the neighbourhood urban development process.

Their vision was realized right after moving to their second location, the first *Szimpla Kert* in Kazinczy Street, which opened on a seasonal basis in an abandoned locksmith's workshop decorated with low-cost, second-hand, re-used furniture and various found objects – such as a Trabant car ("Made in GDR") and old fashioned hairdryers from the 1950s, computers, lamps, gardening tools and living plants – in a very creative, unusual and unique way, smartly balanced between art and rubbish. There are many creative people and designers working in *Szimpla Kert* with Big C and little C creativity, although there is one jack-of-all-trades among them who has a huge imagination and can repair everything. In 2004 – due to the above-mentioned rental-related conflicts with the local government – the venue moved to the present location; another abandoned and decaying, but privately owned one-hundred-year-old house in Kazinczy Street, and widened their scope of activity in the field of culture, becoming more acceptable in the eyes of the local government. Since then, the founders have continuously built their empire, extending the *Szimpla* network of various businesses and initiatives with a clear mission and vision of alternative eco-culture and an urban and sustainable way of living, ranging from the *Szimpla Bringa* (Simple Bike) *Flea Market* of second-hand bikes and gadgets, through street festivals to the local smallholders' *Szimpla Háztáji piac* (Farmers' market) connected to the *Szimpla Háztáji* Slow Food restaurant.

The courtyard of *Szimpla Kert*, full of foreign visitors by night, is unbelievably different on Sundays, becoming an urban market place for organic vegetables and fruit, farm fresh meat, sausages, salami, home-made fruit jams and cordials from local family farms and

small-scale entrepreneurs from the countryside. *Szimpla* farmers' market has become very popular both among environmentally conscious young citizens who come from distant quarters of the city, and elderly locals who enjoy the reasonably cheap, fresh products (helped out with a special discount scheme directly targeting them which also includes other *Szimpla* services). There are usually 35–45 local farmers present, some of whom are very enthusiastic and come only to this market to sell their home-made products because of the fantastic atmosphere. Moreover, within the framework of their community building and educational strategy there are dedicated family and children's events, coupled with "community lunch cooking," where anyone can be a volunteer chef using the market products which are available to create dishes which are then sold to visitors to help finance the initiative. A further part of their cultural-educational and local food promotional initiative is organising wine and *pálinka* (a strong Hungarian spirit, and another Hungaricum) tasting sessions by well-known experts in the *Szimpla Háztáji* slow food restaurant where these home-made products can be found and tasted.

In line with Mieg's (2012) argumentation, we conclude that *Szimpla* as a bi-focal form of sociocultural innovation has somehow become a part of a creative and sustainable urban development project, preserving "core" – architectural-physical – resources, and at the same time creating radically new and innovative "growth" – culturally creative service – resources, which together make up a unique, local identity-building attribute, attracting other creative entrepreneurs, thousands of tourists, and nowadays, old-new real estate investors who have realized the increasing value of the quarter and are polishing up earlier development plans that were interrupted by the financial crisis.

## 7 Public good or public bad?

In an effort to maintain balance, however, we should mention the negative externalities; the disadvantageous features of ruin pubs which have created the ongoing need for conflict resolution tools and mechanisms, be they either cooperative informal solutions or more formal policy resolutions on behalf of the main stakeholders (namely, the creative entrepreneurs and the local municipality). There is permanent, on-going conflict between the ruin pub owners and local residents – third parties, and stakeholders – about late-night noise, littering and sometimes the misbehavior of foreign tourists (sometimes between 10,000 and 20,000 people on a crowded summer night). Obviously, this conflict has come to the attention of local government officials who sought to find a compromise. The mayor of the district, while acknowledging that they had only slowly realized the seriousness and extent of the problem, ruled out closing the bars, since these spontaneous initiatives were making their district more colourful and attractive. Instead, they suggested more strictly enforcing policies for the entertainment quarter based on the local government's official closing policy<sup>7</sup> and increased out-door terrace rental fees, from which they try to financially compensate local residents; for instance, by supporting the replacement of windows with new, better insulating ones. Another socially innovative safeguarding mechanism of the ruin pub owners for preventing littering and decreasing

noise – quite unique in its format – involves the so-called "silence clowns" who patrol the neighbourhood, asking noisy, misbehaving costumers to stick to the rules.

On the other hand, the ruin pub and bar owners – many of them local residents themselves – maintain that, although the influx of visitors has created some problems, the benefits outweigh the disadvantages as the bars earn money and boost property prices in the area.<sup>8</sup> According to a local resident owner, the area had been very quiet for almost fifty years, but the recent changes came so quickly that some people could not get used to them. Truly, on the one hand this spontaneous re-generative development of the quarter brings in money to local entertainment businesses,<sup>9</sup> gives work to many young people<sup>10</sup> who work in the pubs, shops and mushrooming hostels, raises tax revenue for the local government, and increases the property values of local residents.

From another perspective, the over-crowdedness of the area, with noise and littering – the "no-go areas" of Roberts (2006) –, constitutes a "public bad"; a negative externality which diminishes the well-being of neighbourhood residents who can choose between the options of "go-away-quit" or "stay and bear the consequences". Many of them chose the former and have sold their properties – for a higher price, as mentioned, thus being somewhat compensated in a financial-material sense – and have moved to quieter areas of the district or further afield. Others, such as young professionals between 30–40 years of age and students – Hungarian and foreigners alike – have been attracted by the creative atmosphere – despite the above-mentioned negative externalities of the district –, and are continually buying up or renting apartments nearby. Moreover, property owners and real estate investors have revived their earlier development plans and started constructing new apartment houses and hostels. It is a contradiction though, that terminating or closing these ruin bars would create a counter-effect, totally changing this spontaneously started, bottom-up urban regeneration process, leading to a loss of the creative milieu itself, an essential growth resource and factor in the urban development of the quarter.

## 8 Conclusions

Cities such as Budapest are very complex systems, full of individuals and organizations with different views and interests, including those about the planning, development and governing of sustainable and creative cities. Therefore, it is very important what kind of negotiation and mediation takes place during the urban development policy process to meet bottom-up, spontaneous and decentralized social and cultural innovation initiatives with top-down, centralized urban development planning and policy responses.

Nonetheless, we claim – based on document analyses and interviews – that to date there exist no institutionalized fora for negotiation and mediation or meeting places for interested parties where problems can be discussed, conflicts solved and agreement made about sustainable urban development, either at the district or city level. From the first case study we identified a more supportive and inspiring environment in which NGO leaders (the civil sector) had good – though informal – relations with the local government



(the public sector). Moreover, in smaller cities, "where everyone knows everyone" local governments enjoyed supportive relations with local businesses, representing a form of trust-based social capital. This latter turned to be both an essential growth resource and a factor fostering the diffusion of social innovation. In the second case, the private-public, bottom-up-top-down interrelation is not without conflict. There has been a local district referendum in February 2018 initiated by a recently founded local civil group ("For liveable Elisabeth town") about the midnight closing. The referendum was not successful and decisive, as less than 50% (just 16%) of the local citizens voted. However, the conflict was not solved. The dispute is still ongoing between the local residents and the entertainment SMEs whether the ruin bar area is a public good or a public bad?<sup>11</sup>

Finally, learning from our own empirical case studies, as well as from the experiences – either positive or negative – of other creative, culturally innovative and sustainably planned cities (see Cohendet *et al.* 2011; Merkel 2012; Raj Isar 2012; Roberts 2006, among others), we now put forward our own idea for social innovation in local urban governance (on a district and/or city level): the introduction of a permanent, formalized negotiation space; an institutionalized forum for discussion, conflict resolution, and most importantly, for horizontal, participatory and sustainable urban governance. This suggestion is in line with the critical overview and research findings of Scott (2014) about twenty-first century new urbanism, which claims that the enlargement of the urban democratic sphere is a basic condition for the really successful – not self-declared – creative city, and for urban development.

#### Notes:

<sup>1</sup> See for more detail the policy review written by Jane Jenson and Denis Harrison (2013) Social Innovation Research in the European Union, EC Directorate-General for Research and Innovation, later referred to as Jenson and Harrison (2013), available at: [https://ec.europa.eu/research/social-sciences/pdf/policy\\_reviews/social\\_innovation.pdf/](https://ec.europa.eu/research/social-sciences/pdf/policy_reviews/social_innovation.pdf/) (15 March, 2019).

<sup>2</sup> See more detail in Pisano *et al.* (2015) Social Innovation in Europe, ESDN Quarterly report No. 36, April. Available at: [http://www.sd-network.eu/quarterly%20reports/report%20files/pdf/2015-April-Social\\_Innovation\\_in\\_Europe.pdf](http://www.sd-network.eu/quarterly%20reports/report%20files/pdf/2015-April-Social_Innovation_in_Europe.pdf) (15 March, 2019).

<sup>3</sup> See for more detail the web page of these EU-funded projects: [www.si-drive.eu](http://www.si-drive.eu), [www.transitsocialinnovation.eu](http://www.transitsocialinnovation.eu), [www.tepsie.eu](http://www.tepsie.eu), [www.wilcoproject.eu](http://www.wilcoproject.eu) (15 March, 2019).

<sup>4</sup> Sources for this subchapter: official website documents of the Hungarian Maltese Charity Service (Available at: <http://www.maltai.hu/> (15 March, 2019)) and personal communication with László Nagy, Program Coordinator of the Maltese Playgrounds in Óbuda-Békásmegyer (III) District of Budapest (May 2015).

<sup>5</sup> Sources for this subchapter: the official website documents of *Szimpla Kert* (available at: <http://szimpla.hu/> (15 March, 2019) and *Budapest Erzsébetváros Municipality* (available at: <http://erzsebetvaros.hu> (15 March, 2019)) and other internet-based news and resources (available at following websites: <http://7.kerulet.itlakunk.hu/arcok/130524/abel-aki-nem-szimpla>, <http://romkocsmak.hu/index.php?id=blog&cikk=23>; <http://romkocsmak.hu/index.php?id=blog&cikk=18>; <http://index.hu/kultur/2012/11/24/szimplapia> c/; <http://hg.hu/cikkek/varos/11963-szovetsegben-a-romkocsmak>; [http://hetesblog.blog.hu/2016/02/20/elo\\_erzsebetvaros\\_egyesulet](http://hetesblog.blog.hu/2016/02/20/elo_erzsebetvaros_egyesulet);

<http://www.origo.hu/itthon/20150813-maga-ala-temeti-a-romkocsmakat-a-beporgo-budapesti-alberletpiac.html/> (15 March, 2019)), and personal communication with Ábel Zsendovits, one of the founders and owners of “Szimpla”.

<sup>6</sup>Az Élő Erzsébetvárosért Egyesület/For a Living Elizabeth-town, available at: <http://7.kerulet.itlakunk.hu/holmi/legfontosabbak/az-elo-erzsebetvarosert-egyesulet/> (15 March, 2019).

<sup>7</sup> In accordance with the general Budapest-wide rule that from March 2013 bars and restaurants should close after midnight, and should obtain the operational agreement of the given community of local condominiums.

<sup>8</sup> The average flat prices have more than doubled in the last five years in Elisabeth town.

<sup>9</sup> Earning 300 billion HUF per year (Index 2019). Available at: [https://index.hu/belfold/2018/02/18/bulinegyed\\_nepszavazas\\_eredmeny/](https://index.hu/belfold/2018/02/18/bulinegyed_nepszavazas_eredmeny/) (15 March, 2019).

<sup>10</sup> Employing ten thousand people (Index 2019). Available at: [https://index.hu/belfold/2018/02/18/bulinegyed\\_nepszavazas\\_eredmeny/](https://index.hu/belfold/2018/02/18/bulinegyed_nepszavazas_eredmeny/) (15 March, 2019).

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## Teaching Microfinance with the Help of Case Studies

PÉTER FUTÓ

**Abstract** The provision of microfinance for entrepreneurial poor people is a well-known instrument of development policy worldwide. This article describes those concepts of microfinance that are relevant to students on development courses. In particular, the following concepts are described: microfinance, microcredit (MC), micro-deposits and micro-insurance, financial illiteracy and literacy, financial inclusion, the facilitation of micro-entrepreneurship among the poor, female entrepreneurship, creditworthiness, and the sustainability of microfinance schemes. This article summarizes the educational lessons of an EU-financed project "Teaching Microcredit, 2014–2015".<sup>1</sup> This project created the basis for the establishment of a teaching module ("Poverty Alleviation, Social Economy and Microfinance") for students on a Joint Master's Course for Comparative Local Development. The project financed study trips to developing countries. Subsequently, it delivered high-school and university curricula, analyses of microfinance-scheme case studies, visual documents, and a documentary movie for educational purposes. The resulting teaching materials were used in educational pilot activities and disseminated.

**Keywords:** • microcredit • microfinance schemes • micro-entrepreneurship among the poor • "Teaching Microcredit" project • sustainability

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## 1 A conceptual framework of microfinance

Approximately 200 million people around the world benefit from microcredit (Ledgerwood *et al.* 2013). Microfinance institutions (MFIs) take many profit-oriented and non-profit forms: credit and savings associations, co-operatives, NGOs, banks, and even various agencies of local and central governments. Universities and think tanks devote considerable research capacity to microfinance in the context of development economics, with special respect to local development, poverty alleviation (Banerjee and Duflo 2006), financial accessibility, financial literacy, small business development and gender equality.

One of the lessons learnt from the “Teaching Microcredit” Project was that university and high school courses devoted to microfinance should rely on a certain conceptual framework. This chapter is devoted to the identification and interpretation of the most important terms related to microfinance provision.

*Microfinance* is a somewhat wider term than microcredit, and is interpreted as a group of financial services that include *microcredit*; i.e., the disbursement of small-scale loans for entrepreneurial purposes. Microcredit is frequently complemented by *saving* services that are accessible to poor people, also called micro-deposit schemes. Further, the repayment of microcredit is frequently facilitated by features of micro-insurance. Additionally, typical microfinance organizations facilitate the management of microcredit by offering community-based *training and consultancy* services and by organizing self-help groups, which always aim at enhancing the financial and entrepreneurial knowledge of clients, and in some cases create networks of clients jointly responsible for the repayment of micro loans.

In teaching microcredit a suitable unit of analysis is the *microcredit scheme*, which is interpreted as the set of rules governing eligibility, guarantees, the disbursement and repayment of microcredit, and the institutional-organizational framework established for implementing these rules. A microcredit scheme is a model which may be applied by several existing and operating microfinance institutions in a particular country. Some of these schemes may be institutionalized as the financial components of agricultural, craft, trade or other sectoral development projects. Other schemes may be utilized by NGOs, banks or other financial institutions that offer small-scale loans to start-up firms, without any sectoral delimitation. The rules and implementing institutions of these schemes may be determined by governments and international organizations that provide soft loans to microfinance retailers. Finally, other microcredit schemes might be implemented by informal organizations based on local traditions of mutual financial help, such as Rotating Savings and Loan Associations or Islamic Banking.

Any particular microcredit scheme can be characterized by:

- The conditions of eligibility;
- The limitations of use of the credit (e.g. only for entrepreneurial projects);

- The average, minimum and maximum of the volume of individual credit;
- The interest rate;
- The existence and extent of securities and guarantees of repayment, with special respect to group guarantees and collateral;
- The extent and content of the accompanying business services offered to clients; and
- The policy area in which the investigated microcredit programme is used as an instrument (e.g. poverty alleviation, small business development, agricultural development, female empowerment, the empowerment of vulnerable ethnic groups or castes, etc.).

For educational purposes, it has been found useful to differentiate between two types of microcredit, namely *social and commercial* microcredit, albeit recognizing that there is a continuous spectrum between these two basic types. A series of case studies may be used to describe both types and to identify those cases where a microcredit scheme which was originally designed as an instrument of social policy has changed into a profit-oriented commercial enterprise.

*Social microcredit* is an innovative instrument of poverty alleviation. Social microcredit as a rule relies on the ideology that microcredit is a human right, thus society must consequently offer this opportunity to everyone, including poor people, as an act of solidarity. Social microcredit schemes are mostly operated by NGOs, by informal and formal savings associations, or by donor-driven temporary projects. These schemes usually disburse credit with a low interest rate, and do not require guarantees besides group guarantees and informal securities such as social capital, with special respect to trust. Such schemes in many cases are relatively permissive in the case of non-repaying borrowers. Theoretically, social microcredit schemes should be non-profit initiatives. In practice, their economic sustainability typically depends not only on sound management principles, but also on external grants or subsidies.

*Commercial microcredit* schemes are profit oriented. The declared aim of such schemes is the development of small enterprises by providing financial services to them. Most commercial microfinance schemes are economically sustainable because they apply a market-level interest rate, require various types of guarantees, and implement strict procedures in the case of defaulting borrowers. Commercial microcredit schemes are operated predominantly by financial institutes, including banks, but there are many borderline instances in which such schemes are offered by local associations, co-operatives and foundations. The typical target groups of commercial microfinance schemes are not necessarily poor people, but rather the entrepreneurial families of the middle-class.

*Connections with financial policy.* Governments in most countries regulate microfinance provision for the following purposes:

- To safeguard the financial stability of microfinance institutions, with special respect to ensuring the prudence of micro-deposit collection and micro-insurance;
- To establish the institutional framework for channeling government subsidies;
- To open the way to private loans / investors / donors by creating fair competition on micro-credit markets.

## 2 Issues under discussion

Debates about how to develop the microfinance sector exist in almost every country. Moreover, there is a growing body of professional literature which questions the relevance, usefulness and even the *raison d'être* of microfinance. The educational project has inevitably been confronted by various issues that critics (Bateman and Chang 2012), apologists (Yunus 1999), and scientific investigators of microfinance have discussed over the last three decades. The teaching of microcredit must touch upon these issues, many of which have served as research questions in scientific publications and dissertations. Indeed, many students of local development have investigated microcredit provision in their respective home countries in their dissertations, tackling one or more of the research questions listed below:

- Which types of microcredit programs are economically sustainable, and which types are donor dependent?
- Some microcredit schemes ask users to pay relatively high interest rates and require guarantees/ securities: is this compatible with the principle of poverty alleviation, and can these schemes be regarded as part of the solidarity infrastructure of the particular country?
- Is group lending feasible and sustainable? Is it moral and efficient to share the responsibility for repaying microcredit among various individual debtors?
- Is it acceptable to put moral pressure on defaulting debtors by using their existing social capital and social networks to coerce them to repay microcredit?
- Is it a feasible goal to turn a wide strata of poor people into successful self-employed persons and entrepreneurs with the help of small loans accompanied by some entrepreneurial training and consultation? Alternatively, is this outcome feasible only for a narrow group of persons?
- Microfinance is only one of the possible instruments for creating jobs locally – what are the other, competitive approaches and which ones are more efficient?
- Can microcredit projects effectively alleviate and eventually reduce poverty? If yes, under what conditions?
- Is the impact of poverty alleviation measures measurable? Are the methods of randomized impact evaluation appropriate for assessing the poverty-alleviation impact of various microcredit schemes?
- Is commercial microcredit an instrument of social policy, or rather an instrument of SME development policy, or is it just a policy-independent financial product sold to entrepreneurial lower/middle-class clients?



- What is the optimal role of microcredit in financing small businesses? Should microcredit offer help only during the incubation of a business, or should working capital be periodically renewed with no defined end? In other words, should microfinance institutions avoid the long-term dependence of individual small businesses on microcredit?
- What are the specialties of microcredit provision in different cultures? In other words, how may we take into consideration cultural differences and informal and formal traditions of credit provision?
- Is it rational to compare the microcredit markets of a developing country with the microcredit market of a developed country?
- Is it rational to compare a social, non-profit microcredit scheme with a commercial, profit-oriented microcredit scheme?

### **3 How may we compare microcredit markets and schemes?**

Case studies are excellent educational instruments for highlighting, demonstrating and illustrating the above concepts and theories of microfinance. The project described in the introduction identified rich empirical material for comparing different types of microcredit schemes.

Microcredit schemes can be compared according to certain criteria, such as by:

- Identifying the beneficiary (or client) sectors, which are predominantly agriculture, crafts, and trade;
- Identifying the types or legal forms of targeted organizations, which are predominantly small enterprises, social enterprises and farming families;
- Identifying the typical parameters of MC provision; i.e. the sources of refinancing, the interest rate, the maximum and average interest rate;
- Describing the rules for guarantees; i.e., trust, social capital (e.g. group guarantees) or physical securities pledged as loan collateral (e.g. a house, or household objects);
- Describing the services that accompany microcredit provision, such as entrepreneurial training and consultancy, the organization of self-help groups, business facilitation by authorities (e.g. legal / administrative help in obtaining permits or complying with tax rules);
- Describing the policy interventions implemented to improve the entrepreneurial environment, such as the issue of microfinance regulations which enable microfinance organizations to collect deposits and sell insurance policies.

### **4 The case-study schemes**

The following two archetypal schemes were investigated in a North African country. Both schemes serve hundreds of thousands of families, farms and small enterprises.

In the North African country under investigation, the tradition of microcredit provision dates back a quarter of century. State intervention strengthened in the 1970s and 1980s with the establishment of state-sponsored regional development programs and urban development programs which assisted with employment creation through the promotion of handicraft and small-scale trading. Subsidized credit was the main mechanism of these intervention programs. In the 1990s, a series of regulations were issued specifically to establish and support the institutional framework of microcredit provision. By the year 2010, the country had developed a large microcredit market. The country is now host to a wide range of microcredit organizations which offer various types of microcredit schemes. The following paragraphs compare the two biggest of these. Micro- and family businesses in the country play an important role in the national economy with special respect to employment generation. The country is predominantly agricultural, therefore most businesspeople are farmers, but traders and artisans also play a significant role in the social fabric of settlements. The contribution of informal small businesses to employment creation and income creation is substantial in international comparison.

However, despite the combined efforts of the state and the private sector, the penetration of the microcredit sector remains limited and most of the target customers are excluded from funding. Despite the growth in the number of microcredit associations and their full territorial coverage of all the administrative districts of the country, the majority of micro-entrepreneurs eligible for micro-credit are still excluded from funding and suffer from problems with accessing finance.

*“Microcredit Scheme A”* functions according to the principles of social microcredit, which were enshrined into a microcredit law issued at the end of the 1990s. At the same time, a big state-owned bank and a guarantee fund were created from budgetary sources: these institutions guarantee the financial sustainability of this system. Loans are offered by a wide range of local associations, and a network of local offices covers the whole country. The refinancing of these associations by the above-mentioned state-owned bank occurs at preferential, subsidized interest rates. Additionally, the maximum interest rate for microloans has been fixed at 5%; i.e., at a rate much lower than the market interest rate, and the maximum size of loan permitted was also fixed per government decree. Microcredit associations are politicized in the sense that the members of the steering committees need to have the support of regional and local authorities. Microcredit associations have become a vehicle for promoting social harmony through maintaining subsidized interest rates. The beneficiaries of the scheme are predominantly agricultural farmers and artisans, and preference is given to start-ups. The scheme also supports social enterprises, entrepreneurs who create workplaces, and the generally financially underprivileged strata of society. Women represent almost half of the clients of Scheme A. Women micro-entrepreneurs are considered more creditworthy, thus their funding requests are more readily accepted. As to the regional distribution of funds, applicants in less developed regions are more likely to receive micro-credit from microcredit associations than those in developed ones. Microcredit is frequently offered to families located in the vulnerable strata of society and also for projects that combat desertification.

*“Microfinance Scheme B”* started as an international NGO in the early 1990s, but was exempted from the stipulations of the microcredit law; i.e., it was not constrained by the official ceiling on interest rates (5%). Scheme B has benefited from a special permit which has allowed it to provide small loans by charging a high enough interest rate to cover its costs. Consequently, the scheme was able to borrow money both from international development organizations and commercial banks. In the early 2000s, due to the development of the regulatory framework, its legal form was changed into a limited liability company. Today it is the biggest of the microfinance institutions in the country. The interest rates applied by Scheme B go up to 25%, huge compared to those of Scheme A (maximum of 5%). Nevertheless, the repayment rate of Scheme B is almost 100%. Each time that a borrower repays their debt, they become eligible for new credit of a somewhat higher volume. Most borrowers want to maintain use of this scheme and use the loans without collateral offered by Scheme B as a source of working capital. Scheme B pays VAT and other taxes to the state. Scheme B has hundreds of thousands of borrowers, predominantly small businesses active in retailing and handicraft. The clients of Scheme B are predominantly female borrowers. The loan officers of Scheme B visit regularly clients and advise them on financial management issues related to their firms. The renewal of the loans may depend on whether the clients follow this advice.

In the investigated country there is wide consensus about the ultimate goal of microfinance: to develop a countrywide network of sustainable financial services for micro-entrepreneurs that enables them to better integrate into their socioeconomic environment. In spite of this consensus, there is still a very lively debate about the development of the sector. The inevitable shift towards commercialization has significantly increased the divergence of views about the microfinance industry and microfinance policy.

Due to some overlap of their target groups, the two schemes compete with each other. Since financial regulations regarding microfinance change frequently, the conflict between commercial and social microcredit organizations is demonstrated in their respective lobbying activity. Representatives of social microfinance have accused commercial schemes of being profit oriented and operating outside the “solidarity infrastructure” of the country. On the other hand, representatives of the leading commercial microcredit scheme have accused the incumbent social microcredit schemes of being donor-dependent, bureaucratic, and occasionally becoming instruments of local power policies. At the time of the educational project (described earlier) there was a strong and unsatisfied demand for microfinance products that microcredit associations based on the social microcredit model were unable to meet, and the commercial microcredit scheme was considered to be more successful and better disseminated than the social microcredit scheme.

## 5 Conclusions and recommendations

The provision of microfinance to enterprising poor people, if properly done, is a widespread and efficient instrument for international development which is worthy of analysis and study at various levels of educational institutions. The visibility and acceptance of microfinance in schools and universities can be enhanced by analyses of the microfinance schemes of various developing countries based on professional literature and on fact-finding interviews with experts from microfinance institutions and their beneficiaries. The respective teaching activities should rely on specially trained trainers, curricula, textbooks, online sources and visual resources.

The examples of commercial microcredit schemes investigated herein support the hypothesis that commercial microcredit can be sustainable, and even profitable, but the target group is predominantly not the poorest stratum of society. On the other hand, the project could not find any social microcredit schemes that were not donor-dependent. Both types of schemes are efficient at creating jobs for the self-employed and, to some degree, additional, sustainable workplaces. The associated social cost per workplace created is relatively low, therefore microfinance schemes contribute to local development.

Both social and commercial microcredit schemes are legitimate and useful, because they:

- Improve the chance of self-employment for the poor;
- Promote local development and gender equality;
- Replace usury (moneylending);
- Fulfil a huge demand for both types of lending.

