Module I

The relevance of LED today

by

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1. Aims of the module

This module aims to establish why Local Economic Development (LED) has become a necessary, viable, and complementary alternative to traditional development strategies in a globalized world. It argues that, in a world increasingly dominated by flows and economic integration, LED provides the adequate framework both to maximize the socio-economic potential of every territory – regardless of whether rich or poor, developed or underdeveloped, urban or rural, central or remote – and to minimize the risks associated with engaging in development strategies, while generating decent and sustainable employment.

This module specifically aims at:

a) emphasizing how globalization is changing the context in which traditional development strategies are implemented;
b) showing how traditional development policies are becoming less effective in this context;
c) highlighting the potential of Local Economic Development (LED) strategies in a changing world.

2. Structure of the module

In order to achieve these goals, this first Module of this ILO *Sensitizing Package on Local Economic Development* is divided into the following sections:

a) **Globalization:** An overview of how the processes of greater socio-economic integration across the world are affecting the distribution of economic activity and reshaping territorial structures.
b) **The emergence of a new territorial structure:** A look at how globalisation is altering existing territorial links and leading to the formation of a more heterogeneous and complex socio-political and economic landscape.
c) **Problems for traditional development strategies:** A presentation of how recent economic and socio-political changes are rendering traditional development strategies increasingly inadequate for tackling development problems.
d) **LED as a viable alternative:** A brief sketch of how LED strategies can help overcome the development problems of territories around the world. These aspects will be more fully developed in successive modules.

3. Globalization and the reshaping of territorial structures

Globalization is a term generally used in order to describe a series of relatively recent processes that have resulted in a much greater mobility of capital, goods, labour, and, to a lesser extent, services across the world and which are contributing to change the rules that govern the world economy. These processes – triggered by momentous advances in technology and access to information, as well as by changes in the way the world and national economies are regulated (Dicken 2003) – are affecting every country, region, and locality and thoroughly reshaping territorial structures.

Globalization affects virtually every aspect of socio-economic interaction, but its impact is particularly evident in the four areas that will be covered in this section, namely:

a) Trade and changes in its composition;
b) Urbanization;
c) Decentralization;
d) The rise of inequalities.

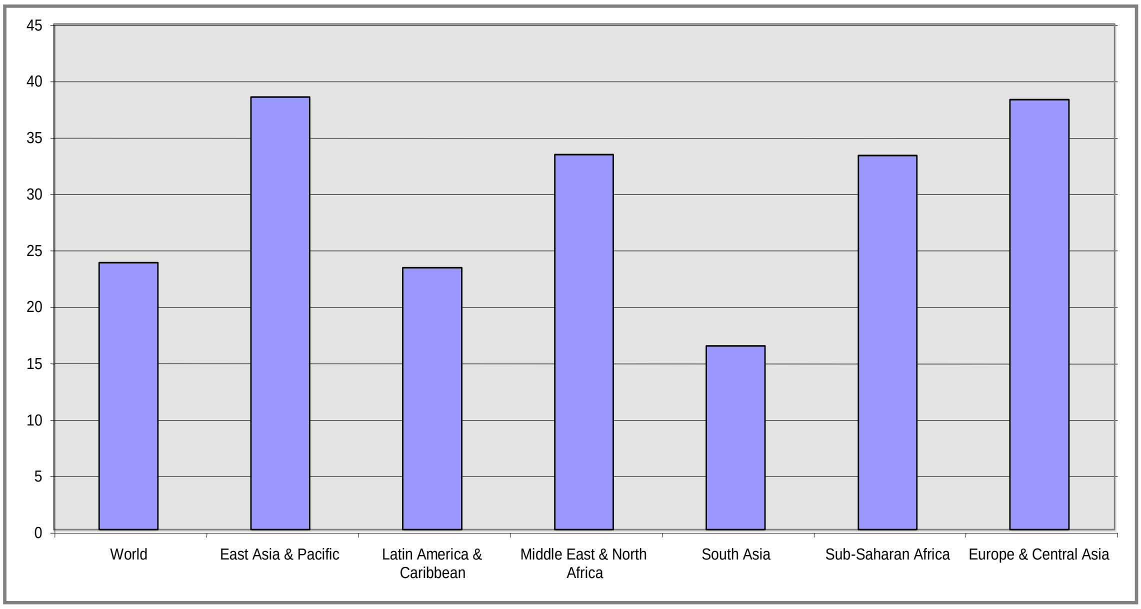
3.1. Trade and changes in the composition of trade.

The last three decades have been characterized by a dramatic increase in trade, as well as in foreign direct investment (FDI) flows. Since 1970 world trade has been multiplied by a factor of ten in real terms and, as a percentage of GDP, the percentage of traded output has risen from a mere 27% of global GDP to more than 60%.