For the above-described reasons, the deliverables of the project advocate sustaining both types of microcredit schemes as efficient, parallel and overlapping instruments of poverty alleviation and small enterprise development. The microfinance markets of Europe and those of developing countries are comparable. The structure, dynamics and causes of poverty in Africa, Asia and the developed world are analogous to a large extent. A global development strategy for poverty alleviation that uses microfinance provision as an instrument makes sense and is feasible. Local poverty alleviation strategies should follow international recipes and national best practices in an adaptive but locally innovative way.

**Notes:**

<sup>1</sup> The “Teaching Microcredit” Project was sponsored by the "Development Education" programme of the EU Commission, implemented by a consortium of European universities and NGOs. Italy: Gruppo di Volontariato Civile (consortium leader); University of Bologna; Bolzano Autonomous Province. Hungary: Hungarian Baptist Aid; Corvinus University of Budapest. Spain: Loyola University Andalusia, Fundación ETEA para la Cooperación y el Desarrollo; Asociación Consorcio de Cooperación, Cordoba.

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## **Evaluation Projects and Programmes**





## Equal Opportunities and Investing in Children: Theory, Policies and Projects

ILDIKÓ HUSZ & ÉVA PERPÉK

**Abstract** The paper first focuses on the theoretical embeddedness of the problem, involving human, cultural and social capital theory, as well as social inclusion and exclusion theory. The second part is devoted to an overview of the respective international conventions, recommendations, and policies. Then the paper shifts to Hungarian national strategies aimed at reducing child poverty and their local implementation. Finally, the last section presents a Hungarian case study of two local development programs from a comparative perspective. The local projects are part of the national Program to Combat Child Poverty that is designed to improve the life chances of children at risk of poverty and social exclusion. The comparative analysis investigates the local programs' responses to similar problems, the types of interventions and services they provide, and the forms of human and cultural capital investment they have made. Special emphasis is put on comparing local programs across different intervention areas on behalf of the Roma from the point of view of their attempts at integration and inclusion.

**Keywords:** • human • cultural and social capital • social inclusion and exclusion theory • child poverty • policy • intervention

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## 1 Introduction

As children are the future of society, investing in children has long been a crucial element of theoretical debates, research projects, national and international policies, as well as of local and global development programs. According to a relatively new socio-political approach, a preventive and child-centred social investment strategy is liable to be more productive than one which compensates for already existing disadvantages or attempts to reduce unfair differences.

In terms of children's equal opportunities, early child development has been proven to be especially effective and profitable in the long term, contributing to better health conditions, greater school attainment, more favorable job market positions, and a lower deviance rate (see the Head Start program in the USA, or the Sure Start program in the UK).

Child poverty and social exclusion constitute a major problem around the world because the increasing wealth of developed countries does not automatically lead to the more just distribution of goods, to more equal opportunities, or to strengthening social inclusion. In the case of minorities, especially Europe's largest ethnic minority, the Roma, the situation is even more complex. The Country Reports of the European Union regularly show that the Roma are more typically characterized by extreme poverty, poor housing conditions, poor education, and lower job-market activity than members of mainstream society.

Our study is mainly based on the analysis of some key documents produced during the program – i.e., on the application documents of local projects, on complex local studies that explored the sub-regions' economic, social and institutional status, on reports about the results of sub-regional surveys, as well as on mid-term and final evaluations of the implementation of the aforementioned program. These documents rely on both secondary and primary data sources.

## 2 Theoretical background

The life chances of children are determined by their “capital-abilities”<sup>1</sup> (Foucault 2008, 229), i.e. by their acquired human, cultural and social capital. Thus, investing in children is a rational social strategy for fostering equal opportunities (Esping-Andersen 2008). Investments can be realized in several fields. From the perspective of the local development program investigated in this paper, expenditures on children's human, cultural and social capital are the most appropriate social investments.

## 2.1 Human and cultural capital

The topic of human capital investment through formal and informal education has inspired a number of scientists since the 1950s, among them several Nobel laureates.<sup>2</sup> The basic observation is that more educated people have higher earnings than less educated ones. Theodore W. Schultz (1961) argues that investing in conventionally accepted physical capital is not profitable enough without large-scale human capital investment. Human capital investment improves personal knowledge and skills so that it boosts the productivity of labor, raises individual incomes, and drives economic development as a whole. Human capital growth can be primarily realized through health-care services and education. According to this reasoning, investing in health-care, education and training is more lucrative in the long run than investing in physical capital.

Some years later, the term “human capital” was effectively and genuinely disseminated by Gary S. Becker in a book entitled *Human Capital* published in 1964. Becker provides a concise, rational-choice-based definition of the term and gives several examples of it: “... activities that influence future monetary and psychic income by increasing resources in people. These activities are called investments in human capital. The many forms of such investments include schooling, on-the-job training, medical care, migration, and searching for information about prices and incomes. ... all these investments improve skills, knowledge, or health, and thereby raise money or psychic incomes” (Becker 1994, 11). Becker’s theoretical assumptions were tested using several empirical models. The author puts special emphasis on education and its costs and benefits are embodied in his estimations. For instance, Becker (1994) measured the economic effects of college and high-school education in the United States in the twentieth century.

Cultural capital is used in a broader sense than human capital, so that in a way sociological cultural capital concepts have colonized human capital ones. Thus, human capital and cultural capital theories are semi-overlapping approaches – although Bourdieu warned us not to confuse the two (Bennett and Silva 2011). Cultural capital theory was first introduced by Pierre Bourdieu and Jean-Claude Passeron in 1977. Some years later, Bourdieu added sophistication to the initial theory by differentiating between economic, cultural and social capital. In the latter’s understanding, cultural capital is basically institutionalized in educational qualifications (Bourdieu 1986, 242–243).

Cultural capital exists in three different forms; namely: “*in the embodied state, i.e., in the form of long-lasting dispositions of the mind and body; in the objectified state, in the form of cultural goods (pictures, books, dictionaries, instruments, machines, etc.), ... and in the institutionalized state, a form of objectification which must be set apart because, as will be seen in the case of educational qualifications, it confers entirely original properties on the cultural capital which it is presumed to guarantee*” (Bourdieu 1986, 243). Cultural capital depends on the field or system of social positions in which the person is embedded.<sup>3</sup> It is embodied cultural capital which is the most difficult to transmit

and may become a part of a person's habitus.<sup>4</sup> Thus a person's position basically depends on the amount and quality of capital they possess, personal habitus, and the related field.

## 2.2 Social capital

A long-debated concept, social capital was probably first thematised explicitly by Lyda J. Hanifan in 1916 (Putnam 1995).<sup>5</sup>

According to Bourdieu (1986, 248), social capital is the sum of actual and potential resources which are related to group membership. Bourdieu (1986) gains everlasting merit for his formulation of capital conversion theory. While economic capital is the fundamental form of capital, at different costs all three types of capital can be mutually converted. Bourdieu discusses the multiplication effect of social capital, as an individual can positively benefit from the members of their social networks.

In this paper, social capital is used in the same sense as James S. Coleman (1988) uses it: *"... social capital inheres in the structure of relations between actors and among actors. It is not lodged either in the actors themselves or in physical implements of production"*. In addition, social capital serves as *"a resource for persons"* (Coleman 1988, 98). In Coleman's theory there are three main forms of social capital; namely, obligations, expectations and the trustworthiness of structures; information channels; and norms and effective sanctions. Coleman (1988) puts special emphasis on social capital within the family and outside it and argues that social capital plays an essential role in school performance; i.e., in the creation of cultural capital.

The opportunities and life chances of children are predefined by multifarious capital abilities and access to diverse sources of capital. Besides investing in the more obvious elements of children's human capital (improving health status or educational attainments, etc.), the local development programs we investigate are aimed at developing the psychological and social well-being of children through improving personal and social skills and competences such as authenticity, self-confidence, self-consciousness, self-reflection, ambitions, interaction, persuasion, adaptation, coordination, cooperation, etc. These characteristics can be regarded as inevitable parts of cultural capital and are undoubtedly related to the social capital a person possesses as well. On a community or societal level, social networks and social capital correlate with social integration, inclusion and exclusion.

### 2.3 Social exclusion and inclusion

Social exclusion is a much broader concept than poverty because it may refer to active or passive capability deprivation (Sen 2000) of a series of: private or public; material, immaterial or abstract; subjective or objective goods, spaces, services, relations, rights, chances, etc. (authors' own definition based on Mathieson *et al.* 2008).

In the present sense, social exclusion was first used by Jean Klafner in 1965 (Allman 2013) and René Lenoir in 1974, although its roots may date back to the social cohesion and solidarity theory of Émile Durkheim [1893] (1997) (Mathieson *et al.* 2008), the theory of Adam Smith (1776) or even Aristotle (Sen 2000). In the 1980s, the European Commission started to use the rhetoric of social inclusion to counter exclusion (Allman 2013). Emphasis on promoting inclusiveness and inclusivity is still easily detectable and persists within the policies of the European Union.

The renewed academic popularization of the concept of social exclusion started with Amartya Sen. Based on Sen (2000, 5–6), the right approach to poverty leads through social exclusion and stresses the relational features of capability failures. According to Sen's argument, an excluded population is produced (e.g. due to long-term unemployment) which can lead to skill and/or motivational loss, loss of freedom, and/or social relations, psychological harm, clinical illness on a micro level; as well as loss of output, and the creation of gender and/or ethnic inequalities, weakening social norms on a macro level (Sen 2000, 19–22). In contrast, inclusive tendencies are indicated if excluded individuals and/or groups are being involved and genuinely integrated into the welfare system, education system, or labor market. Active labor-market positions, school attendance, or other – e.g. civil, voluntary – activities are vital elements for ensuring social inclusion.

Social exclusion may lead to less opportunity to possess the social capital necessary for a successful life. The labor market, educational or territorial exclusion may limit interaction between those who are excluded and the majority, making it more difficult for the former to access some useful information channels, to acquire the appropriate behavioral patterns and social norms, as well as to gain the trust and recognition of others. Moreover, the existence of social exclusion, especially in the form of racial discrimination, affects the value of possessed capital, as well as *“the efforts by individuals to activate their capital, the skill with which individuals activate their capital, and the institutional response to the activation”* (Lareau and McNamara Horvat 1999, 3).

Consequently, tackling (child) poverty and breaking the cycle of disadvantages can be done only by going beyond material security and *inclusively* investing in children's human, cultural and social capital. In accordance with *Europe 2020. A strategy for smart, sustainable and inclusive growth*, this conclusion leads us to the next chapter.

### 3 Respective international conventions, recommendations and policies

Children's rights and their well-being have been the focus of international interest for many decades. Proclaiming that there is a particular need to strengthen care of the child, the League of Nations adopted the *Geneva Declaration of the Rights of the Child* in 1924, and the United Nations General Assembly extended it in 1959. After another thirty years, the next milestone was the United Nations *Convention on the Rights of the Child*, adopted in 1989.

In the European Union, as part of the Social Investment Package (2013), the *Recommendation for Investing in children – breaking the cycle of disadvantage* is a European Commission policy response to child poverty and exclusion, adopted on 20 February 2013. It advises member states to “*organize and implement policies to address child poverty and social exclusion, promoting children's well-being ...*”. (Investing in Children 2013, 6). The Commission recommends that Member States develop integrated strategies based on three pillars; namely, access to adequate resources, access to affordable quality services, and the right of children to participate.<sup>6</sup> The main channels/measures for tackling the above-described aims are family support and benefits, quality childcare, and early childhood education. The Recommendation also highlights the issue of social inclusion: “*The most successful strategies in addressing child poverty have proved to be those underpinned by policies improving the well-being of all children, whilst giving careful consideration to children in particularly vulnerable situations ... such as Roma children, some migrant or ethnic minority children, ... as well as children within households at particular risk of poverty, such as single parent or large families ...*” (Investing in Children 2013, 5).

In order to guarantee the inclusion of children of ethnic minorities, especially Roma children, the European Council formulated 10 Common Basic Principles on Roma Inclusion<sup>7</sup> (Council Conclusions on Inclusion of the Roma 2009). From the point of view of the *Recommendation for Investing in children*, two of them are particularly relevant: Explicit but not exclusive targeting (Principle No 2) and Aiming for the mainstream (Principle No 4).<sup>8</sup> *Explicit but not exclusive targeting* defines “*Roma people as a target group but not to the exclusion of other people who share similar socio-economic circumstances*”. *Aiming for the mainstream* means that the main goal of all Roma-related policies should be to integrate the Roma into mainstream society, while Roma integration should be mainstreamed into national policies instead of being handled as a separate issue.

To achieve their objectives, all related documents promote the mobilization of various financial and non-financial EU instruments – inter alia, the European Social Fund, which also finances the Hungarian Programs to Combat Child Poverty, among others.

#### 4 Hungarian national strategies aiming at reducing child poverty and their local implementations

Twenty per cent of Hungarian children live in income poverty; this proportion is essentially the same as the average for the EU28 countries (21%). Considering other indicators, such as the labor-market position of parents and material deprivation, we observe that poverty or social exclusion affects 34% of children in Hungary compared to the EU average of 26% (Eurostat 2016).

In Hungary, child poverty is highly concentrated in the most deprived regions: in these areas not only is the number of people living in poverty higher, but the accumulation of disadvantages is also significantly greater than in other, better-off areas of the country. The proportion of students with multiple disadvantages<sup>9</sup> is 20% in the most deprived northern and north-eastern counties of Hungary, while less than 1% in the economically most developed areas, including the capital and Western Hungary (KSH STADAT 2016).

In 2007, realizing the need to reduce child poverty and promote equal opportunities for children, the Hungarian parliament unanimously approved the *National Strategy to Combat Child Poverty* (“Child Strategy”) which determines the main areas where intervention is needed to improve the situation of children. The national strategy corresponds to international conventions and recommendations with special regard to the United Nations’ *Convention on the Rights of the Child* (1989) and *Millennium Development Goals* (2000). The major development objectives identified in the Child Strategy were to improve the situation of families with children in terms of income, employment and housing conditions, and to improve the quality and availability of education, social and health services targeted at children. It also formulated several horizontal objectives, such as reducing the disadvantages of localities, improving the living conditions and alleviating the segregation of the Roma, strengthening children’s rights, and promoting cooperation among sectors. In 2011, the Child Strategy, originally designed to last 25 years, was merged into the new National Social Inclusion Strategy<sup>10</sup> which integrates ideas aimed at reducing child poverty, Roma integration, and balancing regional disadvantages.

This change in addressing child poverty does not only mean that, in concordance with the growth strategy of the European Union, the latter document remains effective until 2020 (that is, for a maximum of 10 years). A certain shift of emphasis can also be detected in the targeting logic and means of intervention, such as decreasing the priority of maintaining the real terms of the financial support provided to families, awarding prevalence to the principle of *exclusively supporting the poor* instead the former principle of “expressed but not exclusive” support, as well as predominantly using a project-based intervention logic (see also Ferge 2014). The latter means that the strategy aims at creating solutions to specific problem areas by launching several short-term projects chiefly financed from EU structural funds.

The regional Program to Combat Child Poverty work in line with the Child Strategy to reduce inequality between territories. These projects are financed by the European Social Fund to increase the chances of deprived children in each of the regions. Within the framework of the program that ran from 2009 through 2015, a total of 23 of the most deprived sub-regions<sup>11</sup> were granted financial aid for the duration of 2–3-years, through three tenders, to enable them to elaborate and implement their own equal opportunities projects.

From a developmental point of view, the regions participating in the Programs to Combat Child Poverty have been and are facing very much the same problems: all have (child) poverty rates above the country average, a high unemployment rate, low incomes, and high indices of material deprivation. The education level of the adult population is lower than the country average, just like children's school performance. Most of the 23 sub-regions are located far from the capital, in the periphery of the country (see Appendix), where even the county centers are only accessible with difficulty from the settlements. Several regions are constituted by small villages of fewer than 500 inhabitants, with a settlement structure characterized by a lack of cities,<sup>12</sup> which makes access to educational, health-care and social services very uneven. In most cases, nursery, family day-care, secondary school, outpatient specialty care, and pharmacies can be found only in the settlements which function as sub-regional centers. There are far fewer professionals than needed: there is a shortage of special needs teachers, developmental teachers, speech therapists, child psychologists, physiotherapists; several localities lack pediatricians, and children's specialists are often unavailable even at the regional level. The best established networks are those of health visitors, family support services, and child welfare services; however, their activity is often limited to the provision of a minimum level of services due to the lack of capacity.

Due to the outward migration experienced in these regions in the last decades, many of the settlements have been ageing and depopulating. Some of the empty houses have been bought by poor, mostly Roma families who were attracted to these localities by low real estate prices. This population swap has led to a further decrease in real estate value, triggering a process of ghettoization, in many places by now irreversible. Social (and ethnic) segregation has been increasing not only in villages but also in the cities that function as regional centers. These typically peripheral neighborhoods have even worse access to quality human services. In these areas many families face multiple educational, social, housing and health problems, but the availability of precisely those services which would be extremely important to them is lacking.

To address these issues and insufficiencies, the Program to Combat Child Poverty has defined the objective of improving the availability of services for families with children to reduce overload and to enhance the performance of basic service providers, as well as to strengthen the cooperation between them. By specifically targeting the most deprived regions, this plan can contribute to the national Child Strategy primarily by decreasing



territorial inequality, by developing major social support systems (public education, health-care and social services) locally, and by improving inter-professional collaboration.

Tenders for the implementation of regional Program to Combat Child Poverty were designed as follows: initially, five, later another six, and finally fifteen more sub-regions<sup>13</sup> were invited to apply. As we have already mentioned in relation to the national strategies, the political environment of the program against child poverty had changed in the meantime, as is also reflected in the differences in the invitations to tender. In the first tender, the target group of the program included children and their families living in each region, with priority given to those with social disadvantages and the Roma. In the third call, the definition of the target group already specified disadvantages, including Roma ethnicity, that determined the direction of the eligible interventions. Compulsory activities were increasingly focused on the most deprived children, with the well-known over-representation of the Roma, and the call for tenders directly referred to the concept of ethnic (Roma) ghettos where program activities were compulsorily assigned. This means that, in spite of the program being originally defined as “color-blind,” (free from any direct ethnic targeting), this principle eventually lost its validity.

Below, we will evaluate the programs of two anonymous but real sub-regions: Sub-region “S” and Sub-region “E”. From the regional programs described below, the project for Sub-region “S” was awarded in the first call in 2010, while that of Sub-region “E” in the third call in 2012. This enables us to take a closer look at the impact the two different approaches had on Roma integration. We will examine to what extent each program managed to reach children with multiple disadvantages, and particularly the Roma among them, and whether the children were involved in segregated or integrated ways.

## 5 Data source and methodology

The complex regional programs were accompanied by a mentorship program that provided professional-methodological support for the regional implementers. The authors of this study worked in these mentorship programs doing documentary and empirical research, and preparing situation analyses and evaluations with regard to the progress and success of the regional projects. Our study was based on the following information sources:

- Invitations for tenders as frameworks for the local Programs to Combat Child Poverty, declared objectives, and the set of applicable resources.
- Regional analyses made by the mentorship program and disseminated in the publication *Sub-regional Mirror (Kistérségi tükör)*, explicating the situation, needs and demands of local institutions. These documents formed compulsory parts of the regional tenders, and helped with project planning.

- At least one survey (“Needs assessment”) was conducted in each region to assess the situation, needs and demands of families with children. The results were published in studies; here we only use the data needed for the description of the regions.
- Each local project was submitted to a mid-term and final evaluation (“evaluations”) based on two main data sources: processed interviews with local stakeholders on the one hand, and information collected from beneficiaries of the services launched during the projects on the other. These evaluations were primarily intended to assist with project implementation in each region, occasionally relying on non-public information – therefore the evaluations themselves are not public either. However, an extensive summary of the evaluations in Hungarian (Husz 2016) as well as an excerpt about the experiences of the program in English are available to the public (Bauer *et al.* 2015).

For the purposes of this paper we used the above-described documents to gather information about the two selected regions and performed a secondary analysis of the evaluations.

## 6 Case studies

### 6.1 The program in Sub-region “S”

Sub-region “S” is typically composed of small villages: 20 of its 27 settlements have fewer than 500 inhabitants, and the centers are small towns with populations hardly exceeding 3000. The economy is predominantly based on forestry and agriculture, and additionally some smaller industrial plants and public institutions offer local employment options. In the past, a significant part of the population used to commute daily to the nearby mines and heavy industry plants, which however were closed one after the other upon the political transition of 1989. As evidence of this prolonged employment crisis, the census of 2011 – coinciding in time with the launch of the program – registered an employment rate of as little as 52% among people aged 18 to 59, which was significantly below the national average of 66% (KSH TEIR 2019). Low employment rates in the region led in turn to a significant rise in child poverty rates: 43% of the children living in this region had become poor due to low income, compared to the national average of 26% (MTA TK 2011 and 2013). Only 10 settlements had kindergartens, with two-thirds of children from disadvantaged families; the share of children with multiple disadvantages was 37%, even exceeding 50% in four settlements. Deprived children were represented in high proportion in the five primary schools of the region as well. Pupils of the regional schools regularly performed under the country average on national competency assessments, with absences above average, and schools awarding baccalaureates in lower numbers. According to the estimates of the *Sub-regional Mirror*, 40% of families with children were Roma.

As a first step of the program planning which started in 2009, team members of the mentorship program contacted the sub-regional association with the intention of introducing the Program to Combat Child Poverty. The tender size (600 million HUF, cca. two million EUR) was so significant that the region decided to apply. The former tried to involve as many participants as possible: management travelled among settlements in the first place, gathering ideas and suggestions from local mayors, public institutions, civil society organizations, and entrepreneurs. Only the Roma population was not involved. Members of the project team reported that they had encountered difficulty in the past trying to find common ground with the leaders of the local Roma minority self-governments.<sup>14</sup>

After the start of the mentorship program, the implementing team compiled a local periodical called the *Sub-regional Mirror* and published findings that helped to harmonize the demands of the settlements with real needs. The outlined program elements were later presented at community forums. The first sessions of this iterative consultation were not free from conflict. The reason was that financial demands far exceeded the available funds and, contrary to mayors' intentions, only a relatively small portion was available for spending on infrastructural development<sup>15</sup> (for example, on the renovation of buildings). At last, a compromise acceptable to all local governments was reached by introducing additional feasible program elements into as many settlements as possible.

The project basically focused on compensating for the deficiencies of mainstream institutions; that is, offering services to children in need; services that either did not exist or had limited capacity in the region. To achieve this, project members hired a psychologist, a speech therapist, a health educator, and five developmental teachers<sup>16</sup> who taught in several schools, alternating on a daily basis. By bringing these services to schools, eventually all of them, professionals were able to take care of all the children in the region, including the most deprived Roma kids. Furthermore, each school hired a mentor teacher who was responsible for reducing the school drop-out rate of disadvantaged children. In addition to providing extra tuition and preparing 13–14-year-old children for secondary school, they undertook social work at school: maintaining close relationships with parents, trying to reduce the amount of absences, solving all sorts of other problems, and helping children progress in many other ways throughout their studies until the end of their secondary education. Moreover, three extra family assistants were hired by the project who, joining existing ones, contributed to the better care of disadvantaged families.

Capacity was lacking not only in terms of human resources but also in the limited recreational opportunities that children in this region could enjoy due to the lack of adequate financial resources. Therefore, the program also included the organization of extracurricular and summer activities that schools could not otherwise afford in order to help children often living in an under-stimulating environment to broaden their horizon.

This was particularly important for the most deprived children who, due to the limited financial resources of their families, often had not even crossed the borders of their villages. Activities included (free) extracurricular events such as workshops, skills-development activities,<sup>17</sup> sports events, as well as excursions, and summer camps. In the latter, special attention was paid to involving children from the worst backgrounds, while others living in better conditions were also invited.

Another element of the concept was improving the service quality of mainstream institutions. It appeared to be necessary to facilitate communication between families with children and local institutions, thereby helping to build partnerships. To achieve this, parents' clubs were created in kindergartens to develop parental competencies on the one hand, and to strengthen the relationship between families and kindergartens on the other. Occasionally, pediatricians and health visitors were also invited, which not only improved the accessibility of health care services but at these informal meetings brought parents and professionals closer to each other. Such events were very useful for Roma families who, usually having lower levels of trust in public institutions, considered professionals to be authorities rather than partners. Furthermore, several events took place to raise awareness of professionals in relation to the Roma, such as awareness-raising training for health visitors, and study journeys for teachers to schools which had succeeded in facilitating the integrated education of Roma pupils.

A new institution – namely, a community center<sup>18</sup> – was established only in one settlement: in the most disadvantaged village in the region, almost entirely populated by extremely poor Roma families. This center offered concentrated services for children: not only were learning support, community development activities and excursions organized, but internet use and comfort services (washing and bathing) were also provided. Partnering with the public institutions, the center offered adults a place and opportunity to contact family support services once a week on the spot.

As a whole, the program reached a significant proportion of children in the area by filling gaps in services one way or another. The territorial targeting approach proved to be correct: by implementing a large part of all activities in kindergartens and schools, it was easier to involve the child population of the sub-region. Not only were the most disadvantaged, including Roma families, reached, but children from most different backgrounds were actively involved in all activities. The program strengthened trust between families and local professionals, and thereby mutually sensitized them to understanding each other's points of view and facilitated integration. Moreover, since individual program elements were linked to mainstream institutions, the approach contributed to their development instead of creating parallel project institutions.

## 6.2 The program in Sub-region “E”

The structure of Sub-region “E” is likewise characterized by small villages: the majority of its 36 settlements have less than 500 inhabitants, only one of them being a city. Similarly to Sub-region “S,” since long before the political transition this predominantly agricultural area had been unable to provide a fair standard of living for its population. Therefore, a significant part of the population was forced to commute on a daily basis to nearby industrial centers or mines. During the deep post-transition recession, not only did these workplaces drastically decrease in number, but so did local employment options, leading to the outward migration of younger and more skilled people. This region has never been able to emerge from this crisis of the labor market: according to the last census, only 45% of the population aged 18 to 59 were employed (KSH TEIR 2019). There were kindergartens in 17 settlements, and schools in 14 – though some schools provide education for the first four years only. Most of the settlements were ethnically segregated, which was also reflected in the social composition of the children attending the public education institutions: in ten schools, the proportion of children with multiple disadvantages was over 50%. Segregation could be detected within the city as well, both spatially (Roma neighborhoods) and on a school-by-school basis (*Sub-regional Mirror*).

As early as in the planning phase of the project, which started in 2011, the management tried to provide incentives for the local governments of all settlements with a significant child population to join the program. Due to the large number of settlements, the sub-region was divided into four territorial units, and the services were focused on the centers of these. Each intervention area was assigned a planning team that was responsible for contacting mayors and local institutions, surveying needs, gathering demands, and planning specific services as much as financial resources permitted. Members of the mentorship program played an active initiating role in the work of the teams as well as in negotiations with the local governments from the very beginning. It became clear very soon that although the sum of approximately 600 million HUF (cca. two million EUR) offered by the tender for a two-year term was fairly generous compared to the budgets of earlier human development interventions in the region, the settlements turned out to have even greater demands. As a result, planning was not free from conflict, just like in the other regions covered by the Program to Combat Child Poverty.

These conflicting interests were treated by the management in many different ways. First, managers could take advantage of professional relationships they had established in several settlements in the past. Second, while negotiating the distribution of services across settlements with mayors, they could often refer to the Sub-regional Mirror (*Gyerekszegénység Elleni Programiroda 2009; Magyar Máltai Szeretetszolgálat 2012*) as an objective, factual document, with conclusions usable as a basis for planning. Third, while assigning the available resources, project managers wanted to benefit as many settlements as possible, in the case of the poorest settlements establishing or upgrading a community center, creating a Sure Start children’s house,<sup>19</sup> or some other community

space, and in the case of the less poor settlements establishing or upgrading at least one playground. However, since the sum available for the project was limited by the tender, some settlements that could not be benefited by such institutional development measures were compensated by receiving access to health screening tests and sporting events. Negotiations failed only in the case of a single settlement. The mayor of the central locality of the most disadvantaged sub-region left the program – which was already at the planning stage – because he considered the funding allocated to his area to be too little. Therefore, this territorial unit was awarded fewer services than the weight of problems would have justified.

For the smallest children and their parents, Sure Start houses were established in five locations. Settlements with a large number of needy Roma families were selected. One house was opened in the town center of the sub-regional centre, easily accessible to families with small children, another in the Roma neighborhood of the city, and an additional three in segregated or segregating settlements where the proportion of children with multiple disadvantages (mostly Roma) was high. That is, the houses were basically located close to the most deprived families. As a consequence, they ended up receiving Roma families only, even if originally intended by professionals to be mainstream institutions where children from diverse social backgrounds could be educated in an integrated environment. The location of the two in-town houses further strengthened segregation, which eventually also occurred even in the town-centre house. Although the overall social composition of families in the latter was rather heterogeneous, Roma and non-Roma parents refused to mingle with each other. In order to maintain the level of attendance, the manager of the house decided to create a split schedule to determine who and which session members could attend daily. However successful this method was in increasing attendance levels (an important factor in meeting the criteria for the indicators of the tender), the result was a special form of segregated environment.<sup>20</sup>

Besides Sure Start children's houses, the most resource-demanding and thus most highlighted elements of the program were the community centers and their activities. According to the invitation to tender, at least one community center with complex services was obligatory in all of the segregates or settlements undergoing a process of ghettoization (with a significant Roma population). In region "E" seven community centers were established: one in the already mentioned in-town Roma neighborhood near the Sure Start children's house, three in some ghetto villages in very bad conditions, and another three in other settlements with ethnic segregates.

Attendance rates, and thus the success of the centers depended not only on their physical characteristics (location and layout) but also on the professional and personal qualities of the team members, as well as on their visibility and acceptance. In most places, it was difficult to address people initially, especially when news of the comfort services<sup>21</sup> (bathing and washing facilities) that were provided got around. A feeling of shame kept even those who lacked piped water at home and who could have occasionally benefitted

from these facilities away from the centers.<sup>22</sup> In general, stable groups of users were established when team members maintained good personal relationships with the families outside of the centers as well.

Well-functioning community centers offered a wide range of services: after-school workshops for children, excursions, internet access, nursery consultation, health-screening tests, a wide range of programs for every generation (for example, a cooking club, and a club for teens). In summary, most centers managed to reach quite a number of families, including the poorest ones in first place. However, their integrated operation could only be achieved in a few places: such attempts as a rule were rejected both by the local middle class and by the poor non-Roma.

To cope with insufficient personnel capacity, the program in Sub-region “E” hired several human service professionals (e.g. a speech therapist, psychologist and a developmental teacher). However, since there were not enough resources to allocate professionals to each and every school, professionals performed their activities in the community centers. In this way, their services were brought closer to most deprived families (at least in the settlements with a community center), although other families had no access to the former. The hiring activity of the project occasionally had consequences that opposed the original goals, since some of the staff of the project (e.g. those working in community centers) were attracted by the program away from the local family support services, worsening the shortage of professionals in basic services. These professionals continued to perform certain family support tasks (for example, helping locals handle official matters), but as employees of a community center they were no longer authorized to officially act as civil servants in necessary cases.

Similarly to as in Sub-region “S,” the Sub-region “E” program also facilitated a wide range of educational activities in already existing institutions on behalf of children of preschool and school age. In all kindergartens in the region, activities were organized to strengthen parent-child relationships. In the schools, the deficiencies of students of vulnerable families were remedied by launching classes to promote financial competence and by organizing excursions, sports events, and camps. Furthermore, in the schools of the four most disadvantaged settlements, mostly populated by Roma, preventive classes were held to reduce early school leaving, deviant behavior, and early pregnancy. Taking place in institutions of public education, these events effectively reached children in need, regardless of their social background. The program made vigorous efforts to create access for the poorest families to the summer camps, but success was only partial. One of the difficulties was that not all parents allowed their children to go to the camps.<sup>23</sup> Another problem was that, as an incentive to learn, organizers sometimes required children to get good marks in school as a condition of participation. However, this requirement had an effect contrary to the objectives of the program because it reduced the access of those children to the camps who lived in extreme poverty and were unsuccessful in their

studies, in spite of the fact that it was exactly these students who were in greatest need of such programs.

In general terms, the program in Sub-region “E” can also be considered successful at reaching the most deprived, including the Roma population, thanks to accurate territorial targeting, and to the concentration of resources in the settlements where a lot of Roma families live in deep poverty. However, the program focused on providing special services to the Roma instead of strengthening and improving the quality of mainstream institutions, and this prevented the principle of integration from being properly realized. Although the program was not able to significantly improve the situation of people living in deep poverty, and did not solve the problem of the segregation of the Roma, it contributed to making life more comfortable for them. The program was not able to raise awareness of the necessity of social and ethnic integration; among other goals the program was also not able to improve communication between parents and professionals. The program improved the quality and widened the portfolio of social and educational services in the sub-region, with special respect to summer camps, to consultations with psychologists at the community center, and to the activities of children with the developmental teacher. However, the program in many cases failed to attract many of the vulnerable families for whom these activities were implemented in the first place. This failure also frustrated the professionals who were involved.

### 6.3 Comparison

Case selection is essential in comparative research. To ensure comparability, we picked two sub-regions which are similar in certain regards. As both sub-regions are parts of the Program to Combat Child Poverty, they are underdeveloped. Both of them faced and still face similar economic and social problems, are located in a peripheral area of Hungary, and have a similar settlement structure. At the same time, our two selected sub-regions show several differences in terms of their geographic position (see Appendix), program planning, implementation period, and accomplishments. The similarities and differences are summarized in Table 1.



**Table 1:** Comparison of Programs to Combat Child Poverty of two sub-regions

	<b>Sub-region “S”</b>	<b>Sub-region “E”</b>
<b>Basic characteristics of the sub-region</b>	Small rural villages, mainly < 500 inhabitants, high unemployment, high rate of multiply deprived children, socially and ethnically segregated villages, lack of quality services.	
<b>Planning of the local Program to Combat Child Poverty</b>	Evidence-based; community planning, involving mayors, public institutions, NGOs, entrepreneurs, inhabitants; involvement of Roma representatives lacking.	Evidence-based; partly community planning, involving mayors, public institutions; involvement of Roma representatives lacking.
<b>Implementation of the program</b>		
<b>Main focus and instruments</b>	<p>Mainly: improving existing local institutions: supplementing lacking human resources, expanding on their activities; quality improvements.</p> <p>Furthermore: establishing a new local institution (a community house) in a segregated village.</p>	<p>Mainly: establishing new local institutions for the poorest (7 community houses, 5 Sure Start houses/services).</p> <p>Partly: improving existing local institutions: supplementing lacking human resources, expanding their activities.</p>
<b>Involvement of settlements</b>	Every settlement of the sub-region involved, through existing (mainstream) institutions, especially schools and kindergartens.	Most settlements of the sub-region involved, with special focus on segregated villages. Involvement mainly through the new institutions.
<b>Involvement of the main target group: disadvantaged and/or Roma children</b>	Good level of involvement, predominantly in schools and preschools.	Partial level of involvement in certain schools and preschools and in the close vicinity of Sure Start and community houses.
<b>Main areas of development</b>	Human and cultural capital (skills development, extracurricular activities, programs in school holidays). Social capital and social integration (improving relationships between poor families and institutions).	Human and cultural capital (skills development, extracurricular activities, programs in school holidays).

<b>Features of integration/inclusion</b>	Good level of integration. Children with different socioeconomic status and ethnicity treated and involved together.	Partial level of integration in some services. Segregated participation in Sure Start houses and partly in complex community houses.
<b>Main strengths and weaknesses</b>	<p>Strengths: Effective cooperation with mainstream institutions, filling some gaps, quality improvements; access to all children in every preschool and school; integrated and inclusive implementation.</p> <p>Weakness: remaining differences among settlements in terms of availability of services.</p>	<p>Strengths: Establishment of several new institutions with a variety of previously missing services. Reducing differences among settlements in terms of the availability of services. Some improvement of mainstream institutions.</p> <p>Weakness: duplicated services, role conflicts; lack of integration goals; efficiency problems with some services.</p>

Source: Author's compilation.

As a result of the delivery of different services, both local projects were successful because disadvantaged children – among whom the Roma are over-represented – were effectively involved in the program. Thus, the local programs efficiently reached the main target group of the program and made crucial investments into the human and cultural capital of children. These investments concerned biological, cognitive, emotional, recreational and social needs and deficiencies, as well as bettering the life chances of children.

Through employing speech therapists, physiotherapists and psychologists, significant investment into the human capital of children was made, with special respect to their physical, mental and cognitive health (Schultz 1961; Becker 1964). By providing mentoring and developmental services in schools and preschools and organizing extracurricular activities within and beyond these institutions, the program invested not only in human capital, but also in the cultural capital of kids. Through the complex services of Sure Start and community houses, the program aimed to develop parenting, family management, lobbying and other parental skills which may improve indirectly children's implicit cultural capital (Bourdieu 1986) as well. Similarly, the delivery of recreational services or innovative program elements for children may result in the same development. Meanwhile, some aforementioned program elements fostered networking activities and provided possible channels to create, maintain or strengthen social capital (Bourdieu 1986; Coleman 1988).

The essential difference between the projects' implementation lies in the integration and inclusion of the excluded (Sen 2000). Whilst in Sub-region "S" integrative and inclusive

participation was realized through the involvement of all pupils who attend school and preschool, this was not the case in Sub-region “E”. Paradoxically, as an unintended negative externality of the interventions Sure Start houses and some community houses of Sub-region “E” even deepened the segregation existing between the local Roma and non-Roma families and their children. In contrast, in Sub-region “S” the project managed to inclusively implement the Program to Combat Child Poverty through the equal involvement of children by sensitizing and awareness training, and by strengthening communication between different social groups and professionals. Its accomplishments are basically in line with the principles of the *Europe 2020 inclusive growth* strategy, as well as the *explicit but not exclusive targeting* and *aiming for the mainstream* principles which are two cornerstones of the *Common Basic Principles on Roma Inclusion*.

## 7 Concluding remarks

Concerning development for the poor, there are two main lessons to be learned from the above-described case studies. First, new services may become segregated if they operate in parallel with preexisting mainstream services and institutions. This might be particularly the case with services provided to an excluded minority; namely, the Roma. Even if the new services are of a higher standard, they will not necessarily solve the problem of segregation, and instead may contribute to its maintenance. Consequently, programs aimed at the integration of the segregated should focus on strengthening and supporting mainstream institutions. The introduction of new services is justified only if basic services are not available. Second, well-planned, targeted and implemented social and educational services inevitably raise mutual awareness and improve communication between professionals and families at risk of poverty. Mutual awareness is a precondition of integrated development, while without good communication between professionals and families at risk of poverty, even segregated services function less effectively.

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### Notes:

<sup>1</sup> Foucault in his economic sociology clearly distinguished between labor power (i.e. the capacity to work) and the capacity to generate income; to receive a wage through the help of one's work, also called capital-ability. The idea is that the basic element to be explained by economic analyses is not so much the individual, or processes and mechanisms, but enterprises (Gary Becker (2014) An appreciation by Michel Foucault, available at: <https://kieranhealy.org/blog/archives/2014/05/04/gary-becker-an-appreciation-by-michel-foucault/> (15 March, 2019)).

<sup>2</sup> Prior to this period, human capital, educational investment and its productivity were analyzed by illustrious economists such as Adam Smith (1723–1790) ([1776] 1977), Thomas Robert Malthus

(1766–1834), Georg Friedrich List (1789–1846), Alfred Marshall (1842–1924) ([1873] 1995), Arthur Cecil Pigou (1877–1959) (1928), Arthur W. Lewis (1915–1991), Milton Friedman (1912–2006) and Jacob Mincer (1922–2006) (1958). The term “human capital” was probably first introduced by William Petty (1623–1687) in the seventeenth century (1662). See also Caldari (2010), and Krasniqi and Topxhiu (2016). Alfred Marshall suggestively sums up the core idea of human capital theory thus: “... *the best investment of the present capital of the country is to educate the next generation and make them all gentlemen*” (Marshall [1873] 1995, 106).

<sup>3</sup> In this context, “field” is interpreted as the person’s social position within a given social space. A field is constituted by the conflicts of social groups in defining what cultural capital is, which type of cultural capital is legitimate, and which type is illegitimate. For more details, see: King (2005, 215–232).

<sup>4</sup> In this context, the “habitus” of a person is interpreted as embodied intellectual disposition and tendencies (See King 2005).

<sup>5</sup> Here we omit a presentation of the contribution of several theorists to the evolution of the concept. For a detailed history of social capital, see e.g. Woolcock (1998) or Farr (2004).

<sup>6</sup> This includes the right (a) to an adequate standard of living, healthcare, education, recreation, (b) to protection from abuse, neglect, exploitation, discrimination, (c) to participate in communities and to have programs and services for themselves.

<sup>7</sup> Some examples of European Union frameworks and policies for Roma inclusion: The Decade of Roma Inclusion 2005–2015, the Integrated Platform for Roma Inclusion, and the Social Protection and Social Inclusion Process.

<sup>8</sup> These two principles are implemented most efficiently if inclusion attempts start in early childhood. For more details, see the Roma Early Childhood Inclusion Overview Report. For truly effective Roma integration, the report envisages local community- and family-based programming in the European Union Member States (Bennett 2012). The same programming method is applied to the Hungarian Program to Combat Child Poverty presented in the chapter below.

<sup>9</sup> According to Hungarian legislation, disadvantaged children are those living in families that, in addition to having a low income, are affected by at least one of the following criteria: parents are minimally educated, or in a precarious employment situation, or the family has poor housing conditions. The status of multiple disadvantages applies when at least two of the three listed criteria are met.

<sup>10</sup> For the strategy in English, see <http://romagov.kormany.hu/download/5/58/20000/Strategy%20-%20HU%20-%20EN.PDF> (19 February, 2019).

<sup>11</sup> In 2007, 175 sub-regions were established in Hungary for the purpose of settlement development. Based on their infrastructural levels and the population’s social and economic metrics, 47 of the sub-regions were defined as extremely deprived. In these sub-regions, complex cohesion programs were launched, one of which was the Program to Combat Child Poverty described in the study, and which operates in 23 sub-regions. From 2017 the program has been running in somewhat refurbished form and has been extended to eight new regions.

<sup>12</sup> The sub-regions participating in the program included 532 settlements, of which only 35 were cities, while 346 localities had fewer than 1000 inhabitants.

<sup>13</sup> In the third stage, three tenders were not awarded due to a lack of resources.

<sup>14</sup> Based on experience, involving the Roma population in the planning process proved to be troublesome in other regions as well. This was due to the general lack of Roma civil society organizations, and of Roma middle class as potential leaders, while the leaders of minority self-governments did not always turn out to be creditable representatives of the local Roma population.

<sup>15</sup> It was a general experience in the Program to Combat Child Poverty that mayors chiefly envisaged construction projects, thinking that new or renovated houses would remain assets of the

settlement even after the end of the program. However, they did not see the point in developing “human assets”.

<sup>16</sup> A relatively high number of special needs teachers was necessary because, especially in certain segregates, many disabled children were eligible to attend.

<sup>17</sup> One innovative element was encouraging and supporting student enterprises in every school. Children were asked to create a product or service and then to sell it by finding the right market and sales channels. These enterprises, mostly successful, enabled students to obtain plenty of useful economic knowledge and skills that improved their future chances on the labor market.

<sup>18</sup> An obligatory element of the tender was the establishment of community centers with complex services, specifically in segregated settlements or neighborhoods, to mitigate the shortage of such services in these places which typically lacked them. Apart from the community houses with complex services for addressing all ages, additional community spaces included the Sure Start children’s houses, after-school support programs, youth houses and IT points. However, unlike community service centers, these initiatives limited their activities to specific subject areas or age groups, and were not obligatorily restricted to segregates.

<sup>19</sup> The children’s houses, inspired by the Sure Start program in the UK, constitute in Hungary a new kind of institution for supporting early childhood development. Besides promoting infants’ early development and skill acquisition, they strengthen parental competencies by engaging parents and providing them with knowledge and experience.

<sup>20</sup> As also reported by the evaluation studies about the Sure Start children’s houses, the general experience is that the social composition of the visitors of these houses sooner or later became homogenized, and either middle-class or poor families predominantly visited them. Both socially and ethnically speaking, there were only few houses with an integrated environment (Szomor and László 2014).

<sup>21</sup> Comfort services received a very mixed reception among the population of all regions. As one of the sub-regional evaluations reported, *“Initially ... there was strong opposition: partly because the non-Roma thought something [had been] done again ‘only for the Roma,’ and didn’t understand ‘why is it again the Roma who receive anything at all?’ On the other hand, the Roma did not receive the bathing and washing facilities with enthusiasm, saying that they were clean, and could wash at home”*. The feeling of shame was probably fed by the painful memory of forced bathing in the communist era, a means used by the leadership of the time to “elevate” the Roma who at that time were looked upon as a public order and health risk (Bernáth and Polyák 2001).

<sup>22</sup> In the most disadvantaged settlements, only 15-20% of homes had a piped water supply (*Sub-regional Mirror*).

<sup>23</sup> Camps and excursions were organized in a number of regions covered by the Program to Combat Child Poverty. Generally, involving the poorest families required extra effort. One of the reasons for this was – as already mentioned – that parents were reluctant to allow their children to go to places they were not familiar with. This issue was successfully overcome when trusting personal relationships already existed between organizers and parents. Another inhibiting factor was that some parents felt shame about not being able to provide proper clothing, equipment and bathing amenities for their children. Recognizing this, camps were often organized so that participants had all these amenities at their disposal.

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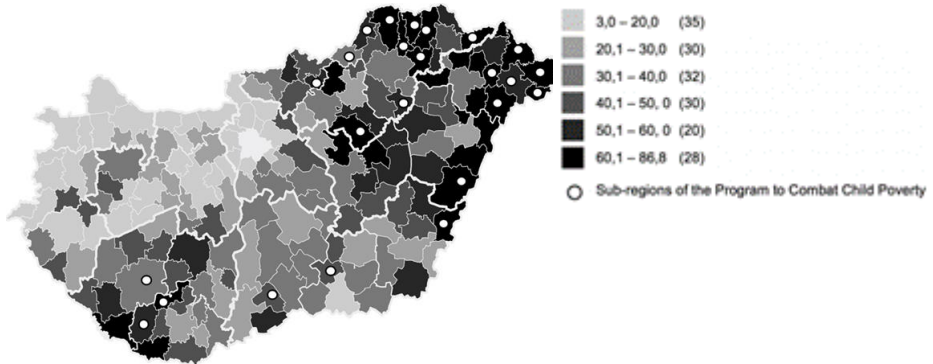
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## Appendix

Area of implementation of Program to Combat Child Poverty and proportion of disadvantaged pupils in elementary schools in Hungary, 2013/2014, sub-region level (%)





# The Role of Local Governments in the Development of the Local Economy: International Findings in Light of Hungarian Case Studies

MÁRTA KISS & KATALIN RÁCZ

**Abstract** This paper evaluates the economic development activities of several Hungarian local governments (LG), by taking into consideration the analogous measures assessed worldwide. Based on the summary of the literature we show that the role of local governments in local economic development (LED) has become strategic over the last few decades, as local governments have been able to mobilize resources and coordinate the stakeholders of local development in line with local requirements as a result of their position. For evaluation purposes, five dimensions of LED are applied. A typology of local economic development strategies is developed by using a conceptual scale ranging from (a) demand-oriented strategies, which focus on the satisfaction of the needs of the population, to (b) supply-oriented strategies, which focus on business support and the promotion of local investment.

**Keywords:** • local governments • typology • business-oriented development • holistic development • community-focused development

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## 1 Introduction

The term 'Local Economic Development' in the 1990s predominantly involved activities like the elimination of obstacles hindering economic growth, the management of the problems that arise from the imperfect operation of the market, and the creation of jobs (Faragó 1991; Bingham and Mier 1993; Blair 1999). However, more recent approaches<sup>1</sup> have defined local economic development (LED) as a conscious strategy by which local stakeholders and institutions aim to promote the most efficient use of local resources (Capková 2005; Bajmóczy 2011; Lengyel and Bajmóczy 2013). As such, the focus of LED is broader than merely meeting economic goals. It is aimed at implementing quality changes such as transforming the employment structure, managing social problems, or improving quality of life (Puljiz 2004). This paper uses the latter, broader concept of LED.

The focus of local economic development is constantly changing in line with economic, social and environmental challenges (World Bank 2004). From the 1960s to the early 1980s, LED concentrated on investing into physical infrastructure. During the second wave of LED – from the 1980s to the middle of the 1990s – the focus was on the preservation and growth of existing businesses. From the 1990s onwards, the concept of LED concentrated on soft infrastructure investments, public private partnerships, network-building and organizational development. Regarding the actors involved in local economic development, the role of local government has been strengthened during the last decades to the extent that – according to certain approaches – economic development is the primary responsibility of local governments. Based on this concept this World Bank publication aims to evaluate not only the activities of local governments (LGs) in economic development, but also LED as a strategic tool for managing local challenges. The analysis focuses on LGs operating in areas with complex structural disadvantages, as this situation puts particular emphasis on LED.

## 2 Conceptual framework and theories

Should the state interfere with economy and, if so, to what extent? This question continues to be subject to debate. Numerous researchers have claimed that these two sectors exist in a mutually complementary relationship, and that the state evidently depends on the economy as it needs income to operate. However, the issue of the necessity and extent of state interference is subject to controversy (Block and Evans 2005). Proponents of laissez-faire philosophy claim that the economy works optimally if the state does not interfere. In contrast, many economic sociologists (i.e., Weber, Polányi, and Granovetter) have proved that the economies of different cultures are deeply embedded in social and political structures and institutions. Block and Evans (2005, 505) – among others – also add that embedded institutions change dynamically due to innovation, and this reflects on the relationship between the state and the economy.

During the last 20–30 years there has been a shift in Western Europe and the USA towards a new kind of development policy – governments have realized that they are now ‘forced’ to deal with economic problems (high unemployment rates, low real wages, budget deficits, and so on) and to interfere with the operation of the market. Although there are debates regarding the consequences of this process, interfering with local economies is today a global trend.

In the USA this is typically undertaken by providing support for the research activities of companies and for industrial modernization, and also by providing capital and training to companies and small businesses (Bartik 1991). Since 1979 the UK has been following a ‘third way’ policy that promotes equal opportunities and the involvement of citizens in the government. The importance of LGs has increased in economic development since the 1980s due to the need to address local priorities and demands, and the system of governments and EU funding (Bennett *et al.* 2004, 211).

As for the countries of Central Europe, the shift came after 1990 due to comprehensive social and economic changes when social and economic problems culminated. The liquidation or transformation of large industrial and agricultural companies, increasing unemployment, and growing social inequality forced LGs to extend their activities; namely, to fulfil their increased social duties by facilitating local development. This was not the typical case in these countries until this time.

The negative impacts of the economic and social transformation from socialism were felt more strongly in rural areas where the gap left by the liquidation of uncompetitive state-owned companies was not filled, or only gradually filled by new investors and local businesses with significant employment capacity (Buček 2005; Lengyel and Bajmóczi 2013). Local governments that found themselves in a difficult situation due to structural changes (mainly in industrial locations) were forced to deal with social problems alone, while increasingly having to meet the challenges of the market (Pearce and Mawson 2003; Capkova 2005). Central Europe was characterized by a policy of decentralisation with the main goal of integrating local needs into governance. As a result of these processes, the role and responsibility of LGs increased significantly with regard to economic development (Capkova 2005).

In general, globalization trends have increased the significance of the local: solutions aimed at dealing with problems locally are gaining in importance, and municipalities are being forced to specialize to benefit from their comparative advantages (G. Fekete 2013). Local governments play a strategic role in this process as the organizations that are in a position to include, mobilize, and coordinate different stakeholders: the local population, businesses, NGOs, companies, and volunteers (Bennett *et al.* 2004; Capkova 2005). Therefore, the involvement of LGs is a necessary but not sufficient condition since LGs are dependent on government, other stakeholders and funds, and, as such, cannot engage in local development alone (Pearce and Mawson 2003; Bennett *et al.* 2004; Mezei 2008).

### 3 Trends and facts

#### 3.1 Decentralization and LD

For several decades the relationship between the level of decentralization and the rate of economic growth has been investigated as a focal question in international research into local government and local economic development. Countries that implemented decentralization policies have a multi-tiered system of government wherein lower levels have independent tasks, competencies and budgets. Local governments play an important role in distributing funds as they have more information about the needs of local residents – provided that the principle of subsidiarity is adequately implemented within the government structure (Vigvári in Tóth 2014).

However, research shows that although fiscal decentralization contributes to economic growth to a certain extent, beyond a certain level the relationship becomes negative (Thiessen 2003). Furthermore, the effect of decentralization is greater when it is supported by a reliable, high-level institutional environment (Buser 2011; Kyriacou *et al.* 2015). Nevertheless, there is some controversy regarding the relationship between decentralization and territorial disparity, and many researchers have attempted to identify the direction and defining factors of these relationships (Canaleta *et al.* 2004; Rodriguez-Pose and Ezcurra 2009; Kyriacou *et al.* 2015). Some researchers have found that an increase in fiscal decentralization leads to a decrease in regional disparities (Ezcurra and Pascual 2008). Other papers show the more complicated interdependence between the degree of decentralization and territorial disparities and draw attention to the fact that other conditions are also decisive in this matter (for example, the level of economic development, and the state and quality of institutions). Rodriguez-Pose and Ezcurra (2009) found that there is a strong correlation between the results of fiscal decentralization and the level of economic development, and the degree of redistribution and the level of regional disparity within the affected country. In high-income countries, the delegation of governance to a local level results in a decrease in regional disparities, while in low- and medium-income countries fiscal decentralization increases regional disparities.