The pace of growth in trade has not been uniform. The greatest advances have taken place since the beginning of the 1990s, associated with the increasing incorporation of countries in the developing world to global flows.

Although most trade and foreign direct investment still takes place among developed nations, the trend is increasingly affecting all parts of the world. Figure 1 shows trade as a % of GDP in 2002 across different supra-regional areas of the world.

Figure 1 Trade as a percentage of GDP in different areas of the world, 2002.

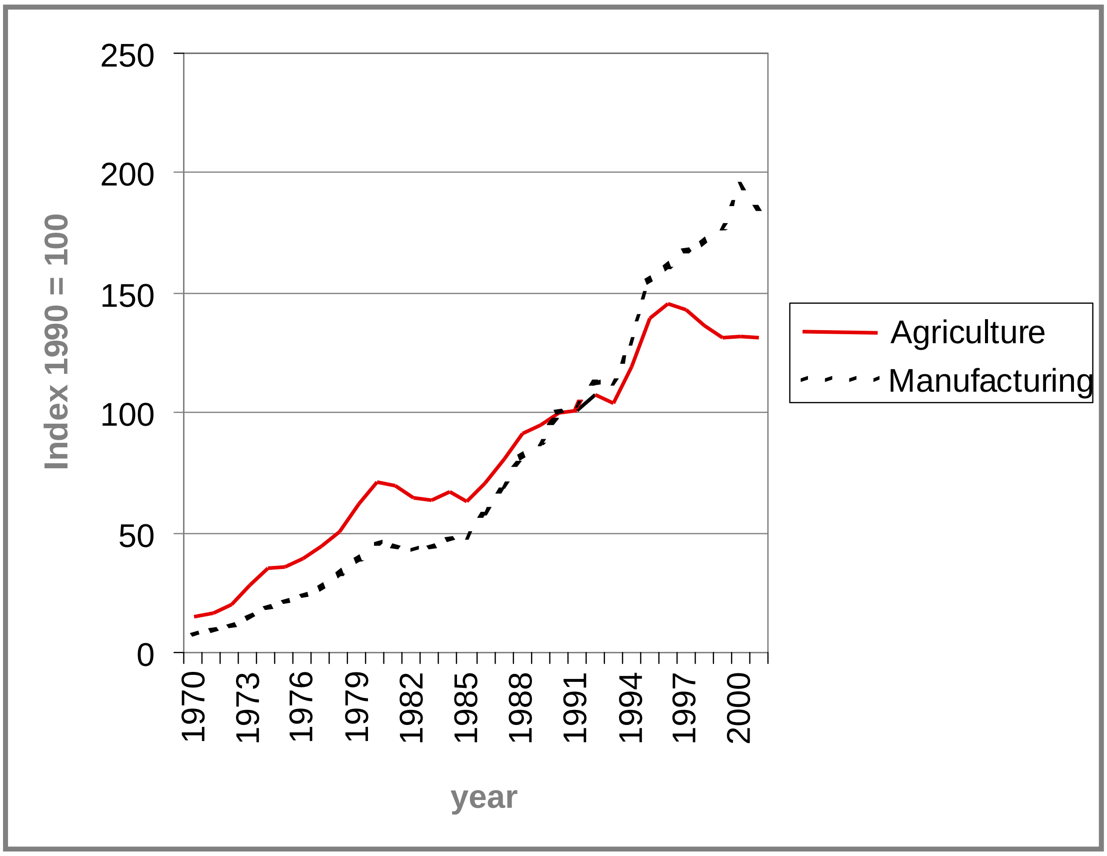


Source: Own elaboration with World Bank data.

Figure 1 highlights that, relative to their GDP, trade has become almost as relevant for the Middle East and North Africa or Sub-Saharan Africa, as it is for East Asia and the Pacific or Europe and Central Asia. Latin America and the Caribbean have levels of trade similar to the world average and only South Asia seems to be lagging behind (Figure 1). Sub-Saharan Africa, the Middle East and North Africa, and South Asia have also experienced rapid increases in trade volumes, especially since the second half of the 1990s.

Recent years have not only been characterized by a swift increase in the volume of trade, but also by a major change in its composition. Trade in agricultural goods and raw materials has seen its importance progressively eroded by trade in manufacturing. Figure 2 shows the evolution of world trade in agricultural goods and raw materials – referred to under the term 'agriculture' – and in manufacturing since 1970.

Figure 2 Evolution of trade in agriculture and manufacturing since 1970.