According to a paper that evaluated local development efforts in the context of the EU, the structure and comparison of local and central government spending is a suitable indicator for highlighting the role LGs play in development (Rusu 2014). In the EU, an average of 11% of local-level budgets are dedicated to tasks related to the economy. In some Member States (for example, the Czech Republic and Ireland) this proportion is over 20%. General public service spending (for example, the operation of political organizations, and general public administration spending) is important from the perspective of local economic development. These factors account for 20% of local budgets, on average, within the EU, albeit with significant differences among Member States (Rusu 2014).

Our analysis which is based on the following case studies on the LED activities of Hungarian settlements support the hypothesis that the delegation of responsibility for governance to lower, local levels has a notable effect on sustainable economic growth and development. However, the extent of this effect largely depends on the characteristics of the governance and institutions and on territorial disparities.

### 3.2 Roles of local governments

Most countries have no legally binding rules that specify whether local governments are required to be involved in local economic development. If a LG takes on this role, it is added to its responsibilities as an additional function. Such LGs perform an 'integrated economic development role' (Pugalís and Tan 2017, 6). The participation of LGs in economic development may vary greatly. The extent and type of interventions depend on a number of external and internal factors such as demographics, the characteristics of the economic environment, and the available financial and human resources and decision-making factors that have an effect on economic development. The economic development activities of local governments are traditionally divided into two categories: (i) grants designed to incentivize businesses that have the potential for greater economic development, and (ii) strategic initiatives for changing tax, budget and government policies to facilitate the growth of the local economy (Bartík 2003).

Based on international studies (ICMA<sup>2</sup> data collected in 2004), the most typical economic-development-related activities of local governments are providing support for private investments and job creation. However, as recent research shows, there is a growing trend for LGs to take on activities beyond their traditional role that serve wider social interests (meet the needs of minorities, disadvantaged groups, and so on) and to promote the fairer distribution of the costs and benefits of economic development (Morgan 2009, 2).<sup>3</sup>

As far as everyday practice is concerned, local governments may play a very varied role. On an international scale, the most typical areas of activity are the following (Pugalís and Tan 2017): infrastructure development and wealth creation; the business-friendly planning of land use; business support; cooperation; networking; lobbying and promotion; the strategic planning of economic development; undertaking feasibility and capacity studies; developing business cases; and conducting sector-based research and stakeholder mapping exercises.

Leight and Blakely (2017, 139–141) have identified four roles of local governments: LGs are 'coordinators' of different actors; they are 'facilitators' regarding their attempts to improve the environment of the local community; they are 'stimulators' as they can promote the creation of local businesses; and LGs are also sometimes 'entrepreneurs or developers.' LGs can use common land or buildings for economic purposes to benefit the community.

LGs may perform their LED activities through different structures: some LGs have a planning department to implement economic development functions (an ‘in-house model’), while others outsource these activities to external service providers (for example, NGOs) (an ‘arms-length model’). Numerous LGs use a mixture of these two models and vary the method used for economic development based on changing circumstances, requirements and priorities (Parker and Donaher 2012).

As demonstrated by various studies, the spectrum of the roles of local governments is extremely wide; there are significant differences between countries but there is a common trend for LGs to increasingly promote partnerships, cooperation and innovation. Additionally, it is now an important task of LGs to collect and use local knowledge and to support, empower and coordinate existing and potential economic operators to increase the effectiveness of their cooperation (Bartik 1991; Pearce and Mawson 2003; Bennett *et al.* 2004; Capkova 2005; G. Fekete 2013; Pugalis and Tan 2017, etc.). Best practices show that networks based on common interests may prove to be a stable form of coordination if membership is limited to the partners that may contribute to local economic development with significant resources, especially if the roles of members are balanced. Local governments often act as catalysts in such partnerships (Tello 2010).

In Hungary over the last 6–7 years the government has manifested a strong desire for local governments to organize farming. This preference has been manifested in various tender-based subsidies offered for local governments. As result, the roles of local governments have expanded to include this new task, themselves becoming market actors (See e.g. Lendvay and Nagyné 2013; Váradi 2015; Molnár *et al.* 2018).

## **4 Comparative case studies**

### **4.1 Assessment criteria and LED Factors**

The selection criteria for the location of case studies were that the settlements should be located in a disadvantaged area, and that the respective local governments should act according to a complex model of settlement development. In the selected case study settlements local economic development is based on the cooperation of numerous institutions and local interest groups (e.g. local government, cooperatives, and non-profit organizations), while the above-described stakeholders in development use a sophisticated system of development tools, including participating in domestic and EU-funded programs and launching local initiatives with a focus on the training of human resources. Based on our preliminary research into the orientation of local government participation, we have chosen different types of cases that cover several types of LED strategies. In particular, we wanted to include into our sample both demand-oriented strategies that focus on citizens’ needs, and also supply-oriented LED strategies that focus on the interests of local businesses. The aim of this qualitative research was thus to create



a typology of LED strategies through analysing the complex economic development practices of municipalities of disadvantaged settlements in Hungary.

The LED Factors taken into consideration were as follows:<sup>4</sup>

1. The main characteristics of the settlement, such as the size of the settlement; factors arising from determining geographical features and endowments, infrastructure and other physical factors; the social characteristics of the settlement and the main characteristics of the population;
2. Resource endowment (financial resources; human resources; institutional resources; technological resources);
3. Strategic planning, the system of tools of the LED (governmental roles; form of strategic planning; direction of development; objectives and devices);
4. Cooperation and coordination (local actors involved in LED; extent and type of cooperation; methods of promoting co-operation; means of coordination);
5. Innovation and sustainability (innovative elements of LED; sustainability factors and predictors).

## **5 The Bácskaháza case study<sup>5</sup> – 'Business-oriented' development**

### **5.1 Main characteristics and available resources of the settlement**

Bácskaháza is a district centre in the south of Hungary near the Serbian border. The settlements in this area are faced with a complex set of disadvantages. The population of Bácskaháza is in constant decline. In line with local endowments and traditions, the majority of businesses are active in the field of agriculture and food. The system of local public service institutions is comprised of several participants, and most institutions are operated through inter-municipality cooperation. The municipality has a kindergarten, an elementary school, a cultural centre and a 'training' swimming pool. The infrastructure of social and health-care institutions is well established. A family assistance office, an employment office and a clinic are also available. Besides the relatively large population (6853 people in 2018), the reason for the well-established infrastructure is the idea of the local government that providing sufficient quality public services is a precondition for stopping further population decline and fostering the development of the local businesses that create jobs.<sup>6</sup>

## 5.2 LED orientation and strategies

The economic development activities of the local government have two dominant elements: on the one hand, they involve implementing measures to improve the employment- and income-generation conditions of the local population, while on the other hand they support local businesses by sustaining the conditions and business services necessary for their operation. In recent times, the priorities within these two elements have varied depending on changes in the macroeconomic environment. In the wake of the crisis of 2008, the priority was to help those employees who had lost their jobs on the primary labour market. Following this, in the last few years the economic development activities of the local government have focused on providing support to local businesses. Beside developing existing enterprises, the local government has paid more attention to motivating those economic actors who were either looking for local (Bácskaháza) employees or intended to establish a company within the settlement.

## 5.3 LED toolkit

From the beginning, LED was based on a process of collective systematic thinking founded on a knowledge of local capacities. As the economic crisis of 2008 unfolded, the local government started to offer jobs to employees who had lost their jobs on the primary labour market. These were agricultural jobs in the framework of various public employment programs, financed by central government funds. A large number of these jobs were created and maintained by the agriculture-oriented public employment programme 'START' which started in 2011. Most of these workplaces were created on the fifty hectares of land and farm buildings owned by the local government. As a part of the program financed by central sources, the nearly 200 workers in public employment started cultivating arable crops, fresh vegetables, hothouse vegetables and producing seeds and raising plants under the management of agricultural experts.

The goods locally produced were primarily used for local consumption: products were sold to local mass catering institutions and directly to locals. A common brand was created (*Bácskaháza Portéka*) for the locally produced food and craft products which has also supported the marketing of the products of local businesses, such as goat cheese, meat products, and craft products. A local shop was opened exclusively for branded products, which are promoted at local and national events and on the internet. To facilitate local consumption, the local government operates a voucher scheme to provide locals with non-monetary aid. In spite of such measures, the lack of demand is the current challenge of this LED strategy, which is based on food production. Therefore, the local government must find and create sales channels that go beyond local markets.

#### **5.4 Coordination and partnerships**

During the last decade, the legal form and the ownership structure of the economic activities of the local government have undergone changes. In the first years LED activities were undertaken by the employees of the local government. Later, a non-profit limited company was founded (owned exclusively by the local government) that creates vegetable-based products with the involvement of the locals that take part in the public employment programme. Additionally, a few years ago the local government established a cooperative to process vegetables and fruit and to sell products. Subsequently, the LG established another social cooperative with a new profile: this initiative offers various services to businesses active in the agricultural sector (e.g. outsourcing workers, or providing services using farm equipment). The local social cooperatives have received considerable funding from external sources.

The local government has taken steps in recent years to extend economic relationships with entities outside of the village by contacting the municipalities, businesses, manufacturers, and consumers of the LEADER community of the area.<sup>7</sup> The goals were the following: organizing the network of product producers, exploring regional markets, aligning manufacturing, and offering a competitive product portfolio.

#### **5.5 Innovation and sustainability**

The employment of agriculture and food industry experts has been a top priority for the local community. This was regarded as a precondition for creating high quality products and of mobilizing local, existing resources, such as assets of arable land, real estate, knowledge and traditions. Operational risks have been reduced by organizing activities into clearly separated organizational units. As a result of this, the operation of the overall system has not been endangered, even though one of the co-operatives has experienced problems. While the local consumption of locally produced goods is the focus, the key to the sustainability of the Bácskaha economic development program is reaching external markets. For this purpose, steps have been taken to identify market partners with greater demand for products.

Due to the macroeconomic changes of recent years, the focus of LED has changed in Bácskaha. Today, the primary goal of the local government is to create a business environment that supports local businesses that have the potential to create a significant number of new jobs. Additionally, the LG promotes external enterprises that are willing to utilize local resources. This is a change compared to the previous strategy of the LED, which was focused on directly satisfying labour needs. This change of direction in local development strategy has been reflected in the institutional background, in the infrastructural characteristics, and in the resulting partnerships.

## 6 The Tófalva case study<sup>8</sup> – ‘Holistic development’

### 6.1 Main characteristics and available resources of the settlement

Tófalva has a population of 780. The village is situated in an area of small villages with extremely unfavourable economic and social indicators. Tófalva itself is among the more fortunate, medium-sized municipalities in the area. The reason for its better economic situation is partly the four-star “wellness” hotel that opened twenty years ago, and partly the relatively large number of businesses that were founded after 1990 on the ruins of the state farm of the village. After the transition, the state farm was privatized and the resulting businesses (mainly animal breeding and cereal-producing enterprises) have since been run by skilled agronomists who previously worked for the state farm (Keller 2016). According to the mayor, another decisive factor is the Swabian<sup>9</sup> origin of the population and their proactive mentality.

However, the depopulation trends of the area have affected Tófalva too – the number of inhabitants has decreased by 200 over the last 20 years. The most important goal of the local government is to stop the depopulation of the village. A complex system is in place to support this goal, including reduced rents, favourable conditions for buying real estate, and recruitment assistance. As a basic concept, the programme looks for young families with the skills to meet local demand who are open to staying in the village for the long term. They do not try to hang on to those highly skilled young people in the village who cannot find jobs that match their qualifications nearby (a widespread strategy in other places).

Another condition of eligibility for support is that applicants should send their children to local educational institutions, as keeping these open is a priority for the mayor. While closing different institutions and rationalization was a trend in previous decades, Tófalva has managed to keep its primary school and kindergarten open. A doctor (a general practitioner), a post office and a library are also available in Tófalva. The majority of local services (public lighting, wastewater treatment, a village bus, and so on) are operated by a successful non-profit limited company (with six or seven permanent employees) that was founded by the local government. Thus, the local government is able to provide services that are not financed from the state budget in such small villages any more – for example, a post service. Moreover, although primary schools are now managed by the state due to the centralization efforts, the primary school of Tófalva offers some extra options that make the institution and the students more competitive (for example, by providing infrastructure for IT training that meets the requirements of the twenty-first century).<sup>10</sup>

## 6.2 Local development policy

Local development policy aims to both serve the interests of the community and create a business-friendly environment (a holistic approach). This is clearly seen, for example, in local infrastructure development measures and from support for business development. While the local government makes great efforts to serve the needs of the local population in a comprehensive manner, it is not forced to make great sacrifices to provide jobs as unemployment is very low (four people are currently involved in the public employment programme and three in another employment programme).

In 2011 a social cooperative was initiated by the mayor in Tófalva using EU funds,<sup>11</sup> with the participation of six locals. The cooperative employs disadvantaged locals and produces fruit and processed goods. The cooperative is currently at the financial break-even point and is expected to generate a profit in the next one-to-two years by developing sales channels. The next phase of the programme will aim to involve disadvantaged persons from neighbouring villages: the cooperative will buy and sell the goods that are produced and collected by participating families. The concept is under development currently. The plan is to provide microcredit to families so they can buy the necessary seeds and tools, and to hire an expert to help them with agricultural activities.

The mayor is committed to elaborating and implementing a long-term strategy and has invited an expert team – a professor and students from Corvinus University of Budapest – to facilitate local development by drawing up detailed plans and suggesting areas for local co-operation. Since the activities of the local cooperative are seasonal a contract was created with the local wellness hotel to provide employment for the members of the cooperative during the winter season. Experts are currently working on defining the conditions of a microcredit scheme.

## 6.3 Coordination and cooperation

The key to the success of the mayor is his openness to cooperating with a wide range of local stakeholders, including the above-mentioned social cooperative, the non-profit limited company, some local consultancy businesses that offer support for innovation and writing tender applications, and local NGOs which are active at organizing local events. The mayor also maintains close relationships with neighbouring villages and their local governments. These municipalities are taking part in several tenders together and the primary school is shared with the neighbouring village.

## 6.4 Future: innovation and sustainability

The settlement has a complex municipality development programme which has been built on expert insights. Some elements of the programme are innovative, such as the activities of the non-profit limited company devoted to improving education and supporting IT

knowledge. Similarly, the agreement between a big local enterprise and the social cooperative regarding agricultural workers' seasonal employment and the sale of local products in the wellness hotel can be regarded as innovative. Together, the local government and the cooperating institutions and experts make up an alliance that is able to react to new challenges in a flexible manner and enables the village to maintain its leading role and favourable economic situation in the region, despite its small size.

Even though the municipality is small, the conditions for the success of local development seem to be in place – the local government has a relatively large budget due to local business tax and tourism tax income and development is based on sound strategies and business-oriented thinking, while the needs of local people are also taken into account. (A holistic approach; see Bennett *et al.* 2004). The mix and mentality of the local population is favourable, and development work is supported by an adequate infrastructure and institutional background and highly qualified experts. Local institutions are involved in the LED process (such as the cooperative, a non-profit Ltd., the school, etc.), as well as entrepreneurs, NGOs and external experts too. Local stakeholders and institutions are well embedded in local society, the community is balanced, and the local government is able to play the role of a catalyst in this cooperative effort (Tello 2010).

## **7 The Zsákfalva Case Study<sup>12</sup> – ‘Community-focused’ development**

### **7.1 Characteristics and resources of the local government**

The current village was built on a previously uninhabited area at the beginning of the twentieth century and was mostly inhabited by low-income agricultural workers (servants). The small village with its limited road connection has been an independent municipality only since 1993. All (100%) of the current population are of Roma ethnicity, with a low level of education and poor financial situation. The settlement was classified as “less favoured” in government decree No. 105 of 2015. In the village there is only one enterprise: a small shop. The elementary school in the village was closed in 2015 but the kindergarten was refurbished to a high standard in 2011 using EU funds. In 2013, a community centre was also built using EU funds. Education and health-care services are available in another settlement six kilometres from Zsákfalva, which serves as the centre of the sub-region. Social care professionals (child protection nurses and family carers) also come from here to provide services to the families in Zsákfalva.

Similarly, to most small villages in Hungary, the local government is the biggest employer in Zsákfalva, providing jobs to a large number of locals as part of the public employment programme. As the tax income of the local government is minimal (the village has a single active small business) the village is highly dependent on state and EU funds and sources. The majority of the locals have worked in different, primarily agriculture-related production and manufacturing programs. The local implementation of

these programs is personally coordinated by the mayor. Most of the locals have never entered the primary labour market, but this has changed significantly in recent years due to increasing labour shortages and the vicinity of the county seat. Consequently, for locals who had gained experience in the public employment program the chance of finding a job has increased. As a result of this, the number of participants in the public employment programme may decrease.

## **7.2 Local development strategies and tools**

The local government has been actively farming on its own land and on leased land since 2011. Additionally, it has created a beekeeping business and a carpentry workshop by using various funds. These produce a small amount of goods for sale, but the primary objective has always been to supply the institutions of the village and to provide jobs for locals. Growth and business development were continuous until 2015. Since then there has been a decrease in the jobs provided by the local government and in the production of local goods. This is a consequence of the fact that the local government relies heavily on central budget funds and the government changed employment policy, its aim now being to enforce more economically sustainable operations and to “push” people towards the primary labour market.<sup>13</sup>

The mayor of Zsákfalva is undertaking all leadership tasks alone and manages all projects single-handed. One of the reasons for this is the low level of education of the local population: no one in Zsákfalva has a university degree, and the number of people with a high school diploma is also very low. Consequently, it is hard to find people who can undertake tasks that require qualifications, leadership, or professional skills. The local government is able to find local employees for administrative tasks, but it has inevitably had to hire external resources to fill the positions of kindergarten teacher, community house manager, and manager of the beekeeping business.

The development concept of the mayor can be said to be ‘community-focused’ because it mainly focuses on satisfying local people’s needs, creating local employment, and developing local reliable and responsible employees and community building. In the last eight years, programs were built on one another following strategic goals: expanding the lands owned by the local government, acquiring the necessary assets, hiring expertise, training local workforce, and developing community social services.

## **7.3 Coordination and cooperation**

In the field of development, the mayor concentrates mainly on the municipality (instead of inter-municipality cooperation) and manages and coordinates locals, institutional stakeholders, and external experts with an all-encompassing, caring disposition.

Locals are employed by the local government farm which as part of the program also provides them with seeds and tools to start vegetable gardens at home. Excess vegetables produced on the local government farm that are not consumed by local institutions are available for locals to buy at a reduced price (and even on credit for those who need it). Lunch is available free of charge (using state funds) and the village has a passenger van to provide transport to locals who need to visit the nearby town to deal with administrative matters. The community house (operated as a part of an Integrated Child Opportunities Programme<sup>14</sup>) provides social and community services. The method of coordination is typically paternalist; however, according to the testimony of various interviews undertaken with locals, the authority of the leader is based on respect. The local government undertakes all roles;<sup>15</sup> it is not only a coordinator, but also a market actor.

#### **7.4 Future: innovation and sustainability**

The development tools of Zsákfalva can be regarded as innovative in the sense that they are aimed at locals' (re)integration into the labour market, human resource development and the utilization of local products (see G. Fekete 2013). However, the mayor – who directs all these tasks alone – is about to retire and no longer wants to take risks, although risk is an essential component of innovation. The development and innovation of local products is currently not a priority, which may be one of the reasons why the sale of these products in external markets has recently declined.

In summary, the community-focused LED strategy of Zsákfalva has been successful since it has reached its goal: the standard of living of locals is increasing, and the village is developing. However, it seems that this small, disadvantaged village cannot run social enterprises according to market principles in a rational, economically sustainable manner. In order to establish such a regime, the village would need support. As far as the prerequisites of sustainable development are concerned, several essential factors are lacking: the local government is practically unable to generate any income and it currently lacks a stable local institutional system and the human resources that would create the sufficient administrative and professional background for fostering sustainable local development. Moreover, most local development projects are isolated and are based mainly on social principles instead of business-oriented ones. If – according to the leader's plan – a couple of local young people (currently two) are successfully educated and become able to lead the village projects, there will be a chance to continue with the LED program, but only with continuous external support.

### **8 Conclusions**

This paper evaluates the activities of LGs in economic development as a strategic tool for managing local challenges. Based on the summary of the literature we show that the role of local governments in local development has become strategic over the last few decades, as local governments have been able to mobilize resources and coordinate the



stakeholders of local development in line with local requirements as a result of their position.

After providing an overview of the relevant literature, five dimensions of LED were described. Based on research, we believe that these are the ones that have the largest effect on the success of local economic development. The effects of these dimensions on local economic development was analysed through three cases, which represented the different types of orientation of local governments. A typology of local economic development strategies was conceived and employed by paying attention to settlement size. We operationalized this typology by using a conceptual scale ranging from (a) demand-oriented strategies, which focus on the satisfaction of the needs of the population, to (b) supply-oriented strategies, which focus on business support and the promotion of local investment.

Our research shows that while the disadvantages affecting municipalities are similar, the paths of economic development activities are very different. These development trajectories as a rule are influenced by many factors. In particular, the size of the settlement influences the number of potential actors and the other resources that can be involved in the development process. If the basic resources of economic development are lacking, then the activities of local governments primarily focus on supplying immediate needs. This situation was illustrated with the case-study settlement of Zsákfalva. A business-oriented approach to economic development is characteristic of bigger municipalities that have better infrastructure, a wider spectrum of local institutions and service providers and a more significant consumer base. This situation was illustrated with the case-study settlement of Bácskaháza. However, the history of the village, the legacy of former activities, and the stratification of local society are also influencing factors. This situation was illustrated with the case-study settlement of Tófalva where local people are relatively better qualified and in a better economic situation, and there are more institutions and services than in the less well-developed settlement of Zsákfalva. As a rule, the LED strategies of settlements with a better knowledge base are also characterized – beside their striving to meet pre-existing social goals – by a significant business orientation.

As far as coordination is concerned, in smaller municipalities without appropriate human resources power is more likely to be concentrated in the hands of one person: a local leader. This facilitates quick reactions when decisions have to be made, but in the long term poses questions about the sustainability of the local system of economic development. In these places, the output and pace of local development depends significantly on external resources, a fact which is also highlighted in local plans and strategies.

The predominance of state dependence in the development of smaller and weaker settlements has resulted in so-called institutional isomorphism (DiMaggio and Powell

1983). This means that in the examined regions the institutions created as tool of LED show a great deal of similarity. As an example, one characteristic organizational form of development is the local food-producing social cooperatives directed by local governments. Nevertheless, differences in choosing the legal forms and ownership structures of the organizations that operationalize LED do exist, and typically depend on local influencing factors.

One general observation is that LED involves network-building activity which is primarily based on the co-operation of local public and private stakeholders; external players are rarely involved. Network-building nearly always involves the development of an organizational background: the local government, acting as the coordinating body, creates new organizational forms that help to improve the utilization of resources, to mitigate operational risks, and to facilitate access to markets. In smaller municipalities the key players in the network are the representatives of public administration; in the case of bigger municipalities there is a more significant chance that partnerships will be formed that integrate representatives of the for-profit sector as well.

The economic development concepts of local governments are generally characterized by a high level of innovation. Due to the lack of internal resources, the economic development activities of LGs that operate in areas with disadvantages are characterized by constant experimentation. This results in innovative, often groundbreaking solutions that usually adapt to challenges in a flexible manner and create new combinations of public-private and public-civil partnerships. As for the sustainability of these development models, based on the case studies the decisive factor appears to be whether a concept essentially tailored to local needs is successfully aligned with the wider development regimes of the area.

**Table 1:** Comparative overview of local development strategies of the case study settlements

<b>Municipality</b>	<b>Main characteristics of the settlement</b> <i>Size, geographical characteristics, infrastructural and social factors</i>	<b>Resource endowment</b> <i>Income / support, human-, institutional- and technological resources</i>	<b>Strategic planning, LED toolkit</b> <i>Form and direction of development, objectives and tools</i>	<b>Networking, Partnerships</b> <i>Roles of LG, actors, extent and methods of cooperation &amp; coordination</i>	<b>Innovation, Sustainability</b> <i>Innovative elements in economic development, sustainability factors</i>
<b>Zsákfalva</b>	Small village, servant-legacy, 100% Roma ethnicity, low level of education and living conditions, poor infrastructure, little available land.	Lack of institutional and human resources, lack of incomes, state dependency, EU support.	Strategic thinking, complex development aimed at self-sufficiency, retreat from the market.	LG produces for internal market and local people, characterized by isolated operation.	Social orientation, goal is self-sufficiency, depends significantly on funding, sustainability depends on individual successors.
<b>Tófalva</b>	Mid-size, Swabian traditions, layered society, presence of professionals and entrepreneurs, good infrastructure, economic centre of the micro-region.	Qualified human resources, good institutional resources, own incomes +state/EU support.	Complex development, strategic thinking, direction of development: both community- and market-oriented (holistic).	Business function is separated from LG, strong cooperation of 3-4 institutions, good connections with nearby municipalities.	Innovative ideas, good cooperation skills, flexible organizational structure, sustainability is an important consideration.
<b>Bácskaháza</b>	Large municipality, strategic position in the sub-region, layered society, rich institutional system, good infrastructure, plentiful municipal land.	Rich institutional system, qualified human resources, own incomes +state support.	Strategic thinking; the role of the market is increasingly important, separation of institutions.	Extensive cooperation between local institutions, the local government is involved in business activities, but organizational profile is being streamlined.	Innovative ideas, experimental phase, strong orientation towards new government policy.

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**Notes:**

<sup>1</sup> Local governments play a key role in the process of creating an adequate environment for local enterprises (Czene and Ricz 2010). However, recent approaches have attempted to define the concept of LED based on a wider group of participating actors (Martin 2000; Pike *et al.* 2015; Bajmóczy 2011; Áldorfa and Topa 2015). However, according to a narrower approach the local development process is inspired by local governments and other community-directed organizations (Blakely and Bradshaw 2002). More generally, LED is interpreted as a process whereby public, business, and NGO sectors co-operate in order to create more favourable conditions for the expansion of economic growth and employment (Swinburn 2006).

<sup>2</sup> International City/County Management Association (2019).

<sup>3</sup> In Hungary, a strong social orientation characterizes local economic development initiatives (Czene and Ricz 2010; G. Fekete 2011). Characteristic forms of the former include social land programs and social cooperatives, which are also used by the local governments in our case studies.

<sup>4</sup> The precise definition and the detailed content of these factors have been explained by the authors in another paper, which has been also published in the present volume (see Márta Kiss and Katalin Rácz: An overview of factors and policy measures influencing Local Economic Development).

<sup>5</sup> The name of the case study settlement is a pseudonym.

<sup>6</sup> The local government tries to encourage young people to stay by providing settlement- and rent subsidies.

<sup>7</sup> The LEADER program is a European Union initiative aimed at supporting rural development projects initiated at the local level to revitalize rural areas and create jobs.

<sup>8</sup> The name of the case study settlement is a pseudonym.

<sup>9</sup> German Hungarians are the German-speaking minority of Hungary sometimes called the Danube Swabians. There are 131,951 Germanic speakers in Hungary (according to the 2011 census).

<sup>10</sup> The school, with the help of the local government, joined a Microsoft program that provides software and computers to institutions. Additionally, the IT training in the school includes a course on programming robots.

<sup>11</sup> Supported by the EU co-financed Human Resources Development Operational Programme (HRDOP), Subprogramme 1.4.1 -15 “Professional support for Integrated Child Opportunities Programmes”.

<sup>12</sup> The name of the case study settlement is a pseudonym.

<sup>13</sup> In 2015, the local government employed 65 locals as a part of the public employment program, but the respective number had sunk to 24 by 2018. A carpentry workshop was closed due to a lack of demand for its goods. The beekeeping business faced some difficulties too, but at present seems to be surviving.

<sup>14</sup> Human Resources Development Operational Programme (HRDOP) -1.4.1 -15 Professional support for Integrated Child Opportunities Programmes.

<sup>15</sup> Such roles are: political, ownership, definition of norms, authority, communication, employer and market (see Lendvay and Nagyné 2013).

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## Teaching Business Climate Development with the Help of Case Studies

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**Abstract** This article presents a practical conceptual framework of Business Climate Development as an area of development policy, and introduces the terms used for evaluating Business Climate Development projects and programs. The structure of such programs and the method of their evaluation is demonstrated with the help of an illustrative case study in which a Business Climate Development program is evaluated in a post-soviet republic. The evaluated program was financed by an international development organization and lasted for five years. It supported central and local authorities to register businesses, issue various businesses permits, dispatch inspectors to oversee various business activities and manage taxation. The program was evaluated by a team of consultants who identified, classified, assessed and judged the activities of the above-mentioned Business Climate Development program. The program and its evaluation has been presented as a case study to students of a Joint Master Course for Comparative Local Development.

**Keywords:** • business climate • case studies • evaluations • policy measures

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## 1 The business climate and its evaluation: a conceptual framework

The business climate is the general legal, institutional, economic and social environment of entrepreneurship and enterprises in a particular locality, region or country, comprising of the attitudes of the central, regional and local governments, of financial institutions, labour organizations and non-governmental organizations towards businesses and business activity. A business-friendly environment is demonstrated by the ease of doing business as influenced ...

- By the institutional and regulatory framework of fair competition, employment, trade and taxation;
- By favourable macro-economic constraints such as inflation and economic growth;
- By the wide availability of support offered to businesses by authorities;
- And by the positive attitude of society towards businesses.

Why are business climates more favourable in some countries than others? According to the theory of institutional economics, between-country differences in business climates as a rule are explained predominantly by legal and institutional factors. In particular, the presence of an informal economy is explained predominantly by unfavourable business conditions (Dabla-Norris *et al.* 2005). Within one country the business climates of various regions and settlements may also show significant differences (OECD 2001; Shane 2005). Local variations in business climates are as a rule explained by a wide range of theories that take into consideration differences in inherited economic structure, social capital, social stratification, tradition, and also by centrum-periphery relationships (European Commission 2010). Business climate development is one of the major tasks for local economic development (The Cities Alliance 2007; Swinburn *et al.* 2006).

The business climate has frequently been a subject of comparative research. The business climates of various countries are comparable, and are indeed compared with the help of numerous qualitative studies and various quantitative indicators. One of the most influential quantitative indicators is the "Ease of Doing Business" indicator, which has been determined for a wide range of countries (The World Bank 2008). The components and influencing factors of a business climate have been tackled not only with the help of numerical indicators, but also by qualitatively investigating the impact mechanisms of relevant development programs, supporting projects, and business development regulations in order to evaluate their success or failure.

*Case studies* are qualitative instruments of research which possess high didactic value in development education. Case studies are not only suitable for descriptive purposes but may be used to highlight a preferred contextual framework and, with the use of theories, can be used to explain observed and presented phenomena (Yin 2003). However, research is not the sole area in which case studies may be instrumental: likewise, case studies are excellent ingredients of evidence in consultancy and teaching. Most case studies of business climate development are of the stand-alone type because of the national or local

limits of interest, or due to difficulties with data collection. Consequently, it is not easy to find comparative case studies, in spite of the fact that comparative case studies are much more suitable for supporting or rejecting certain general hypotheses about the causal mechanisms of policy interventions.

*Evaluations* involve consultancy efforts to assign value to certain policy measures; i.e., to assess whether certain projects, programs, or policies were (or are) successful. Specific measures of business climate development are evaluated according to their contribution to local economic development (OECD 2009). In particular, case studies of project evaluations are frequently used in teaching about local development to demonstrate how a selected policy area – in this case, business climate development policy – functions in a particular country. Additionally, students of local development, when writing their dissertations, frequently choose project and program evaluation as the preferred genre.

## 2 The case-study program

*The evaluation project.*<sup>1</sup> The following case study relies on experiences from a real-life consultancy effort. The consultants prepared an interim<sup>2</sup> evaluation of a business climate development program in a post-soviet republic in 2014. The evaluation took place when the program under evaluation had already lasted for seven years, and was still ongoing. The evaluation project lasted for two months. The team of evaluators consisted of four consultants (three international consultants and one local) and was delegated by an independent private consultancy.

*The evaluated program.* The beneficiary of the program under evaluation was the government of the case-study country. The program was financed by a developed country in the framework of a bilateral development agreement, and implemented by an international development organization. The first wave of the program ran from September 2007 to June 2013 with a budget of nearly five million USD. At the end of the first wave of the program (in 2013) the donor country decided to extend it by another one-and-a-half years and contributed to the budget an additional more than one million USD.

*Policy areas.* The evaluated program promoted business climate development reforms in the case-study country in the following policy areas:

1. The initial registration of businesses;
2. The issuing of permits to businesses;
3. The implementation of business inspections by government authorities;
4. The simplification of taxation; and
5. The modernization of agricultural governance.

*Aid delivery mechanisms.* According to the conceptual framework of the evaluation, the activities of the evaluated project were implemented with the help of four so-called “Aid Delivery Mechanisms,” including:

- “Monitoring and Research” (e.g. implementing business surveys and analysing them using statistical methods, providing quantitative and qualitative studies about small business development).
- “Promotion of legal changes” (e.g. lobbying government agencies for business-friendly regulations and supporting such measures with know-how and study trips).
- “Capacity building” (e.g. providing technical assistance to government agencies, creating web portals, drafting regulations and providing services that facilitated the membership of the beneficiary country in various international bodies).
- “Awareness Raising” (e.g. workshops and training courses for NGOs and for associations of entrepreneurs).

The evaluation covered the program's activities in the above five “policy areas,” as detailed in the above four “aid delivery mechanisms”.

The evaluators used the following traditional qualitative evaluation criteria:

- Relevance (coherence with stakeholder needs and government policies);
- Effectiveness (delivery of planned results);
- Impacts (direct and indirect effects of program activities on the targeted policy areas and on beneficiary institutions); and
- Sustainability (the capability of program outcomes to survive for several years).

A traditional fifth criterion, efficiency (program delivery model, value-for-money, timeliness, etc.), was dropped due to the lack of time for gathering and validating financial data.

The evaluators were requested to assign quantitative indicators, or so-called Evaluation Rankings, to each of the four “aid delivery mechanisms” and to each of the five “policy areas”. Evaluation Rankings ranged theoretically from "Highly Unsatisfactory" (numerical value = 1), "Unsatisfactory" (2), “Fair” (3), and "Satisfactory" (4) to "Highly Satisfactory" (numerical value = 5). For the purposes of the present article, the actual ratings are not relevant, but their justification may be enlightening, because:

- They demonstrate the various important factors and components of a business climate;
- They indicate by what “aid delivery methods” these components are addressed by the measures of specific “policy areas;”
- They suggest what instruments can be used for developing the business climate of a particular country.

*The main information sources of the evaluation were:*

- Desk research; i.e., analysis of internal program documents, of the online- and paper-based deliverables of the program, and of documents provided by the beneficiaries;
- Interviews undertaken with the expert staff of the evaluated program; and
- A number of personal interviews with government officials, international donors, national experts, private sector representatives, businesses, social and labour organizations in the case-study country.

### **3 Comparative overview of the business environment in the case-study country**

The case-study country is rich in natural resources, but according to national plans its economy must be diversified by developing entrepreneurship in the service, manufacturing, trade and agricultural sectors as well. In the few years preceding the evaluation, the case-study country had made moderate progresses in improving its business climate. However, compared to some neighbouring countries the country had lagged behind in various business areas. The comparison was made feasible with the help of the yearly "Ease of Doing Business" indicators and related sub-indicators.

During the years preceding the evaluation, several independent experts had assessed the business environment of the case-study country, and the reports were available online. The general opinion of these independent experts was that the country was not fulfilling its own potential in terms of entrepreneurship development, the readiness of firms to grow, and their innovative activity. Business surveys implemented by the evaluated program and also by other projects showed that business-people in the country perceived serious obstacles to doing business, such as the lack of financial resources, regulatory deficiencies, and their interactions with courts.

An analysis of the recent "Doing Business" indicators compiled by the World Bank (2014) enabled the evaluators to compare the business climate of the case-study country with that of its neighbouring countries. During the preceding years, the case-study country had implemented some decisive reforms in a few areas: for example, business registration had been simplified. However, the same Doing Business rankings showed that the complex regulatory areas where the intervention and co-operation of numerous ministries and subordinated authorities were needed still required new approaches and reforms.

The relevant professional literature recommended implementing reforms in a wide range of policy areas, such as:

- Competition policy;
- Taxation;
- Anti-corruption policy;

- SME financing;
- Governance of permits, with special respect to the simplification of construction permits;
- Governance of inspections;
- Property registration;
- Foreign trade; and
- Resolving insolvency.

#### **4 Activities of the evaluated program by policy area**

The activities of the evaluated program can be sub-divided into distinct groups of deliverables according to the policy areas that were relevant for business climate development. The ease of doing business in a particular country depends on a multitude of factors. The following description illustrates the multi-dimensional and multi-disciplinary components of a business climate and the wide variety of policy measures available for its development.

*Business Registration.* Previous business surveys that assessed the needs of entrepreneurs revealed that in the case-study country prior to 2007 the administrative burdens and insecurities associated with business registration constituted a serious obstacle to small business development. By 2007, the government had decided to modernize the registration of new enterprises. At that time registration took one or two months and involved the completion of thirty administrative procedures, including obligations towards the register of companies, statistical authorities, and various sectoral inspectorates (labour, fire prevention, food safety, etc.). The evaluated program supported the respective efforts of the government using a wide range of deliverables to simplify business registration. Program experts did research on comparable business registration systems worldwide and submitted discussion papers about best applicable practices for business registration. Moreover, the program also organized study tours for officials to countries with well-functioning business registration systems. Subsequently, reform of this policy area followed and the government set up a countrywide network of “One Stop Shop” offices and an e-government system for business registration.

*Permits and Licenses* issued for businesses by local and central government agencies are very important ingredients of the business environment. The needs assessment survey of 2007–2008 had shown that there were some 230 types of administrative procedures associated with the permits and licenses in force. Such a complexity of obligations constituted a serious obstacle to entrepreneurship development in the case-study country. Research indicated that this thick interface between business and government was infected by corruption and favouritism and was causing administrative burdens and insecurity to businesses.

In order to achieve the aims of the program, the capacity building of the respective stakeholder organizations had to be supported by lobbying efforts. During the first years of the program, its experts had co-operated with the respective sectoral line ministries to reform the field of permitting and supported them with know-how, dissemination events (e.g. workshops), and subsidized study tours of government officials. However, the reform of permits did not progress as quickly as expected. Therefore, at a later stage, the program changed its target group within the government and identified a different network of government agencies that was closer to high-level political decision makers. As a result, the business-friendly messages of the program were more likely to receive attention. However, one of the compromises that the experts of the program had to make was that the range of permit areas to be reformed had to be limited, and could not include the crucially important area of construction permits.

Nevertheless, program activities in the area of permits and licenses resulted in ...

- Some legal reforms;
- The launch of an e-permits webpage;
- The organization of awareness-raising conferences; and
- The dissemination of several brochures about permits.

*Business Inspections reform.* Previous research into small business development in the case-study country had repeatedly shown that inspections implemented by labour-, fire prevention-, veterinary- and other government agencies constituted obstacles to entrepreneurship development in the country. The evaluated program successfully lobbied high-level policy makers and various sectoral government agencies to improve the legal framework of inspections. Various aid delivery instruments were implemented, such as inviting specialized consultants to hold training courses, research, publications, study tours, the provision of legal and IT advice, and website development.

Importantly, the above efforts culminated in the critical support given to the drafting of the Inspection Law of July 2013. This law has considerably reduced and limited the arbitrariness of inspections. In particular, the scope of business functions that inspectors were entitled to control was limited, the fines issued by inspectors were more thoroughly regulated, and the timing of inspections was also reformed by limiting the occurrences of unannounced, unexpected inspections. Moreover, the law resulted in the establishment of an e-government website (an “E-registry of inspections”) which has made inspection visits more transparent, predictable, and provided accountability and supervisory mechanisms for the respective government bodies. In particular, the program has engaged with the Labour Inspectorate Service, the State Fire Safety Inspectorate, and the State Veterinary Service, and has helped to introduce international best practices for inspections. Moreover, the evaluated program has compiled checklists for inspectors and drafted guidelines for risk-based inspection.

*Taxation* is a crucially important policy area for business climate development. The administrative burdens associated with taxation as well as the level of tax burden are major components of the business environment. The program offered technical assistance to the government in the relatively narrow policy area of transfer pricing. Transfer pricing refers to rules and methods for pricing cross-border transactions between various national subsidiaries of international enterprises. Countries with transfer pricing legislation generally follow the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations. These rules allow tax authorities to fight money laundering and tax evasion by adjusting prices of products, services, and tangible and intangible property in the case of cross-border transactions within the same multinational firm. With the help of the technical experts assigned by the program, the government of the case-study country obtained the necessary know-how about exchanging tax policy information according to internationally agreed methodology.

*Agriculture* is the biggest sector of the economy of the case-study country, besides the extraction of raw materials by the mining sector. Therefore, improving the business environment of farmers was very relevant for meeting the objectives of the program. The program offered two components in this policy area: (a) seed certification, and (b) value chain analysis.

- The modernization of seed certification was implemented through various technical assistance activities that contributed to the simplification of the associated administrative procedures and accelerated the application of best international practices. Although seed certification is a relatively narrow area within agricultural policy, its reform has impacts on food safety, environmental management, and on the subsidization of agricultural entrepreneurs, among other areas.
- The other deliverable of the program in relation to agricultural policies was the elaboration of value chain analysis models. Value chain analysis is a method which helps to identify market failures in subcontracting-supplier relations, and identifies promising areas of investment, thereby improving the competitiveness of selected products. The program established such models for the horticultural sector, thereby enhancing the export potential for the fresh fruit and vegetable products of the case-study country.

## **5 Aid delivery mechanisms applied by the evaluated program**

*Monitoring and research of the SME sector.* The advisory activities of the program were based on a series of surveys that assessed the needs of local businesses. The surveys were based on the professional compilation of policy-area-specific questionnaires and on good and feasible sampling strategies. In particular, a 2012 survey of the awareness of businesses about the e-registry of inspections served for both the purpose of needs assessment and impact assessment. Additionally, experts from the program prepared legal analyses and policy assessments and published studies.



*Promotion of legal changes.* The evaluated program intervened with regulatory agencies for the purpose of reforming certain rules that were perceived as disadvantageous to the business sector. For each selected policy area, the program engaged with one (or more) governmental counterpart institution to obtain commitment for the intended reform. The relevant advocacy activity was supported by legal drafting, by offering technical expertise to government agencies, and by organizing thematic public-private consultations. The success of such lobbying activities depended to a large extent on the co-operation of the counterpart beneficiary organizations. Some government agencies – e.g. inspectorates in certain sectors – were more open to applying business-friendly international best practices, while others eagerly guarded every bit of their administrative and controlling power. The project was coordinated with the activities of some donor organizations that were active in the case-study country. These organizations co-operated with each other in promoting various legal changes on behalf of small- and medium-sized businesses.

*Capacity building for institutional development.* The evaluated program assisted a wide range of counterpart government agencies in applying international best practices, by setting up e-government websites, by setting up awareness-raising websites, by publishing and disseminating various brochures about the legal and institutional changes promoted by the program, by funding and organizing study tours for staff of government agencies and other stakeholders, and by organizing consultations with business associations.

*Awareness-raising.* The evaluated program organized a wide range of workshops and training courses for the staff of the relevant government agencies, for associations of entrepreneurs, NGOs and other organizations.

## **6 Conclusions and recommendations of the evaluation**

The overall judgement of the program was positive, especially when considering the fact that the results of the program had been achieved in a difficult administrative context. In this particular setting, the term “difficult” means that some government agencies were not interested in or were even opposed to reforms. In spite of this, the program delivered satisfactory results overall, which not only benefited the business sector of the case-study country, but also involved the building of trust and goodwill at the highest level of government.

The evaluators recommended improving the business environment of the case-study country by engineering reforms that produce higher quality regulations and well-trained, committed regulators. It was also recommended to continue the activities of the program by extending its advisory-advocacy functions. In particular, it was recommended that the project offer professional help to the government in the policy area of improving regulation. This involves efforts to establish administrative processes for systematically reviewing and updating regulations, and, if necessary, phasing out obsolete regulations

by taking into consideration evidence about their impacts on businesses. An important tool for taking such a systematic approach to better regulation would be advocating for the introduction and application of regulatory impact assessment within public administration.

## 7 Didactic conclusions

Evaluations can be readily used for educational purposes. Case studies of development consultancy activities such as project and program evaluations may serve as useful illustrations of development policy measures. Stand-alone (single-country) case studies of business climates may serve as useful evidence for demonstrating the structure of business climates in a particular country, region or settlement. Such case studies may highlight the constituent factors of the business environment and identify the policy measures for improving and eventually reforming the business climate. Comparative case studies are more suitable for generalization and for delivering lessons that can be learned and used in other territorial units. If the investigation covers two or more comparative territorial units, than it is possible not only to reveal ...

- How certain policy interventions work; but also
- Why under certain circumstances the investigated policy intervention has succeeded or failed.

### Notes:

<sup>1</sup> Throughout this article the evaluation effort is called a “project,” while the aggregate of the evaluated activities is called a “program”.

<sup>2</sup> Interim evaluations differ from ex ante evaluations and ex post evaluations in relation to their timing: in the case of interim evaluations the development project which is the subject of the evaluation is ongoing at the time of the evaluation.

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## Social Capital and Local Development: Citizen Participation in Decision-making Processes

SINISA ZARIC

**Abstract** Social capital as a term has been used widely to operationalize interpersonal trust among citizens, trust in local and other institutions, trustworthiness, as well as citizens' networking in various associations, clubs and organizations at local and other levels. Confidence is the most important component of social capital. Trust enables the realization of complex, non-routine projects by a community. There is a correlation between social capital and local development. In local communities, social capital has predominantly been interpreted as a function of trust. It has recently been identified as a special type of intangible property of the community which fosters the collecting of ideas and suggestions from citizens, and the selection of projects based on this procedure (Jordan et al. 2010). The process of citizen sourcing has been defined and described as "tapping into the collective intelligence of citizens" (Howe 2008). Local communities which possess significant stocks of social capital are expected to engage in better forms of mutual cooperation. Significant limitations of these collaborative procedures (Sharma 2010) are a) social capital has predominantly been proposed as a means of creating alternatives to local projects, and for selecting the most suitable of these; b) the process of proposing projects should occur within certain financial-methodological parameters, and proposals should be supported by statistical surveys and model calculations, and c) it is necessary to evaluate the results of findings obtained by the use of crowdsourcing techniques (Zaric 2014). This paper analyzes the social capital of several case-study cities in Serbia, Finland, and Belgium.

**Keywords:** • collaborating • crowdsourcing • citizensourcing • policy process • trust in local institutions

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## 1 From collaborative strategies to crowdsourcing, and from crowdsourcing to citizen sourcing

Crowdsourcing is a model of problem-solving distributed among many individuals. The potential and talents of a “crowd” are sometimes also called the “power of the many”. Discovering this potential is one of the most recent results of social and economic development. In the business model of crowdsourcing, the “crowd” plays a crucial role. “Citizen sourcing” is a different model that is derived from crowdsourcing: here, citizens are the focus. The aim of citizen sourcing is to involve citizens in various activities: for example, in public work or other projects of local governments.

The “power of the many” has been harnessed in the activities of a wide range of companies, such as in production processes and in marketing for designing promotional campaigns. Recently, citizen sourcing has been used as a component of the process of community development and in the planning and implementation of public projects. These remarkable participative solutions and strategies are employed for the purpose of establishing closer relationships with customers (Ogawa and Piller 2006), as well as other stakeholders or citizens.

When exploring the practices of crowdsourcing, attention should be paid to the expenses and costs of this approach and to identifying ways of reducing these. Both in terms of outsourcing and crowdsourcing, managers are investigating the possibility of getting input at a lower price. Crowdsourcing is an engaging process that is not easy to manage. Efficient crowdsourcing requires the close cooperation of different functions, departments and business lines within a company to be successful. Delegating processes to a crowd is costly, but it is more frequently efficient to do this than to outsource the process to an external company; i.e., to a subcontractor.

- In outsourcing, the partner to whom the company “delegates” a part of their process is known and is well defined.
- With crowdsourcing, on the contrary, the process is “outsourced” to an undefined group of people.

In citizen sourcing, the group of people who participate in the so-called “co-creation”<sup>1</sup> of a city – for example – are citizens. Efficient citizen sourcing has been made possible by widespread internet access and the rapid development of social media creates fertile ground for such opportunities. In the case of citizen sourcing, the inputs of citizens may help local governments or other public bodies. The point of citizen sourcing is the belief that the crowd/citizens ...

- Sometimes know more than the employees of the company or local government responsible for implementing the project in question; or
- Have some different skills, knowledge or capacities additional to the responsible internal managers; and

- Can most probably precisely express their needs, wants and perceptions. This is of crucial importance for creating inclusive and democratic local government.

## 2 From collaborative strategies to crowdsourcing and citizen sourcing

The history of economic models offers some evidence about complete economic systems based on the participation of employees. Whether these models have been institutionalized and instrumentalized or not, these attempts are of interest to economic theory. The major examples are self-management in Yugoslavia<sup>2</sup> and “*Mitbestimmung*”<sup>3</sup> in Germany. Besides these macro-level approaches, management theory has been specifically interested in the problem of how to involve employees in the process of implementing tasks and attaining the goals of a company.

In the theory of crowdsourcing, there are four basic questions which are of crucial importance:

- What does the crowd (citizens) want?
- What can the crowd (citizens) create?
- What does the crowd (citizens) think?
- What will the crowd (citizens) fund (finance)?

Crowdsourcing has been, until now, mainly thought of as a management process (Sherman 2011). However, recent approaches have also taken into consideration the fact that crowdsourcing has been successfully implemented in the processes of business, co-creation (Bruni *et al.* 2018), and in community projects implemented by local governments. Therefore, in the recent professional literature crowdsourcing has been investigated within a hybrid conceptual framework that mixes terms from business, organizational theory, technology, sociology and social psychology.

## 3 Definition of crowdsourcing: from collaborative strategies to crowdsourcing and citizen sourcing

As with many new terms in management and marketing, the term crowdsourcing was also recently coined.<sup>4</sup> Crowdsourcing comes from the words “crowd” + “outsourcing,” and the first known use of this expression can be found in writing by Jeff Howe<sup>5</sup> (Howe 2008). The term citizen-sourcing is a derivative of crowdsourcing (coined from “citizen” + “outsourcing”) and, according to dictionaries of management, means outsourcing the tasks of (local) government to citizens, as a well specified part of the crowd.

Some definitions of crowdsourcing have become a part of glossaries and business dictionaries. “The practice of obtaining needed services, ideas, or content by soliciting contributions from a large group of people and especially from the online community rather than from traditional employees or suppliers”.<sup>6</sup>

Jeff Howe (2008) points to the correspondence of crowdsourcing and outsourcing. The author finds the process of outsourcing crucial for understanding crowdsourcing as a process that is driving the future of business. He states that crowdsourcing is a process that involves the outsourcing of certain tasks to a distributed group of people. Consequently, the model of citizen sourcing concerns managing citizens' inputs in order to improve the decisions of local government. This process can occur both online and offline, and the difference between crowdsourcing/citizen sourcing and ordinary outsourcing is that tasks or problems are outsourced to an undefined public rather than a specific body, such as paid employees (Howe 2008), or paid professionals from the organizations of local government.

Recently, two authors – Estelles Arolas and Gonzales Ladron-de-Guevara – defined crowdsourcing as a type of participative online activity in which an individual, an institution, a non-profit organization or company proposes to a group of individuals of varying knowledge, heterogeneity, and number, via a flexible open call, the voluntary undertaking of a task. The authors emphasize the benefits of both sides: the crowd and the crowdsourcer:

*“The undertaking of the task, of variable complexity and modularity, and in which the crowd should participate bringing their work, money, knowledge and/or experience, always entails mutual benefit. The user will receive the satisfaction of a given type of need, be it economic, social recognition, self-esteem, or the development of individual skills, while the crowdsourcer will obtain and utilize to their advantage that what the user has brought to the venture, whose form will depend on the type of activity undertaken” (Estellés Arolas and González-Ladrón-de-Guevara 2012, 197).*

#### **4 Trends: The rise of strategies that are based on the participation of many actors**

Originally, the instrument of crowdsourcing came from the business world. From the very beginning, the model was associated with certain benefits. The major costs incurred by the crowdsourcer are associated with organizing and maintaining social groups and networks. In many cases, the crowdsourcer has to introduce some form of monetary incentive to stimulate the participation of the crowd.

The respective costs are always measurable, but the associated benefits are not measurable in all cases. For example, in the case of citizen sourcing when the technique of crowdsourcing is applied to public affairs there may be measurable benefits, but those associated with the general well-being of the community are frequently intangible. The motivation of citizens (Hars and Ou 2002) comes from a desire to improve the conditions of local communities and neighborhoods through the projects that are selected and



implemented. However, the crowd/citizens generally participate as unpaid or underpaid innovators.

The role of members of the crowd or of participating citizens can be threefold:

1. As active participants they can be considered as value-adding workers or managers in the administration of a project;
2. They may possess capacity which represents a valuable economic asset in the project;
3. They may be systematically integrated into the corporate structure or may be activated within the citizen-sourcing platforms.