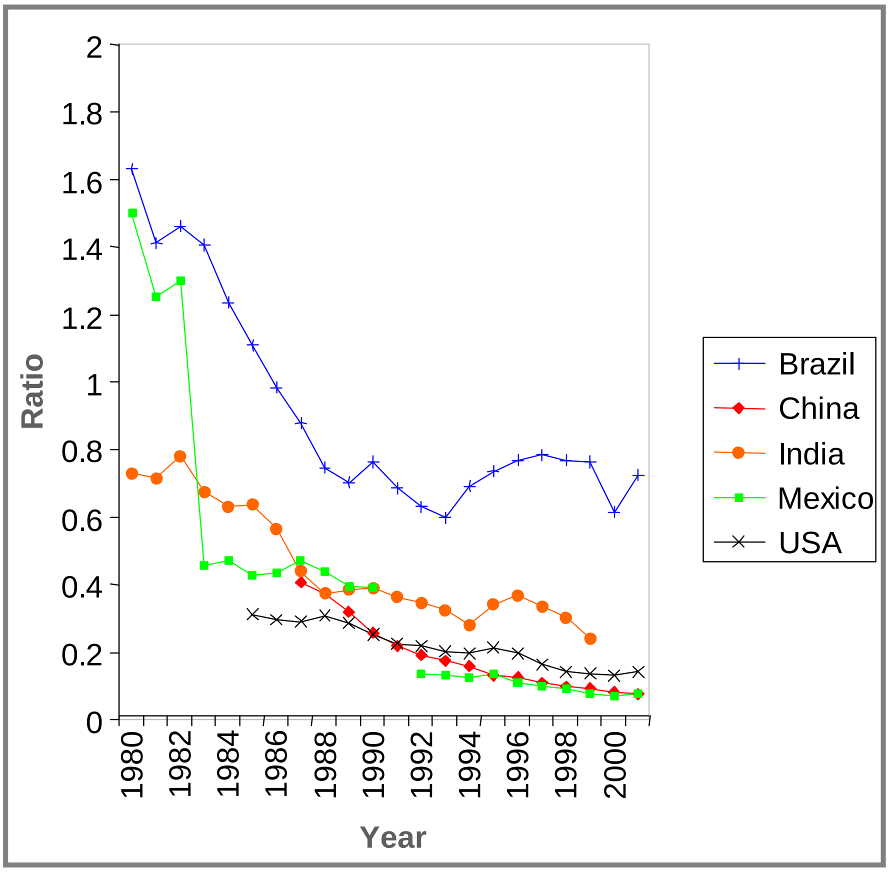


Source: World Trade Organization, 2001

The figure indicates that, although trade in both agricultural and manufacturing goods has been expanding rapidly over the last decades, trade in agriculture has struggled to keep up with manufacturing trade since 1990. The important structural barriers remaining in agricultural markets, coupled with often rapid and wild fluctuations in the price of agricultural produce and raw materials, have played an important role in these developments.

The sectoral shift in trade is, once again, prevalent across most countries and regions in the world. Figure 3 depicts the balance of agricultural to industry export ratios in five selected countries. The most important feature extracted from Figure 3 is the declining importance of agriculture, relative to industrial goods, in the trade composition of the selected countries. Countries such as India or especially Mexico, which, as recently as 1980, relied heavily on the export of agricultural products and raw materials, are now dependent on the manufacturing sector for the bulk of their exports. Even countries where this transition has been less radical, such as Brazil, increasingly rely on manufacturing, rather than the primary sector, as their main source of trade (Figure 3). The trends in these countries are largely replicated in many other middle- and low-income countries.

Figure 3 Shift in the composition of trade in selected countries.