## 5 Types of citizen sourcing

The technique of citizen sourcing can be applied in a rich variety of ways. Here are some of the most common areas of application:

- Various local development projects may rely on citizen sourcing. This approach is also called the collaborative development of a territory, whereby the term “territory” may refer to neighborhood, settlement or region.
- Urban planning projects involve neighborhood intervention. Such projects, as a rule, require the co-operation of a wide range of stakeholders in proposing, designing and implementing spatial interventions that improve the quality of the urban environment.
- Competitive bids in relation to specifically defined tasks or problems. In such cases, the most important task is to create platforms that can facilitate the access of citizens, improve presentation of the related ideas, and help with management activities related to collecting and processing the ideas of citizens.
- Permanent open calls. Keeping calls open is one of the more important tools in terms of creating permanent relations with creative communities and groups (Leadbeater and Miller 2004). This may be understood as part of the effort to establish so-called open government (Obama 2009). This technique may be implemented in various forms:
  - Community reporting. This helps citizens and policymakers to become partners who provide true, authentic information about problems in local communities.
  - Project evaluation. This technique is very much in use. Project evaluation by citizens occurs in many cities and local communities.
  - Citizen-to-citizen support. Such support is articulated via chats and discussion forums. It can strengthen networking and generalized trust, having indirect but positive impacts on local development.<sup>7</sup>

The citizen-sourcing model puts citizens at the center of focus by identifying them as a resource. Citizen sourcing is crowdsourcing practice applied by governments with the goal of tapping into the collective intelligence of citizens. Through citizen sourcing, governments can collect ideas, suggestions and opinions from their citizens, thereby

creating a permanent feedback loop of communication. Thanks to modern technologies, the time has come to unlock the wisdom of the crowd and the wisdom and creative potential of citizens.

In the citizen sourcing model, cities are interpreted as powerhouses of collective intelligence. More precisely, it is citizens who are considered capable of detecting and identifying the need for local common and public goods. But the process is not only about identifying preferences and making opinions and voting available on the internet. Additionally, it is citizens who can suggest projects, select projects from various alternatives, and participate in monitoring the process of implementation of these local projects.

Citizen sourcing has its own typology and criteria for evaluation. Nam (2012) suggests a very simple dichotomy of approaches to citizen sourcing by identifying the contents as “cool” or “hot”. The criterion according to which citizen sourcing project may be evaluated is the extent and impact of citizens’ involvement in the decision-making process in local government projects and public policies.

**Table 1:** Citizen sourcing: Cool or hot?

Cool	Hot
The aim of citizen sourcing is only to improve the image of the (local) government. As a result of the citizen sourcing exercise, the (local) government hopes to look “cool”.	Information creation with citizens Service improvement with citizens Solution development with citizens Policy making with citizens

Source: Author’s construction adapted from Nam (2012, 14; Table 2).

The proposed distinction could be enriched by inserting a third category: a “moderate” type of citizen sourcing. The “hot” type of citizen sourcing could thus delineate four activities:

- Solution development with citizens;
- Monitoring projects derived from a citizen-sourcing platform (monitoring the process, auditing facts and figures);
- Policy making with citizens;
- And public expertise (Dutton 2011).

The enriched, extended table would thus be as follows.

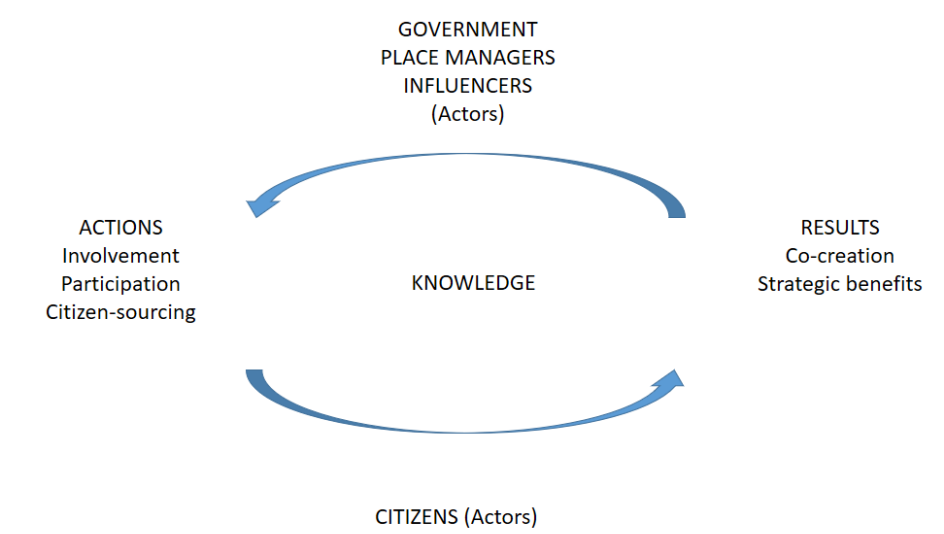
**Table 2:** Citizen sourcing: Cool, moderate and hot

Cool	Moderate	Hot
Improving the image of (local) government	Information creation with citizens	Solution development with citizens
		Public expertise
	Service improvement with citizens	Monitoring (controlling, auditing)
		Policymaking with citizens

Source: Author’s construction, adapted from Nam (2012).

This typology suggests the importance of “shaping “the crowd (e.g. citizens). While all citizens can take part in cool approaches to citizen sourcing such as image making, not all can participate in solution development, and especially in monitoring. This problem is due to the role of knowledge (See Figure 1). In these terms, one may understand citizens as a kind of specific human capital that has a significant impact on the quality and quantity of local government products/services.

**Figure 1:** Actor-to-actor relationship and the role of knowledge



Source: Bruni et al. (2018, 18).

Citizens are able to undertake certain roles in project monitoring. This does not imply that these citizens have to be certified auditors or accounting managers: it is enough if they are able to undertake performance auditing; i.e., if they are able and qualified to

evaluate whether the goals and objectives of the monitored or evaluated public project have been fulfilled.

Dilemmas arise about whether so-called “hot” activities should be limited to a restricted group of qualified citizens, or should be open to the whole body of citizens. There are arguments both for and against such kind of limitations. The supporting arguments for the former approach concern the qualifications (or lack thereof) of citizens. The “contra” arguments are inspired by the desire to adhere to the principles behind citizen sourcing and its potential for open innovation (Table 3).

The areas for the application of citizen sourcing, as described by Nam (2012), represent a matrix of possibilities for fostering the means of co-creating in local environments and community lives.

**Table 3:** Areas of application of citizen sourcing

Dimension	Category
Purpose	Image-making Information creation Service co-production Problem solving Project design and formulation Policy making
Type of wisdom collected	General opinion/supportive thinking Professional skills and knowledge Innovative ideas
Strategy in decision making	Contests Co-working with professionals from administrative bodies Wiki Social networking Social voting

Source: Author’s construction, adapted from Nam (2012, 14; Table 1).

There are three main stages in the process of evaluation (design evaluation, process evaluation, and outcome evaluation – Table 4) each of which is characterized by specific evaluation criteria. In many of the completed projects of citizen sourcing in different countries (Belgium, Iceland, the USA, Colombia, and Serbia) most of the evaluation criteria have been already introduced (albeit not all of them in every project).

**Table 4:** Evaluation Criteria

Focus	Criteria
Design evaluation	Sociotechnical design Functional design Procedural design Government 2.0 policy design
Process evaluation	Transparency Openness of information about operations and decisions of government Openness of information for participation and collaboration Openness of participation and collaboration processes Participation Inclusiveness Representativeness Diversity Collaboration Communication Partnership Deliberation
Outcome evaluation	Effectiveness Impact

Source: Nam (2012, 16; Table 5).

## 6 Citizen sourcing in practice, and the case of the city of Pancevo (participative budgeting)

Citizen sourcing is a useful model for developing more inclusive and democratic cities, but its application does not look back on a longer tradition (Torres 2007). However, there are already a number of cases that offer evidence of the feasibility and practicability of applying the philosophy of crowdsourcing to the problems of local governments and local communities. Citizen-sourcing projects are present in many cities worldwide: from Latin America (e.g. in Medellin<sup>8</sup>) to Europe (e.g. in Ostend<sup>9</sup>). Some projects have become very well known and have started to serve as the benchmarks for further applications of the approach. There have been various contributions to the general methodology of the citizen-sourcing approach as a result of these many completed projects. One of them is the creation of the internet-based platform called Citizenlab.<sup>10</sup>

In spite of the large number of positive outcomes of developing citizen sourcing projects, there has been a lack of a critical approach to completed initiatives. In particular, many authors have failed to recognize that this inclusive and democratic approach may be used

to manipulate voters by giving them the illusion that they are becoming decision-making factors in community development.

In Serbia, citizen-sourcing projects are carried out under the name of "participative budgeting". These projects are supported from EU funds with the cooperation of BIRN<sup>11</sup> and NALED.<sup>12</sup> The projects involve citizens in the process of decision making and increase the transparency of economic development measures. The program has initiated the implementation of citizen-sourcing projects in ten Serbian municipalities, the city of Pančevo being one of them.

Citizen-sourcing projects involving participative budgeting – including the case-study project in Pančevo – are implemented in the following way, as a rule:

1. First, the budget which is available is identified, about which the opinion of citizens is collected. In many cases, this budget is a residual amount of the annual budget of the local government which remains unspent. In selected cases, however, the local government exclusively devotes finances to participative budgeting in order to facilitate the co-production of public services and municipal activities (Cassia and Magno 2009).
2. The second step consists of elaborating and investigating various alternative ideas and attaching budget lines and costs to the related hypothetical tasks.
3. The third step is to vote on the previously defined alternatives and to compare the number of "likes" and "dislikes" associated with them.
4. Finally, the chosen project is implemented.

The framework of the Pančevo participative budgeting project for 2016 was based upon six characteristics.

- For the year 2016, the budget to be decided on was approximately five million dinars (cca, 42,000 euros).
- The proposed and selected projects had to conform with the aims and constraints defined by the document *Strategy for development of the city of Pančevo for the period 2014–2020*.<sup>13</sup>
- The project proposals had to fit into one of four areas: they had to be either ecological [pro-environmental], or cultural, or social proposals, or facilitate industrial development.
- The call for proposals and the ideas received were completely transparent to the public.
- The compilation of the shortlist and the selection of proposals had to be carried out by the local municipality team on the basis of the following criteria: a) to what extent the project proposal was clear and feasible; b) how well the project proposal matched the priorities defined by the aforementioned "Strategy..."; and, c) the required financial resources.
- The project proposals were uploaded and presented on the internet and the winning entry was decided based on the number of "likes" received by each proposal.

One of the critical aspects of citizen sourcing is motivating citizens to take part in initiatives (Brabham 2009) and, crucially, getting them engaged in the development of solutions, monitoring and performance auditing, and ultimately policy making. Since the level of trust towards institutions is relatively low in Serbia, the response rate to the participative budgeting call of the Municipality of Pančevo was also relatively low.

In total, 903 votes were collected, a number which was evaluated by the Pančevo municipality as a good response. Four project proposals were nominated, with the results being as follows:<sup>14</sup>

- Purchasing a catamaran boat for tourists – 353 votes;
- Developing cultural-tourist paths – 279 votes;
- Renovating the public clocks in the city – 194 votes;
- Publishing a services guide to the city of Pančevo – 77 votes.

The process of evaluation was based on a table that included some well-defined criteria:

- The project should be important to the city; its deliverables should significantly improve the quality of life in Pančevo (1–5 points).
- The project should be understandable to citizens, and the recommended intervention should serve some specific need of the city (1–5 points).
- The benefits of the project should be enjoyable by a huge number of citizens (1–5 points).
- The project costs should be small (1–5 points).
- The implementation period should be short (1–5 points).

As a result of the voting, Pančevo obtained a catamaran boat for cruising on the nearby Timiș river.<sup>15</sup>

Critical evaluation of this example reveals the following facts:

- For this proposed project only some 353 citizens voted from a total of 76,200 inhabitants living in the urban area.<sup>16</sup>
- Pančevo is known as an industrial city (it has major processing industries), and has pollution-related problems. The nomination of the tourist boat as the winning option from the participative budgeting process signifies that the local government is dealing with peripheral problems that are not of crucial importance.
- As a general conclusion, it seems that in the process of launching a citizen-sourcing project the local administration should have started from the principles contained in theories of local economic development and should have assessed more thoroughly its resources and capacities (Blakely and Bradshaw 2006). Starting from the right place is critical from the point of view of the success of participative budgeting projects (Loukis 2018).

## 7 Conclusions

Integrating the ideas and knowledge of citizens through the process of fostering cooperation between citizens and local governments is a dynamic and sensitive task (Surowiecki 2004). Crowdsourcing techniques and the results thereby obtained rely on outcomes previously generated in the area of business. Citizen sourcing could benefit from the collection of successful case studies of commercial crowdsourcing and from citizen sourcing projects, as well as from learning the lessons of crowdfunding platforms, as summarized in publications and studies that address the topic. Schmidthuter and Hilgers (2017) are right when they state that studies and research on citizen sourcing are lacking compared to the range of publications about the business applications of crowdsourcing. ICT-based methods (Bertot *et al.* 2010a; Bertot *et al.* 2010b) were first introduced by companies. In particular, crowdfunding platforms established by the so-called creative industry have been very significant contributors. The technique is increasingly implemented by government agencies in the framework of citizen-sourcing projects.

Evidence collected from local communities such as Pančevo (Serbia), Ostende, Hasselt, Brussels (Belgium), Reykjavik (Iceland), Medellin (Colombia), etc. confirm the fact that collaborative strategies, including crowdfunding and citizen sourcing, have a better chance of being successful in those cities and regions which are characterized by bigger stocks of social capital (Beugelsdijk and van Schaik 2005). The level of generalized trust and institutional trust (Parent *et al.* 2005) drives the willingness of citizens (Lukensmeyer and Torres 2008) to participate in calls and to select and manage projects in local communities. An analysis of the success of citizen-sourcing projects in Flanders (Belgium) shows that there is a positive correlation between the success of citizen sourcing on the one hand, (Ostend, Hasselt, etc.) and the level of social capital as measured at the level of European regions. In particular, trust scores at the NUTS 1 level in Europe are highest for Flanders, Belgium.

### Notes:

<sup>1</sup> “Co-creation” is defined by Wikipedia (2019) as follows: “Co-creation is a management initiative, or form of economic strategy, that brings different parties together (for instance, a company and a group of customers), in order to jointly produce a mutually valued outcome”. Available at: <https://en.wikipedia.org/wiki/Co-creation> (15 March, 2019).

<sup>2</sup> “Self-management” is defined by Wikipedia (2019) as follows: “Workers' self-management (also referred to as self-management, labor management, autogestión, workers' control, industrial democracy, democratic management, and worker cooperative) is a form of organizational management based on self-directed work processes on the part of an organization's workforce”. Available at: [https://en.wikipedia.org/wiki/Workers%27\\_self-management](https://en.wikipedia.org/wiki/Workers%27_self-management) (15 March, 2019).

<sup>3</sup> “Mitbestimmung” is defined by Wikipedia (2019) as follows: “Codetermination in Germany is a concept that involves the right of workers to participate in management of the companies they work for. Known as Mitbestimmung, the modern law on codetermination is found principally in the Mitbestimmungsgesetz of 1976. The law allows workers to elect representatives (usually trade



union representatives) for almost half of the supervisory board of directors". Available at: [https://en.wikipedia.org/wiki/Codetermination\\_in\\_Germany](https://en.wikipedia.org/wiki/Codetermination_in_Germany) (15 March, 2019).

<sup>4</sup> Examples of other management and marketing terms that have been coined relatively recently include e-commerce, telemarketing, stakeholder, etc.

<sup>5</sup> Jeff Howe is a technology and management journalist and theoretician who in 2005, together with Mark Robinson as editors of the technology periodical "Wired", coined the term "crowdsourcing" to describe how businesses were using the internet to "outsource work to the crowd".

<sup>6</sup> Defined by the Merriam Webster Dictionary. Available at: <https://www.merriam-webster.com/dictionary/crowdsourcing> (15 March, 2019).

<sup>7</sup> Another example of crowdsourcing is the "Coop-Online Coach" in Switzerland: a site where users can trade information about healthy eating and exercise. Available at: [www.coopcoach.ch](http://www.coopcoach.ch) (15 March, 2019).

<sup>8</sup> The website "Mi Medellin" is a citizen-sourcing initiative of the city of Medellin (Columbia). See: <http://www.mimedellin.org/> (15 March, 2019).

<sup>9</sup> Oostende is a city of more than 70,000 inhabitants in Belgium. In 2018 its local government launched a project which aims at asking citizens for their creative ideas to improve life in the city on an ongoing basis (CitizenLab 2019). See: <https://www.citizenlab.co/case-studies-en/ostend> (5 March, 2019).

<sup>10</sup> CitizenLab is a Brussels-based company that produces citizen participation software for local governments to help them engage citizens and drive better policy decisions. See: <https://www.citizenlab.co/> (5 March, 2019).

<sup>11</sup> BIRN is the abbreviation for the Balkan Investigative Reporting Network. This is a civil sector organization for advancing critical journalism. See: <http://www.birnsrbija.rs> (15 March, 2019).

<sup>12</sup> NALED is a civil sector organization designed to promote Local Economic Development. Its name is an abbreviation for *Nacionalna Alijansa za Lokalni Ekonomski Razvoj* (National Alliance for Local Economic Development). See: <http://naled.rs/> (15 March, 2019).

<sup>13</sup> The document is available at: <http://www.pancevo.rs/sadrzaj/uploads/2014/07/City-of-Pancevo-Development-Strategy.pdf> (15 March, 2019).

<sup>14</sup> Report on the results of the participative budgeting voting. See: <http://www.pancevo.rs/vesti/rezultati-glasanja-u-okviru-projekta-participativno-budzetiranje/> (15 March, 2019).

<sup>15</sup> Report on the implementation of the project involving the purchase of a catamaran by the city. See <http://www.pancevo.rs/vesti/pancevo-dobilo-svoj-katamaran-panuku/> (15 March, 2019).

<sup>16</sup> Data retrieved from: <https://en.wikipedia.org/wiki/Pancevo> (15 March, 2019).

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## **Assessing Entrepreneurship and Innovation in Higher Education Institutions: The 'HEInnovate' Initiative at the Universidade de Aveiro, Portugal**

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& VICTOR NETO

**Abstract** HEInnovate is the name of a questionnaire-based self-assessment tool for higher education institutions, which has been used to evaluate their entrepreneurial and innovative activities. The method has been elaborated and disseminated by the OECD and the EU. This paper presents this self-assessment method and portrays its application at the Department of Mechanical Engineering (DME) of the University of Aveiro (UA), Portugal. The paper provides insight into how these results are utilized in designing and implementing activities that connect the university more deeply with wider Society.

**Keywords:** • HEInnovative • Portugal • universities • innovation • entrepreneurship

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## 1 Introduction

HEInnovate is the name of a questionnaire-based self-assessment tool for higher education institutions (HEIs), which has been used to evaluate their entrepreneurial and innovative activities. This paper presents this self-assessment method and portrays its application at the Department of Mechanical Engineering (DME) of the University of Aveiro (UA), Portugal.

The elaboration of the method and its international dissemination is an initiative of the European Commission, of the EU Commission's Directorate General (DG) Education, Youth, Sport and Culture,<sup>1</sup> and of the Local Economic and Employment Development Programme (LEED) of the Organisation for Economic Co-operation and Development (OECD). The HEInnovate Programme was launched in 2013 (OECD 2014). The participating institutions (universities, university colleges, polytechnics, etc.) have used this method in dozens of countries to assess their leadership and staff capabilities, together with links with business. The lessons learnt from the international application of the HEInnovate instrument have been summarized in a series of publications (e.g. OECD 2018).

HEInnovate was used twice at DME as a tool for positioning the department (Gabriel 2017). This exercise was fully supported by the leadership structure of UA. The current paper describes the setup, the implementation of the questionnaire-based tool within DME, and especially its results and related outcomes. In particular, the paper provides insight into how these results are utilized in designing and implementing activities that connect the university more deeply with wider society.

## 2 Project activities

HEInnovate – as a method – was applied in the self-assessment of the department twice – in 2015 and 2016. In 2013 the OECD originally introduced the method with only seven groups of evaluation questions, also called dimensions (OECD 2013). The extension of the evaluation questionnaire by an additional, eighth dimension, “Digital Transformation and Capability,” has occurred later on. Thus, users at the Department applied seven dimensions to analyse and diagnose their experience and to assess the extent of innovation- and entrepreneurship-friendliness of the University. During the questionnaire-based survey, respondents were asked to evaluate a series of relevant criteria/statements (see Table 1). The same process was followed during the interviews and group sessions.

**Table 1:** Structure of the HEInnovate questionnaire and selected criteria/statements

Dimension	Selected examples of criteria/statements for numerical evaluation
Leadership and Governance	Entrepreneurship is a major part of the university strategy.
	There is commitment at a high level to implement the entrepreneurial strategy.
Organisational Capacity: Funding, People and Incentives	The entrepreneurial agenda is supported by a wide variety of funding sources/investment, including investment by external stakeholders.
	The higher education institution has sustainable financing in place to sustain the entrepreneurial university strategy.
Entrepreneurial Teaching and Learning	The higher education institution is structured in such a way that it stimulates and supports the development of entrepreneurial mindsets and skills.
	Staff takes an entrepreneurial approach to teach in all departments, promoting diversity and innovation in teaching and learning.
Preparing and Supporting Entrepreneurs	The university raises awareness of the value/importance of developing entrepreneurial abilities amongst staff and students.
	The university actively encourages individuals to become entrepreneurial.
Knowledge Exchange and Collaboration	The university is committed to knowledge exchange with industry, society and the public sector.
	The university demonstrates active involvement in partnerships and relationships with a wide range of stakeholders.
The Internationalized Institution	Internationalization is a key part of the university's entrepreneurial strategy.
	The university explicitly supports the international mobility of its staff and students (including Ph.D. students).
Measuring Impact	The university assesses the impact of its strategy on entrepreneurship across the institution.

Source: OECD (2013).

During the first application of HEInnovate at the department in 2015, the sample of respondents consisted of one hundred and four persons, all of the members of the Research Unit 'Centre for Mechanical Technology and Automation' (TEMA) (Hetherington *et al.* 2015). The implementation of the HEInnovate instrument followed a consistent, systematic and practical approach, described as follows:

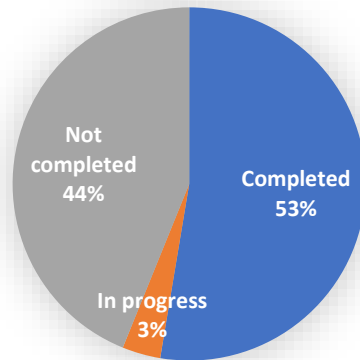
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- A workshop<sup>2</sup> was organized about the potential, objectives, functionality and expected impact of the program, which was followed up by a preliminary study.
- The primary target audience was defined with the support of the Director of the DME. The target audience was selected in a way as to represent the wide range of visions and perceptions of different actors inside DME and UA, namely:
  - Scholars working on projects;
  - Post-Doctoral and Ph.D. students;
  - Researchers;
  - Professors.
- Personal invitations were sent to each person from the target groups, using official email communications through the HEInnovate Internet platform. To this end, a workgroup was created within HEInnovate on November 25<sup>th</sup>, 2014, entitled "Department of Mechanical Engineering, University of Aveiro, Portugal". The personal emails sent by the organizers of the present report also included a summary of the main ideas behind HEInnovate and its importance for the purpose of effectively raising awareness about the self-assessment tool.
- The time period for data collection for the assessment was defined as November 25<sup>th</sup> to December 31<sup>st</sup>, 2014.
- The analysis of the incoming data and the preparation of a preliminary report lasted from January 1<sup>st</sup> to February 28<sup>th</sup>, 2015.
- Personal invitations to personal discussion sessions were sent out using the official email communication channel, offered by the HEInnovate Internet platform.
- Personal discussions were held on March 3<sup>rd</sup>, 2015 in order to enrich the findings with individual feedback.

The questionnaire was completed online via the HEInnovate Internet platform. The data collection software ensured that the confidentiality of the users was automatically respected. One hundred and four invitations to complete the self-assessment were sent out. Only 40% of the former were invited to a personal discussion, being these individuals those who had completed the questionnaire and given permission for the recording of their personal data. Figure 1 shows the proportion of respondents that participated in each phase.

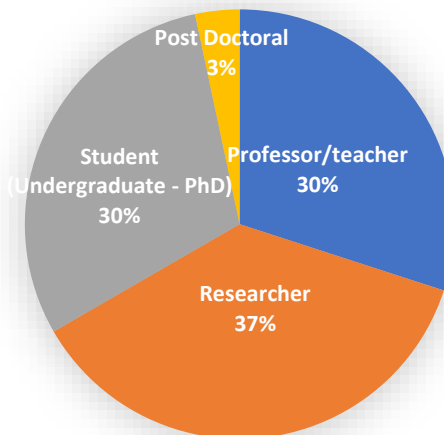


**Figure 1:** Proportions of sample invited to participate according to the participation activity



With regard to the completed questionnaires, the positions and professional categories of respondents within HEI were distributed across four main fields, as shown in Figure 2.

**Figure 2:** Proportions of respondents according to position/professional category



About 43% of respondents to the questionnaire decided to remain anonymous.

The results of the questionnaire-based survey were shared and debated in a personal discussion session which was devoted to the following topics:

- The usability and user-friendliness of the self-assessment tool, and personal experiences with HEInnovate;
- Did the application of HEInnovate contribute to any changes in the perception of entrepreneurship at the department?
- How can HEInnovate be used, in practice, to initiate long-term, sustainable institutional changes?
- Identifying the key stakeholders to be involved;
- Current challenges to making a real change in attitudes at the university;
- Feasibility or relevance of widening the application of the HEInnovate instrument to other levels of the institution.

During the personal discussions, the 'Entrepreneurship Development in Teaching & Learning' topic was the one debated at greatest length. The project highlighted that the stakeholders participating in the discussions had distinct perceptions and visions about how entrepreneurship should be present at the University (Heitor and Horta 2016). During the personal discussion, the opinions of students were also voiced, since the members of the Association of Mechanical Engineering Students (NEEMec)<sup>3</sup> of UA was also contacted and invited to use HEInnovate.

On the occasion of the second application of HEInnovate at the University, in 2016, project managers ensured the deeper engagement of users based on lessons learnt from the first application of the HEInnovate instrument. For this purpose, among others, an additional personal discussion was organized prior to implementing the questionnaire-based survey.

During the personal meetings, HEInnovate was optimized as a communication instrument to foster the entrepreneurial and innovative spirit of the university. The meetings improved the applicability of the HEInnovate assessment method to the particular case of the Department of Mechanical Engineering and the Integrated Master course in Mechanical Engineering. At this point, the relevance of each of the seven topical areas (also called dimensions) was discussed, interpreted and contextualized for each of the targeted respondent groups, namely, for the students, for the staff of departments, and for the staff of the rectory (Gabriel *et al.* 2016c).

### **3 Lessons learnt from the project**

Respondents and other stakeholders who have participated in the project found that HEInnovate was a powerful tool for diagnosis, both for individuals and for the institution. There was a wide agreement that the findings/outputs are operationalizable; i.e., they can

be immediately converted into strategic actions. The responses to the questionnaires and the personal discussions revealed the following findings.

The Project contributed to the creation of the Science and Engineering Education (SEE) Group within the university in 2015. This is composed of a team of teachers from higher education and researchers from the Department of Mechanical Engineering. Initially, the group focused on the study and development of skills that are essential to the teaching of engineering-related fields, namely those most similar to mechanical engineering at the university level. The SEE Group is currently working on improving educational services and facilitating interaction with students to attract them to Science, Technology, Engineering and Mathematics subjects (STEM) and the respective careers. The university has developed innovative models of teaching entrepreneurship in classrooms and at summer academies. Several activities were carried out to improve the engagement of academic staff and students in studying entrepreneurship, innovation and STEM (Neto 2018; Gabriel 2015).

In 2016, the SEE Group organized the first National Engineering Education Forum, which attracted one hundred participants, to debate the future of engineering education (Gabriel *et al.* 2016b). The aim of the forum was to improve university leadership and governance with special respect to entrepreneurial teaching and learning, training, and supporting entrepreneurs, facilitating knowledge exchange and collaboration in an internationalized setting. The summary report of the forum (SEE Group 2016) reinforced the fact that the keys to better engineering education are improving the professional profiles of higher education teachers (EC 2017a), and introducing innovative models and methodologies for learning and teaching.

International connections in the field of entrepreneurship and innovation have proved to be fundamental to research, development and innovation (RD&I) activities.

- The academic staff of UA has attended training courses offered by a German think-tank of entrepreneurship research, Strasczeg Center for Entrepreneurship (SCE), München. The courses were attended by the academic staff at the university and by teachers from other higher education institutions (HEInnovative 2017; EC 2017b; University of Aveiro 2016a; University of Aveiro 2016b; University of Aveiro 2016c).<sup>4</sup>
- Under the scope of the Erasmus+ Programme, students and teachers at UA participated in classes and workshops devoted to entrepreneurship research, presented by European experts.
- In 2018, the University of Aveiro, in a joint initiative with the Portuguese Society for Engineering Education (SPEE), organized the Third International Conference of the Portuguese Society for Engineering Education.

The SEE Group and the HEInnovate Project have contributed to more active research activities at the university, resulting in a wide range of scientific publications (Andrade-Campos *et al.* 2018a; Andrade-Campos *et al.* 2018b; Gabriel 2017; Gabriel *et al.* 2016a; Gabriel *et al.* 2016b; Gabriel *et al.* 2016c; Gabriel *et al.* 2017; Gabriel *et al.* 2018).

DME has participated in six European RD&I projects in collaboration with international partners under the scope of the Horizon 2020 EU Research and Innovation programme. Moreover, DME also participated in a national research and development project under the *Fundação Calouste Gulbenkian* program for innovation in Higher Education (Ashley 2018).

#### **4 Impact**

One of the goals of the SEE Group is to convert the results of its Research, Development and Innovation (RD&I) results into impacts on society that go beyond the boundaries of the scientific community and the university. HEInnovate has provided guidance on to how to improve inter-university communication, and how the graduates of UA can apply the results of RD&I in entrepreneurial projects and in start-up companies (Hofer and Kaffka 2018).

HEInnovate has improved awareness about entrepreneurship and innovation at the university, helped increase the quantity and quality of knowledge about important related areas, and improved both inter- and intra-departmental communication between colleagues, as well as with the central administration of the university. Particularly, the momentum generated by the HEInnovate Project has facilitated the collaboration of various departments of UA in various projects.

At the national level, the HEInnovate Project has facilitated the participation of UA in relevant professional networks and positioned UA as an active partner in different initiatives involving HEIs for entrepreneurship and innovation.

At the international level, the HEInnovate Project has increased the number of collaborative projects with international partners and facilitated the interactive dissemination of scientific knowledge.

#### **5 Conclusions**

The HEInnovate initiative has supported the members of the SEE Group to properly diagnose and understand the level of entrepreneurship and innovation within the Department of Mechanical Engineering of University of Aveiro, Portugal. It has also catalysed important debates about the entrepreneurial and innovative strategy of the university (Hofer and Kaffka 2018).

The project has also identified several barriers to innovation and entrepreneurship within HEI, such as:

- People's resistance to change.
- Doubt about the relevance of entrepreneurship as a tool for growth and knowledge.
- Mistrust associated with colleagues positioned lower in the hierarchy of HEIs.

The project highlighted the importance of teachers at HEIs having an entrepreneurship-friendly and innovative attitude and pointed out the overriding importance of international connections and networks, crucial for engaging in effective collaboration.

#### Notes:

<sup>1</sup> This DG was formerly called DG Education and Culture.

<sup>2</sup> 'HEInnovate workshop: Entrepreneurial University Good Practice Exchange'. November 18th, 2014, Lisbon.

<sup>3</sup> In Portuguese: NEEMec = Núcleo de Estudantes de Engenharia Mecânica.

<sup>4</sup> For further information please check:

- Re-launch of HEInnovative, Innovating Higher Education, 18 November 2015, Brussels, Belgium. Available at: <https://heinnovate.eu/en/news/heinnovate-re-launch-november-18th> (15 March, 2019).
- Conference i3: iGNITE. iNSPIRE. iNOVATE – Facilitating change in Higher Education, 19–20 May 2016, Brussels, Belgium. Available at: <https://heinnovate.eu/en/news/i3-igniteinspireinnovate-event-registration-now-open> (15 March, 2019).
- Make Innovation Work in Higher Education Conference, 27–28 February 2018, Brussels, Belgium.
- Train the Trainers Western Balkans and HEInnovate: Supporting Institutional Change in Higher Education, 14–15 June 2018, Ruse, Bulgaria. Available at: <https://heinnovate2018-bulgaria.eu/> (15 March, 2019).

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## **Conclusions**



## Varieties and Perspectives of Local Development: A Conclusion

BRUNO DALLAGO

**Abstract** This chapter outlines the state of the debate on local development and places the content of the book within it. The chapter stresses the problematic nature of localness and highlights the existence of different broad and alternative varieties of local development, depending on their mix of adaptation to local circumstances and international integration. Given this complex and multidimensional nature of local development, it is important to use a comparative method and a systemic, simplified and coordinated approach to it. Using this methodological perspective, the chapter identifies three fundamental dimensions of local development: efficiency, stability, and rights. These dimensions identify the fundamental features of local development and the roles it plays. The chapter ends by identifying unsolved problems and open challenges in local development research.

**Keywords:** • comparison • efficiency • local development • proximity • rights • stability • system • varieties of local development

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## 1 Introduction

This book deals with local development as seen from many different angles and has the final goal of clarifying how it should be taught to new generations of university students. Therefore, the book is premised on two fundamental considerations. First, local development is important and complex. Second, local development is a subject worthy of academic research and education so as to foster the related knowledge and have future agents capable of solving problems and promoting local development. Therefore, the book is based on the implicit understanding that local development is inadequately well understood; that it has to be further promoted by more- and better-skilled agents, and that it should make use of better tuned, more effective policies. Implicitly, these observations send the message that spontaneous developments, albeit real and important under certain conditions and circumstances, are not sufficient everywhere and at all times. This opens the question what should be done to foster the positive response that local development represents.

It is therefore important to understand what local development is, why it is important, why it is complex, why it is in inadequate supply, and why a comparative and systemic approach is necessary. These may appear to be odd demands after so many analyses and publications have already come to light, so much money and effort has been invested in local development projects and efforts, and after so many spontaneous processes have led to both successful local development and also its failure. Clearly, raising these kinds of questions is equivalent to stating that these analyses and publications are inadequate or have at least been ineffective so far, that spontaneous processes have at least been insufficient, that the money and effort that has been spent has not been enough, and was not always spent well – or perhaps that counterproductive processes have emerged and undesirable objectives have been met. This book is therefore welcome as it provides a finely tuned, variegated picture of local development by means of analyses and case studies.

This concluding chapter aims at providing a comparative and integrated systemic picture of local development and highlights how the book contributes to the development of such a picture. Since local development includes an extremely variegated set of components which vary from one context to the other, but also includes some reference points that are common to all cases, it is important to understand and distinguish both what is specific and idiosyncratic, and what is general and universal in local development. From this perspective, local development involves the connection between the particularity of the locality and the generality of participation in social life, including at the national and global levels.

Any locality and any particular component of it is in a sense unique: it has features, traditions and components that are distinct from those of other localities that have emerged from many different factors of economic, natural, political, social, technological origin. At the same time, any locality, particularly in the modern open world, shares some

fundamental general features and factors that allow the locality to interact with other localities and the rest of the world. Examples of the former are nearly infinite, and include particular cultural traits and traditions, social groups and minorities, economic activities, and areas of natural beauty. Important cases of the latter include the observance of law and order, respect for property rights and contracts, the existence of a recognized government and compliance with its decisions, and adaptation to policies, be they at a local, national or international level.

For example, when the European Central Bank takes a monetary policy decision or a national government adopts an environmental law, the effects are felt not only at a national level, but also at any local level. Although local adaptations may be different depending on the particular features of localities, the latter nevertheless have to adapt. Since the fundamental economic features of localities do not change perceptibly in the short term, and provided that the central bank or the national government has good knowledge of the localities, monetary or environmental policies can also anticipate the effects of particular policies at a local level. This effect is therefore predictable and manageable, at least in part. At the same time, any particular behavior of or interaction among localities may prompt central authorities to make and implement certain decisions. Therefore, what is general is important for what is local, just as much as the latter is important for the former. This also means that local development, to be effective, should be in tune with general external circumstances, as much as the latter should be in tune with their territorial composition.

Given the variegated essence of local development and its many different features in diverse parts of the world, the comparative approach is particularly useful and productive for highlighting these differences and their nature, thereby allowing the mapping of local developments. At the same time, comparisons allow us to distinguish what is general from what is particular in many different localities. This permits identification of the general features of local development. This combination of particular and general features in any case of local development also requires an integrated systemic perspective. “Integrated” means putting all the particular components into their proper place, and the mutual relations in order, to arrive at a complete and coordinated (i.e., systemic) perspective about local development.

This concluding chapter outlines the state of the debate on local development, considers the most proficient approach for studying and governing local development, looks at unsolved problems and open challenges, places the contributions of this book in these perspectives, and proposes topics for further research in relation to open local development. The following section introduces the concept of local development and stresses the problematic nature of localness. Section 2 completes the picture by highlighting the existence of different broad and alternative varieties of local development, depending on their mix of adaptation to local circumstances and to international integration. Section 3 distinguishes between external and internal processes in local development, while Section 4 looks at the causes of failure of local development

programs and stresses the importance of an integrated approach, of which this book provides an example. The topic of Section 5 is the multidimensional nature of local development and the difficulty of treating it in a synthetic way. This requires a simplified and coordinated – i.e. a systemic – approach. Section 6 aims at giving substance to this perspective by identifying three fundamental dimensions of local development: efficiency, stability, and rights. These dimensions, which are extensively and properly treated in the book, identify the fundamental features and roles that local development plays. Yet much remains to be researched and understood about local development. Section 7 looks at the interplay between vertical and horizontal relations in local development, while Section 8 highlights some fundamental challenges from this perspective. Section 9 concludes.

## 2 On local development

Local development generally refers to the change and transformation of a locality, usually in the sense of improving one or all of the following: its level of material and social welfare, economic performance, well-being and opportunities offered to its inhabitants, knowledge and circulation of ideas, availability of technologies, resilience to shocks and negative events, external relations, internal stability and cooperation, or social and environmental sustainability. The study of local development is therefore a way to interpret performance and change at a meso-level using localities as the unit of investigation rather than focusing more narrowly on individual social actors and organizations. A locality is usually meant as a territory; i.e., any social and geographical component situated below the national level, so that the latter includes the interaction among various localities.

In the above configuration, local development directly relates to the way that societies, economies and institutions interact among themselves at a local level as well as with the rest of the world; i.e., with those of other localities and countries. Moreover, local development also depends on the ability of local actors to improve the social and material potential of their own localities, to encourage cooperation, and to inspire the participation of the local population and institutions.

However, the concept of “localness” is problematic for different reasons. Geographical spaces (“territories”) are internally and externally heterogeneous, while there is rarely a unified “local interest”. Moreover, the relationship between the spatial dimension of processes and institutions is dynamic in the sense that it changes through time, and depends on the nature of problems and processes. So the boundaries of the “local” may shift according to the issue and the processes under consideration, and different definitions and concepts of what is local typically exist. For instance, from an administrative perspective the local refers to criteria of administrative convenience, while cultural approaches highlight shared values and identity. For the economist what matters are the predominant patterns of industrial and agricultural production and exchange, while for political scientists the important feature is the existence of an executive power

with competence over the locality concerning some critical matters. The sociologist usually sees in the local the prevalence of established social patterns of relation and interaction, while the legal scholar looks at competence in terms of legal norms and the existence of a legislative council competent to deal with critical matters. In a historical perspective, local refers to common historical vicissitudes, self-identification and external recognition, while according to geography the local has to do with commonalities of orography, altimetry, catchment basins, and the environment.

All these definitional vagaries clarify how difficult yet fundamental it is to take a comparative systemic approach to local development, and may lead to the question being raised whether limiting development spatially really makes sense. The answer to this question is obviously positive, because there are factors of a social, technological, intangible and material nature that make the locality a better level of analysis for certain issues and processes and local action or action at a local level the most effective. To name just a few of these, economies of agglomeration are real and important, the role of local constituencies critically significant, local social relations and collective action effective, the competence and power of local governments important, and the local production and circulation of intangible factors such as knowledge and ideas strategic.<sup>1</sup>

For these and similar reasons, what is socially relevant for local development goes beyond the limits of other perspectives (e.g. geographical and sometimes historical ones) because the overstepping of those "alien" boundaries allows social constituencies to capture advantages and resilience from cooperation and participation, and to progress more speedily and effectively. To understand why a certain locality forms and is active and resilient, taking a systemic view is necessary. This is a view that looks at consistencies in the relations among the different components of local development, and pursues generalizations that allow a simplified analysis of what keeps a locality together and working and makes its functioning predictable. To understand why localities have different features and levels of performance and evolve in different ways, and, in particular, why some localities and others do not (Feldman 2014), a comparative perspective is necessary. This is a perspective that confronts different localities, highlights differences and similarities in their construction and working, relates these to the outcomes, and through such comparison identifies better ways of promoting local development.

However important local development is, one should never overlook the existence of important and powerful obstacles to it. Some of these are external to the locality, such as an unfriendly or centralizing national government, the existence of distributive coalitions among other localities, and tensions and conflicts with other localities. However, most obstacles are probably of an internal nature and include entrenched local policy styles, political instability, a lack of cooperative and innovative attitudes among local participants, extreme poverty, an undeveloped infrastructure, and many more (OECD 2003). One of the merits of this book is how it presents directly, or provides analyses and elements that allow for, a comparative and systemic view of local development.

### 3 The varieties of local development

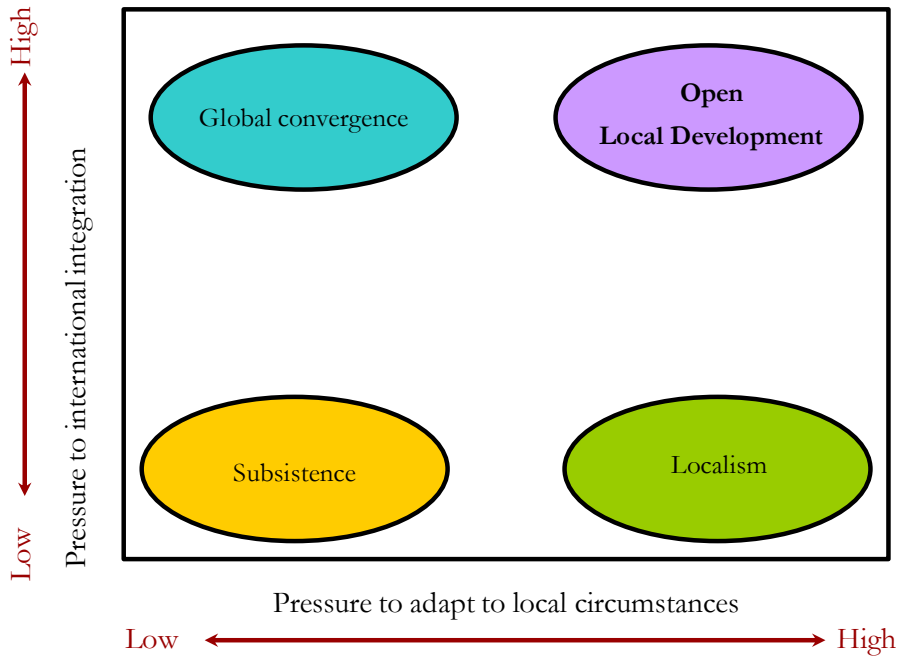
One of the most controversial issues in the analysis of local development is why and how different and separate localities should continue to exist and why some of them flourish and others ail. This question leads us to enquire whether each locality should be self-sufficient in its own particular way, or whether each locality should specialize based on its endowments and interact and exchange with other localities. The essence of this question concerns the static and dynamic role of the cohesive force of proximity (Balland *et al.* 2015; Boschma 2005) – the essence of a locality in its economic, geographic, political, and social sense – vis á vis the remoteness, advantages and threats from the rest of the world. Being larger and more powerful, we can consider remoteness (the rest of the world) as a constraint on proximity (local development), but also as a source of opportunities. It follows that local development can be open to the rest of the world, or closed and self-sufficient. Both positions have a rationale, depending on the nature and attitude of each component (proximity and remoteness), from which the potential advantages and disadvantages of interaction are created.

In today's economies, local development has to be located within the perspective of globalization (Scott and Storper 2003), just as the present book does. This means that, following Rodrik (2007), local development should pursue the best possible adaptation to and use of local circumstances, while being respectful of general issues and rules. This boils down to finding one's best possible place in the world, and doing what one knows and does best (i.e. knowing what, and knowing how). In short, being pragmatic and in tune with one's reality and aware of external conditionalities and opportunities.

As a matter of fact, there are a number of alternative varieties of local development that exist or can be adhered to (Figure 1). The most traditional one is local development as subsistence.



**Figure 1:** Alternative varieties of local development



In this case, local development is based on the isolation of a local constituency from the rest of the world in a posture of self-defense. There is a static adaptation to local circumstances in that local development is the only way for the community to survive, and this is usually done by making traditional use of what is available locally. This is most often a weak choice that is unable to support a strong and flourishing society; a choice that comes from isolation from surrounding territories, be this due to a very low level of development, entrenched power coalitions, threats from neighbors, a lack of infrastructure or the conservative attitude of local constituencies.

Localism represents a variety of local development in which self-sufficiency is the outcome of a free choice by local society. In this case, local development is based on adaptation to local circumstances and resources based on the supposed superiority of one's locality, an aversion to foreign practices and societies, and fear of invasion or anxiety about the contamination and disruption of one's culture. This variety may be associated with good economic performance and social and political stability in favorable conditions (e.g. the Italian free municipalities in the Middle Ages), yet the advantages of exchange and interaction with other localities and specialization are foregone.

Global convergence is the preferred variety of mainstream economics and politics (Fukuyama 1992). With this variety, only the pressure for international integration matters along a standard model, be this neo-liberal, Marxist, confessional, or something else. Adaptation to local circumstances is mostly seen as a meaningless curiosity and a sign of backwardness and isolation. All that matters – be it due to the nature and working of markets or democracy, or something else – is that localities should converge to one “best” standard. Exchange, specialization and competition in the economy, and inter-locality and international trading and cooperation are important in this variety of local development, and are based on the optimal allocation of resources, similar political regimes, equal rights and local or national sovereignty. This variety allows only for some minor local variants of the same model, leaving local idiosyncrasies and, consequently, local development out of consideration.

This variety of open local development promises to overcome the unilateral, limited and one-dimensional (or dimensionless) nature of the previous varieties. It is based on the necessity of and interest in integrating internationally and making the best possible use of local circumstances. Clearly, localities differ in terms of their internal composition and construction and their relation to the rest of the world. As to the former, localities are endowed with qualitatively different resources, along with quantitative differences due to their particular traditions and preferences, dissimilar religious practices and political structures, distinctive social components and organization, separate natural environments and geostrategic placements, different kinds of knowledge, and many more issues. All these variables can be considered the endowments of localities; i.e. features and variables that are a given at any time. Following this perspective, the only choice available for a locality is to adapt to these endowments and make the best possible use of them in order to improve efficiency and the level of development, and to pursue social and political stability and guarantee desirable rights to its citizens.

Such qualitative differences – together with the quantitative differences in the endowment of resources – create opportunities for advantages and gains by means of specialization and interaction with other localities. If any locality is able to make the best possible use of its endowments, it will find its best possible place in the world. Since endowments vary qualitatively and quantitatively, and since the abilities and constraints on using them vary from one locality to the other, localities differ in both an absolute and relative sense from each other. Different varieties of local development follow, which make the comparative approach particularly useful and important.

Thus, a locality rich in natural resources may have a favorable basis for development and exchange with other localities. This is the case, for example, of Canada, a country in which extended localities specialized in cod fisheries, the fur trade, cereals, and timber. This specialization stimulated the development of an upstream industry producing machines for mechanizing those staple activities, and a downstream industry for transforming the raw materials into finished products. This regional specialization affected the regions’ and the country’s economic, social and political development and

brought export-led growth to a more sophisticated and successful level (Altman 2003; Watkins 1963).

In other cases, abundant endowments of natural resources have led to slower growth or economic disaster and social and political disruption, as in the many cases that are referred to when the “curse of natural resources” is mentioned (Frankel 2012; Venables 2016). In a similar vein, any locality that includes different linguistic or ethnic components may find in this complexity a reason for development and stability, or one for disruption and tragedy. In the former case, cultural and ethnic variety may attract tourists or may create opportunities for different forms of specialization and entrepreneurial activities within the same locality. The existence of linguistic minorities has been shown to foster the establishment of beneficial relations and cooperation with countries where the minority language is the national language, as in the case of the German-speaking minorities in Central Europe. In the latter case, however, the linguistic or ethnic complexity of a locality may end up in tension, contrasts, and mutual obstruction, even leading to civil war.

This book fully adheres to the perspective of this open variety of local development, including its various declinations in the case of different localities. What emerges is a rich panoply of the many varieties of local development that can exist, from highly developed and stable localities (e.g. Regensburg, in the paper by *Litzel and Rust*) to war-torn and natural-disaster-affected localities (e.g. see *Waisová and Cabada* on environmental cooperation and security, and *Pant* on central Nepal). This panoply offers an excellent basis for further research, particularly that which employs a comparative perspective across localities and time and investigates the reasons for and rationale of the different varieties of local development, different ways of adapting to and making use of local circumstances and their advantages and disadvantages, and the conditions necessary for and the possible modes of the beneficial openness and international integration of a locality.

#### **4 External and internal processes**

In a thought-provoking book about the fundamental challenge of development – i.e., alleviating poverty and conserving the environment –, Sayer and Campbell (2004, 3) ask the fundamental question “... why [has] the manifestly sensible goal of managing natural resources in an integrated manner ... proven so elusive”? This observation can be extended to any type of resource, including human and intangible ones. The latter case is even more challenging, since human and immaterial resources – such as knowledge or entrepreneurship – can be considered, following Baumol (1993), as evenly distributed among countries and localities, while natural resources are not. Since there is abundant theoretical knowledge and practical evidence that a lack of natural resources is not necessarily an obstacle to development (as the cases of Japan and other highly developed European countries show) and that their abundance may even be counterproductive (as the case of many African countries proves), an even more challenging question is why

potentially available resources either remain underutilized, are plainly wasted, or even become instruments of reverse development and tragedies.

Yet the above quotation stresses a subtler problem: it is not necessarily the management of natural resources that fails, but that a more complex issue is involved: the integrated manner in which resources should be managed. This has little to do with natural resources themselves and much to do with individuals and society: the human and intangible sides of the problem. And this is indeed the approach that this book takes, even when chapters deal with the natural aspects of local development. Indeed, local development foresees an integrated approach among and by human beings based on institutions.

Taking an integrated approach to comparative local development is neither simple, nor without danger. The traditional approach of the social sciences to the issue of local development is that there already exists a good approach which starts with the availability and allocation of resources – be they natural, social, human or intangible –, incorporates their good management, and leads to output and benefits for local people. These processes also sustain the long-term local and global value of those resources. This approach should lead scholars to ask and enquire about the compatibility of the different instruments and goals, be this in a technical or social sense, which has much to do with institutions. Many critics of development programs in developing countries, for instance, maintain that the lack of success in integrating development and environmental conservation derives from the impossibility of combining two inherently divergent goals and agendas. This is the position of some members of the environmental movement (including supporters of “de-growth economics”; see Latouche 2009), but also – on the opposite end of the environment-development spectrum - of advocates for developing countries and the governments of poor countries.

A subtler and more convincing criticism of integrated development programs comes from scholars such as Ostrom (1990). In her deep and challenging analysis of the commons, Ostrom (1990) maintained that local constituencies are able to solve issues with the governance and scarcity of natural resources through many and different cooperative and integrated institutions and approaches that lead to the proper management of the environment and development for the community. However important and progressive this view is, it may suggest that if this phenomenon is lacking, or fails, it is because the community does not have the opportunity to create and implement the proper solutions through an evolutionary process. A lack of local development is thus assumed to be due to interventions external to the community or because of internal ruptures. This is true enough, but it overlooks the problem that a lack of development or its disruption may come also from entrenched local interests.

Various cases involving both scenarios are considered in this book: natural disasters (*Pant*), globalization (*Trevisan*), institutional failure and lack of security (*Waisova and Cabada*), child poverty (*Husz and Perpec*), a lack of infrastructure (*Haller and Moller, Horváth*), local democracy and inclusion (*Kukovič et al.*), social and cultural innovation

(*Orbán*), social capital (*Zaric*), together with broad multi-factor overviews (*Kiss and Rácz*) and discussion of the role of governments and governance, regulation of the use of land (*Elliott*), and the role of local governments (*Kiss and Rácz, Kukovič and Haček*) and their local finances (*Tózsza*). Some further important issues are hinted at more than thoroughly analysed in this book that deals primarily with Europe: the demonstration effect and its consequences for consumption and investment in less-developed localities, the growth of inter-personal and inter-regional inequalities, and the priority awarded regional and national financial stability and the consequent limitations that are imposed on social and development policies, particularly within the European Union (EU).<sup>2</sup>

Various types of external intervention that have occurred to the detriment of local development can be identified but these are certainly blurred and borderline cases: e.g. neo-colonialism, and the presumed fight against terrorism and the defense of human rights, including the struggle against child labor in developing countries. In most cases, however, it is usually difficult to hide the negative effects of the latter. However, it is the effect of historical processes, idiosyncratic institutions, resource and investment localization and divergent interests within individual countries and localities that is perhaps of a more serious and resilient nature. Various countries show serious internal divergence, including in the form of increasing inter-regional differences even within coherent areas, thereby activating important instruments for inter-regional convergence such as the European Union (Eurostat 2018), apparently at odds with prevailing trends in an age of converging inter-national differences (Lange *et al.* 2018). The cases of Northern and Southern Italy, Eastern and Western China and Germany, or the more geographically scattered model of the United States and many others are well known and do not require further mention, except to stress that within these broad areas there are further important patterns of development and stagnation of smaller localities. Again, the book offers important contributions that delve deeply – directly or indirectly – into this complex set of external and internal issues: from theory (*Möller*) and measurement (*Dauth*), to infrastructure (*Haller and Möller*), technological progress (*Horváth*), reducing child poverty (*Husz and Perpék*), local democracy (*Kukovič et al.*), the role of universities (*Litzel and Rust*), social and cultural innovation (*Orbán*), but also reconstruction plans after disasters (*Pant*), local finances (*Tózsza*), globalization (*Trevisan*), environmental cooperation (*Waisová and Cabada*), security management (*Waisová and Cabada*), and social capital (*Zaric*).

Interpersonal inequalities often go hand in hand with inter-regional inequalities, in part because the nature and goals of domestic constituencies may conflict with local development goals and because the development of one locality may be counter to the interests of other localities. This conflict may be open; for example, concerning the allocation of resources from common funds. This is the case with EU funds (conflicts over the size of the common EU budget and the share within it of the different chapters; in particular, Common Agricultural Policy and related funds vs. structural funds for the promotion of local convergence) or national funds (transfers to Southern Italian regions in contrast to higher taxes for Northern Italy, or similar processes in Germany after

unification), or public investment in one area but not others. The situation may be less evident when there are social contrasts (e.g. the successful green revolution in poor countries, particularly in India, was to the advantage of certain regions and wealthier farmers and the disadvantage of poorer ones who were left less able to compete than before). Another case is that of Common Agricultural Policy in the EU which has mostly helped large-scale, wealthy farmers in central-northern EU to the disadvantage of other areas, particularly Southern Europe, which has had to compete in more unfavorable conditions (De Grauwe 2014).

## 5 Explaining success and failure in local development

It is wrong to state that local development programs have been unsuccessful or had distorting effects. Many successful cases of intervention exist, and this book offers many such examples, case studies and analyses. Yet a comparative approach to local development should not be limited to the comparison of different cases and issues of local development through a horizontal, cross-sectional approach. There also is a dramatic need for a trans-level approach which incorporates the relationship between local development and national or international development. Can we really promote local development without the more general process of development in a country and at an international level? Sayer and Campbell (2004, 4) maintain that “[m]any attempts to integrate complex sets of knowledge and the interests of diverse sets of actors into a common framework have yielded disappointing results. ... What is surprising is not the improvement of integrative methods over the past 40 years – rather it is their fundamental similarity. The words have changed but the paradigm remains similar”.

This statement is perhaps too strong. Looking at this book, there are chapters whose content goes beyond this criticism in outlining a potentially new paradigm. For instance, *Waisova and Cabada* offer an integrated example that is based not exactly on a new paradigm but which offers an integrated approach to the difficult issues of local development, environmental cooperation, peace-building and security. The two chapters by *Futó* and those by *Gabriel et al.* and by *Haller and Möller* stress the role of education and the presence of a dynamic university as the most important factors in fostering paradigm change. These explanations are clearly in line with the three-helix analysis (Etzkowitz and Klofsten 2005) and the claim for the need for a creative class in a locality (Florida 2002). These chapters offer a hint of the explanatory power of an integrated analytical approach, although they cannot in a clear-cut and unequivocal way specify what the causes are, and what the effects. Does a locality need security to develop, or is development the best guarantee of security? Is education the cause or the effect of local development? Case studies tend to suggest that both are required depending on local circumstances and particular events, and that a circular process of mutually reinforcing – or weakening – events may be in operation.

However, the underlying operational approaches of most local development programs remain doubtful, and side effects and unforeseen consequences abound. It is not only

peaceful areas that run the risk of missing out on international support that is concentrated in conflict-affected areas. It may also be the case that external support, or the prospect of it, may set in motion processes that disrupt the chances of local development. Within unstable localities or states, some social groups or politically powerful people may find it convenient to cause instability or conflict if they are convinced that they will be able to make gains from international help or domestic resources allocated to conflict resolution and local development. The case of selected regions in the south of Italy show that the availability of massive transfers from the central budget to those regions may prompt traditional criminal organizations to reorganize in order to capture valuable rents. Criminal organizations may then invest in rents or parts of them in the regular economy and use violence to avoid competition from clean businesses (Arlacchi 1986). Even well-intended support for local development may reverse development. The situation in the former Yugoslavia (Dallago and Uvalic 1998) and many other localities and countries are examples of this danger. It is important to undertake further research to foster understanding of this kind of danger: namely, to identify the factors and the circumstances that activate such negative processes and define the instruments that can be used to avoid such danger or combat it and reverse its effect.

It is important then to make it clear that local development is not an exclusively one-way process. In reality, it may fail and be reversed. It may even restart again, either due to well-chosen policies or because of "spontaneous", unplanned and unmanaged sets of events that reactivate virtuous processes that lead to local development. The chapter by *Trevisan* presents an important case in point: that of Italian industrial districts. These were one important component of the dynamic economic development and social transformation of Italy until the 1980s, after which the districts started to weaken and fail, apparently because of their inability to adapt properly to globalization. Yet the agony did not end in the death of many districts, nor was it an endless process. Many industrial districts in later years were revived and again became competitive after years of transformation and restructuring. While policies played a role in this happy development, self-help and reorganization played an outstanding role.

This particular case suggests that it may be possible to invert unfavorable and negative trends. It is therefore important to build a theory of the factors and circumstances that may support and strengthen this process and its management. The book offers interesting responses to this need, although not necessarily definitive and generalizable ones. Perhaps the main such answer is that it is important to invest in human beings, since these are the most fundamental resources for local development. This requires starting with children, who must be given proper opportunities (*Husz and Perpék*) and continue on to higher education, where the teaching of local development should be more prominent than it has been so far (*Futó, Gabriel et al.*), and the role of universities should also be elevated (*Litzel and Rust*). It also requires proper roles for infrastructure (*Haller and Möller, Horváth*), land use and the environment (*Eliott, Waisová and Cabada*), local governments (*Kiss and Rácz, Kukovič and Haček*), social and cultural innovation (*Orbán*), the protection of fundamental rights of both businesses and minorities (*Ferrari*,

*Penasa*), security (*Waisová and Cabada*) and democratic consolidation and participation (*Kukovič et al., Zaric*). The analysis of all these issues should be done comparatively whenever possible to assist with understanding and placing individual cases in context. It should also aim at the development of a general systemic theory of local development to place each factor in relation to the others and clarify the overall interaction network in a multi-factor analysis.

## 6 The multidimensional nature of local development

It is not easy to understand precisely what local development is, why it is important, why it is complex, why it is in inadequate supply, and why the comparative approach is really necessary. Often, general (national) and international (globalization) processes are offered as alternatives. Most analyses of local development deal with what is directly or indirectly within its purview: a set of needs (development) promoted and managed – sometimes governed – at the local level (local) by means of resources (natural, human, financial, technological); resources that sometimes come from outside the relevant locality (national, international, other localities). The book offers various contributions to all these different cases.

However, local development also has different dimensions that this book considers extensively. According to these perspectives, local development means pursuing the stability and cooperation of local constituencies. This may require only political agreements and proper institutions, without the use of resources, or may require the use of resources produced locally or elsewhere. Stability may be good in itself or may be a precondition of development and the production of more and better resources. There is also a third level: the implementation of the rights of human beings as a supreme good. This may be, in turn, a precondition of development, as Sen (1999) forcefully stresses, or may require the use of local or external resources.

All these dimensions are better considered in the next section. They are important and require that local development is analysed in a complex, multidimensional way. A common trait is that local development arises from differences within countries and pursues the particular advantages – human, social, economic, financial, national, international, technological, and physical – of localization (Porter 2000). This book reflects these different dimensions of analysis and offers explanations for why local development is important (see *Möller* on theories of local development).

Using an integrated and multidisciplinary approach to the study of local development is fundamental, as stressed above. Yet it is extremely difficult. This approach has produced astonishing results in many fields (in particular, in the natural sciences and technologies). In social sciences it is intrinsically more complex and difficult, therefore also fragile and more complex to manage. This is so for different reasons. The number of variables that social research is required to manage is much higher than in the case of the natural sciences, and the value of such variables is often difficult to assess, being imprecise,



blurred, or plainly concealed. Moreover, social sciences have to deal with the well-known problem of the participating observer, whose observation and implementation of action influence the phenomenon under study through modifying the value of parameters. This is a fundamental difference from the natural sciences that can make use of the ideal conditions of laboratories or observation from an enormous distance. Third, the subjects of local development – and quite often the organizations who promote and support it, and also the scholars who study it – have their own idiosyncratic interests and goals that may be at odds or even conflict with each other. The most evident cases of this in this book are presented by *Waisová and Cabada*, but they can also be found in other chapters. Fourth, the variables at stake and their value may easily change through time due to external influences or interaction among the variables themselves. The chapters by *Haller and Möller*, *Kukovič et al.*, *Litzel and Rust*, *Pant*, *Tózsá*, *Trevisan*, *Waisová and Cabada* offer the most prominent example of such changes in this book.

These problems are particularly serious in the case of local development, since the number of variables is extremely high and distances are much shorter (distance actually being replaced by vicinity) while the role of the observer is more direct. In the present book, the chapter by *Kiss and Rácz* about the factors and policy measures that influence local economic development (a subset of overall local development) enumerates 17 different factors. The number of fundamental variables (those that are the main subject of a chapter) considered in this book is 30! Nevertheless, the importance of an integrated, systemic approach requires that some simplification and generalization occurs through a comparative analysis of local development. The collaborative and coordinated research of experts of different aspects and dimensions of local development around previously well-defined topics, such as this book contains, is one important and effective way to do the latter. The system perspective requires also that local development is seen as a fundamental part of a more complex reality, which includes different levels (national, international) and different fields (economy, society, polity, law, geography, strategy, nature, technology, and many others). This book also offers a vast range of different analytical angles inspired by different disciplines. A proper system view is still lacking, but at this level of knowledge and analysis of local development, pretending to offer one would definitely be premature. Yet it is necessary to work consistently in that direction, while various important elements and inspiration may be obtained from the present book.

## 7 Three critical dimensions

As mentioned above in Section 5, local development moves around three main dimensions, as defined in this book. The common thread of the three perspectives is difference: local development makes sense and is important because there are differences within countries and internationally among different localities. This situation goes well beyond the statement that geography matters, and that resources tend to agglomerate in particular spaces, although this is certainly true and important (Krugman 1995).<sup>3</sup> What is fundamental is that space and distance matter for human activity in different ways, both material and immaterial. The latter span from spillovers and agglomeration economies in economic activity to a sense of belonging, the circulation of ideas, transaction costs, common culture, interpersonal relations, trust, and many more. These aspects stress that local development has its own *raison d'être*, both in its own right and as an organizational principle of more complex societies.

This is the perspective that the European Union takes in building European integration and pursuing convergence within it among different countries and NUTS localities. The main goal of EU regional policy design is to reduce the development gap among NUTS localities and among member countries in order to promote economic, social and territorial cohesion. The communication "Regional policy contributing to sustainable growth in Europe 2020" that the European Commission published in January 2011 encourages EU member countries to increase their expenditure on regional development in terms of education, research and innovation, and to base their future investment on smart specialization strategies. These initiatives are at the basis of the Europe 2020 strategy that calls for partnership among national, regional and local authorities for their implementation. Eurostat defines the local development perspective at the basis for an important part of its statistical activity:

*"Comparing data at a regional or subnational level is often more meaningful and such an analysis may also highlight disparities within countries, such as an east-west divide in Germany or a north-south divide in Italy. Alternatively, such analyses may reveal differences in patterns of economic development, for example, Germany and Poland have polycentric patterns of development with several relatively large cities spread across their territory, whereas France and the United Kingdom are examples of a more monocentric pattern of development, as their economic activity is more concentrated in and around the capital cities of Paris and London" (Eurostat 2018, 8).*

A proper way to organize the analysis of local development, and a way that reflects the approach of this book, is to look at the fundamental dimensions that local development has. There are three such fundamental dimensions, which should not be seen as alternatives. They coexist in many cases and often support each other, although trade-offs also occur. An important way to follow an integrated and systemic approach to local

development is to keep all these dimensions under due consideration. While most papers deal with different perspectives and some of them cut across all the three dimensions (e.g. *Kiss and Rácz* on factors and policy measures influencing local economic development), they can be organized along the three different dimensions that differences in inter-locality assume, all based on institutions of a different type and nature. Taken together, as in this book, they may represent an important step in the direction of an integrated systemic approach to local development.

A first such dimension is that of *efficiency*. In this perspective, local development aims at managing differences in order to pursue competitiveness, innovation, higher incomes and wealth, more jobs, and more well-being. This requires the better allocation and use of resources, use of productive factors (economies of agglomeration, scale economies, scope economies), and better knowledge for creating higher (individual and social) economic and social returns. Since activities leading to efficiency are socially embedded (Granovetter 1985) and based on individual engagement and effort, both the dimensions of stability and rights are important for enacting the efficiency dimension. Various papers in this book take mainly, although not exclusively this perspective. These include the chapters by *Kiss and Rácz* on the role of local governments in the development of the local economy, those of *Gabriel et al.*, *Dauth*, the two chapters by *Futó, Haller and Möller*, the two chapters by *Horváth, Litzel and Rust, Möller, Tózsá, and Trevisan*.

A second dimension is that of *stability*. Here, local development is considered fundamental to managing potentially disruptive differences in levels of complexity and leading the former to a situation that promises long-term sustainability through shared settlement. When assuming this perspective, various important issues come to the forefront, such as sustainability, governance, opportunities, and social capital. Local development aims at attenuating contrasts and conflicts, granting rights and equal treatment (democracy), favoring the cohabitation of differences and thus also reducing the cost and difficulty of managing them. This dimension requires resources that are produced through the previous dimension of efficiency or imported from elsewhere through economic or political channels, and benefits significantly from the third dimension of rights in identifying and implementing solutions. However, resources are not produced in this dimension, but are used to make social and political returns and to create a stronger basis for prosperity. As a matter of fact, this dimension deals with the preconditions and forms of local development and with the components of it that improve quality of life, individual wellbeing and social interaction. A question typically treated in this dimension is whether local development is a precondition of stability or whether it is a consequence. An alternative interpretation is obviously that it involves a circular causation process in which both local development and stability are both cause and effect. Various papers in this book take mainly this perspective, including the two papers by *Elliott, Husz and Perpék, Kukovič and Haček, Kukovič et al., Orbán, Pant*, the two papers by *Waisová and Cabada* and the paper by *Zaric*.

A third dimension is that of *rights*. People and social groups, in particular minorities, differ in terms of situations, preconditions, equity, opportunities, psychology, motivations and preferences. These differences may be seen as an asset or as a problem. Their role can equally be one of strengthening or of weakening local development, depending on the attitude of people and groups, the prevailing institutions, and the attitude of governments. Rights are a fact: they are either respected or not. But they also involve processes supportive or hindering of their respect and their transformation into different- or different-level rights. Respecting rights does not necessarily require the use of resources (although their repression may require a great deal of resources), but better institutions, democracy and a specific state of mind. When these factors are properly fixed, rights may offer excellent conditions for upgrading efficiency and guaranteeing stability and are at the core of local development, meant in a broader individual, collective and social sense. For example, minorities may represent a problem and a cost when they are repressed or clash with governments or majorities. However, when their rights are recognized and properly integrated they may create opportunities for the development of the entire locality and the country. This happens through tourism, ethnic entrepreneurship, or through the political and economic relations of the former with other countries. Various papers in this book broadly follow this perspective, including the papers by *Ferrari, Penasa, Husz and Perpék*, but many other papers include this dimension in a direct or indirect way.

## 8 Vertical and horizontal relations in local development

If properly managed, local governance should guarantee a resilient basis that promotes local development, helps to advance it and, if it runs out of steam, to consolidate and relaunch it. What is still missing, and what research should contribute to, is understanding and building a general systemic theory of what may increase the resilience of local development, what may weaken successful processes of local development, both internally and externally, and what may put the process in motion again.

Traditionally, there are also perhaps the most challenging questions that theories, analyses and case studies of local development seldom dare to raise, but which have come increasingly to the forefront in recent years: what should highly developed localities and countries, their enterprises and governments, and international organizations change in their stance and behavior to foster and consolidate local development elsewhere? Should external support take the initiative directly or should it rather contribute to fostering a context more conducive to local development through locally governed and owned action? International political and economic relations, and also inter-regional and regional-national relations, are often depicted as zero-sum games. According to this perspective, any case of successful local development increases international competition and supposes that the newcomer obtains its proper place in the international or national arena at the expense of older development localities. If this is the case, it would make sense for the latter to help the most desperate cases (e.g. to avoid unwanted inflows of

refugees, or to soften the worst consequences of military intervention and stabilize friendly countries, but not to cooperate with potential competitors).

If the game is a positive sum one, as it generally is, this approach is myopic. Not contributing to the dynamic and resilient development of others prevents the global arena from becoming wealthier and more stable, and rights more diffused and guaranteed. This deprives developed localities and countries from the opportunity of sharing these advantages. The best way of playing a positive sum game is to open up developed localities' and countries' economies and societies to deeper interaction through trade, cooperation and alliances among equal partners. Obviously, this approach strengthens competition and disadvantages some developed localities or their internal components. These constituencies being less competitive or rent-seekers, it should be in the interest of the developed localities and states to reallocate resources to better uses and compensate the losers with part of the gains. Unfortunately, these kinds of engagements are rarely credible *ex ante*. Moreover, losers and coalitions of would-be losers may be quite powerful and take revenge in various ways, including through the electoral process, as various cases in Europe and North America give witness. Thus providing external, one-way help for less developed and problematic localities is ultimately easier, even if it may be less effective at contributing to their development.

Along with "vertical" processes between the developed and the less developed, horizontal processes also need scrutiny. An excellent topic for further research in comparative local development would be the careful mapping of the relation between one locality and the others in the same country and abroad. This should be done from the perspective of positive-sum interactions in order to understand the approaches and factors that can be activated to build and strengthen coalitions that want to pursue the advantages of a positive-sum game, including how to compensate credibly the potential losers. Here, a suggestion by Sayer and Campbell (2004) may be useful, albeit indirectly. Organizing multidisciplinary teams to tackle a problem as complex as local development seems sensible and easy enough, but meets with barriers of different kind that often mean that such attempts result in failure. Yet this is not always the case, as proved by the successful collaboration of large teams of diverse scientists in space research, computer technology development, and the study of life-threatening diseases. These are typically scientific endeavors with vast and rewarding commercial applications.

## **9 Further challenges and research perspectives**

Unfortunately, as seen in the previous section, most of the cases relevant to the social sciences may be different and much more complex than those of the other sciences, in particular in the case of local development. Even the apparently closed field of study of small- and medium-sized enterprises (SMEs) in local development hardly attracts multidisciplinary approaches and a sufficient amount of dedicated and focused resources, and lacks efforts to make a difference and overcome the danger of failure. Moreover, the cost of failure in this latter case is borne not by scientists and governments, but by the

lack of opportunities for potentially entrepreneurial people, their employees, stakeholders, and taxpayers. In broader projects of local development and in fields of poverty, destitution, and conflict, the greater cost is borne by the poor, the destitute, the socially weak, and the threatened. But these are weak constituencies who can hardly mobilize alternative resources and, even less, political support, except perhaps through the unlikely threat of armed conflict. On the other hand, such efforts offer good opportunities for specialists to obtain substantial rewards by working on such projects, as the share of transaction costs in the budgets of projects fostering local development and support testify.

It seems that projects and initiatives for local development have an in-built weakness: a lack of focused interest and potentially conflicting interests among those involved, constituting an interesting case of the failure of collective action. Research is needed to better understand how to streamline interests and focus interests and action on relatively simple goals with achievable returns. Much of the effort that goes towards fostering local development has a public, or at least collective, nature and this may weaken the interest and effort of individual participants, and increase uncertainty concerning the direction and consequences of such efforts and the allocation of costs and gains. The governance of these projects and this action is of the utmost importance, and comparative analysis and comparative case studies may provide an extremely useful instrument for this purpose. This book offers hints in this regard, such as in the study by *Horvath* of travel and tourism, or *Orbán's* analysis of social and cultural innovations.

A third important issue that needs work is identifying a comprehensive indicator or set of indicators that permit the assessment of progress in local development, the evaluation of its internal and external sustainability over time, and the appearance of problems and threats. In recent work based on a previous study, *Lange et al.* (2018) further elaborated an interesting approach to the analysis and future of development. While the World Bank study looked mainly at countries, it also provided important suggestions that comparative analysts of local development could and should appropriate and utilize. The study investigated development through the comprehensive measure of wealth to monitor sustainable development in a country. The measure of wealth is treated as an indicator complementary to gross domestic product (GDP), which measures only current income. The study considers that development involves managing a broad portfolio of assets, including produced, human, and natural capital. Such consideration of comprehensive national wealth signals if GDP growth can be sustained over the long run.

One interesting finding of the World Bank study, which should be carefully considered in comparative local development research, is that more than two dozen low-income countries are now classified as having middle-income status. These are countries where wealth is mainly comprised of natural capital – in contrast to high-income countries, in which human capital accounts for 70% of wealth – and that have succeeded in upgrading development in part by investing resource rents into infrastructure and education and health; i.e., by investing in human capital. Wealth accounts also indicate areas of concern

in those low-income countries – especially in Sub-Saharan Africa – where rapid population growth has outpaced investment, thus decreasing per capita wealth, and in 12 other countries in which the percentage of people living in extreme poverty has jumped over the last decade. These cases demonstrate that rapid investment in infrastructure and education and sustainable long-term management of the natural asset base are necessary for materializing the potential advantages of population growth. Moreover, out of the 13 fragile and conflict states that have remained low-income since 1995, a majority are resource-rich but have failed to use resource rents to build better institutions and invest in people. This is an observation that highlights the link between poverty, fragility, and governance.

These conclusions strengthen the various findings of the present book. They also offer a useful approach to the analysis of local economic development and provide hints for other social scientists. While it is true that the existence of a national government for implementing policies, re-allocating resources and transferring income may be to the advantage of local development, it is equally true that a lack of borders and the barriers that go with them may make the outcome of market and ungoverned processes more extreme.

## 10 Conclusions

This book offers an up-to-date perspective based on an open, multidimensional view of local development. It also provides evidence of and support for the well-established perspective of the varieties of local development. The latter has important merits, particularly considering that this was not always so. Indeed, local development has had dissimilar meanings in the past and policy suggestions and implementation were different. These separate approaches were sometimes successful and even contributed to the overall development of countries. Consider, for example, two cases described in this book: Italian industrial districts in the post-war period, and the successful recovery of the central Nepalese region from an earthquake. Being largely based on local resources, these examples show that a closed type of local development may be successful.

These successful cases refer to a time that was different to the present: the general context was dissimilar, problems were distinctive, and policy-making was different. Yet the case of the development of Italian industrial districts also proves the advantages and threats of international integration in the frame of globalization. The political and institutional foundation for globalization was laid by the allied powers in Bretton Woods in 1944 and further developed in subsequent decades. While this involved fundamental institutional changes at a global level, other processes took place at a regional, inter-country level, based on, and further strengthening, the process of globalization. First among these was the process of European unification and the accompanying processes of administrative decentralization.

Globalization has directly affected states, but reflects inevitably on localities, for both external and internal reasons. Externally, globalization has strengthened the pressure to compete and create common social and political standards. This has required that countries activate all their internal resources: the promotion of local development and opening up localities to interaction with the rest of the country were important instruments for reasons ranging from economic and political convenience to the build-up of national and international infrastructure, to defense, and law and order.

To appreciate the opportunities and threats of globalization, it is important to distinguish between mobile and immobile resources. The former include people, but also finance and ideas. The latter include real estate, agricultural land and areas of natural beauty and resources. In a globalized world, mobile resources can come and go and any locality wanting to flourish has to retain its mobile resources and attract others from outside by respecting and nurturing the three dimensions of local development – efficiency, stability, and rights – to make the locality attractive. Immobile resources are stable and may create a patient, resilient basis upon which to build a strategy of local development. However, their economic and social meaning and their natural value depend on local ability to preserve, cultivate and upgrade them, thereby influencing the chances of sustainable local development.

In a classic example, when a road or railroad is built across a locality, external people have an opportunity to reach that locality as tourists, businessmen, workers, or in other roles. Local people in turn may find the opportunity to visit the world, serve in the national army, or look elsewhere for better paid jobs or opportunities. Consumers may start to choose between locally produced goods and imported goods, while owners of capital have the opportunity to invest outside the locality, and so on. Yet others may find a threat in this in the form of the destruction of traditional jobs, depleted environmental assets and pollution, etc. In short, the locality has now to pay attention to being as attractive as the surrounding localities, including for its own inhabitants. At the same time, it has the opportunity to benefit from a broader spectrum of opportunities. This new situation drives the need for different approaches to and instruments of policy-making. The more the situation evolves, the more policy-making has to change to be effective. International organizations such as the OECD and the World Bank have often stressed this principle in their publications.

Different important messages emerge from this book. The most important one is perhaps that globalization offers important opportunities for pursuing efficiency, stability, and rights. The book also offers a diversity of precious analyses and case studies of important issues and situations. The main objective is to provide a detailed and sound basis for what is increasingly recognized as the main driver of local development: education.



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**Notes:**

<sup>1</sup> It is important to stress that an important and burgeoning literature exists about the role of knowledge in economic and social activities and its relation to local development, usually linked to entrepreneurship and innovation (Asheim and Parrilli 2012; Camagni and Capello 2009).

<sup>2</sup> On the role of policies for local development, see Viesti (2002).

<sup>3</sup> Krugman (1995, 48) appropriately observes that “the supply of factors to any one region or locality will typically be very elastic, because they can come from someplace else”. However, one should note that agglomeration also involves more complex and subtle aspects of a different nature that find proper representation in this book.

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