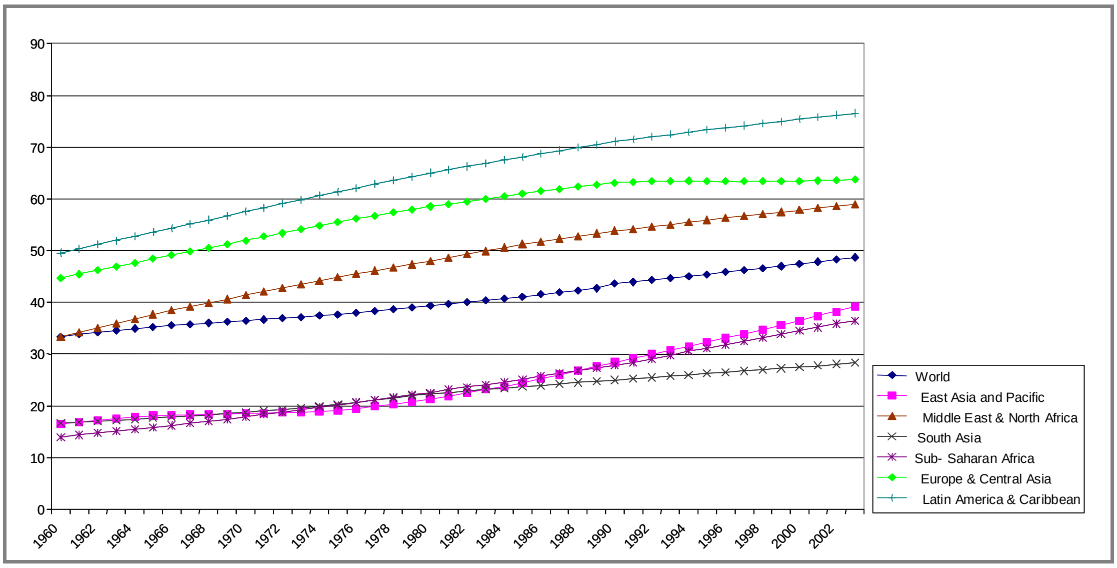
Source: Own elaboration from Comtrade, United Nations Statistics Division data

Two important points can be derived from the above discussion. First is that the rapid increase in trade since 1970 has been almost universal, affecting virtually every space across the world. Second, the rise in trade has been accompanied by a sectoral shift whereby countries are increasingly becoming more and more dependant on trade in manufacturing goods, to the detriment of agricultural goods and raw materials, which were the main components of trade in many countries until relatively recently.

3.2. Urbanization

As prevalent as the rise in trade has been the rise of cities. Cities across the world have been thriving, with the fastest urban growth in recent years taking place in low- and middle-income countries. Now-a-days almost 50% of the world's population lives in cities. The size of the urban population ranges from below 30% of the total in South Asia to close to 80% in Latin America and the Caribbean (Figure 4).

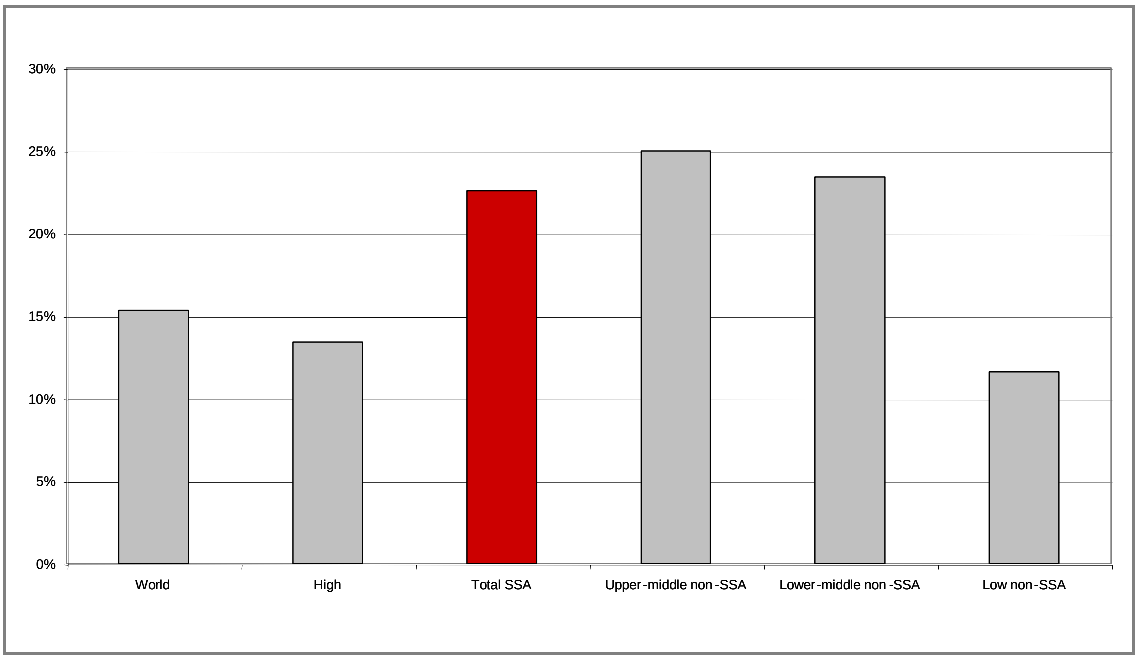
Figure 4 Urbanization trends across different parts of the world.



Source: from World Development Indicators (World Bank 2005)

The pace of urbanization varies significantly across regions of the world. It was slowest in the heavily urbanized Europe and Central Asia region and fastest in East Asia and the Pacific and in Sub-Saharan Africa.

Figure 5 Increase urban population as % of total population from 1960 to 2003



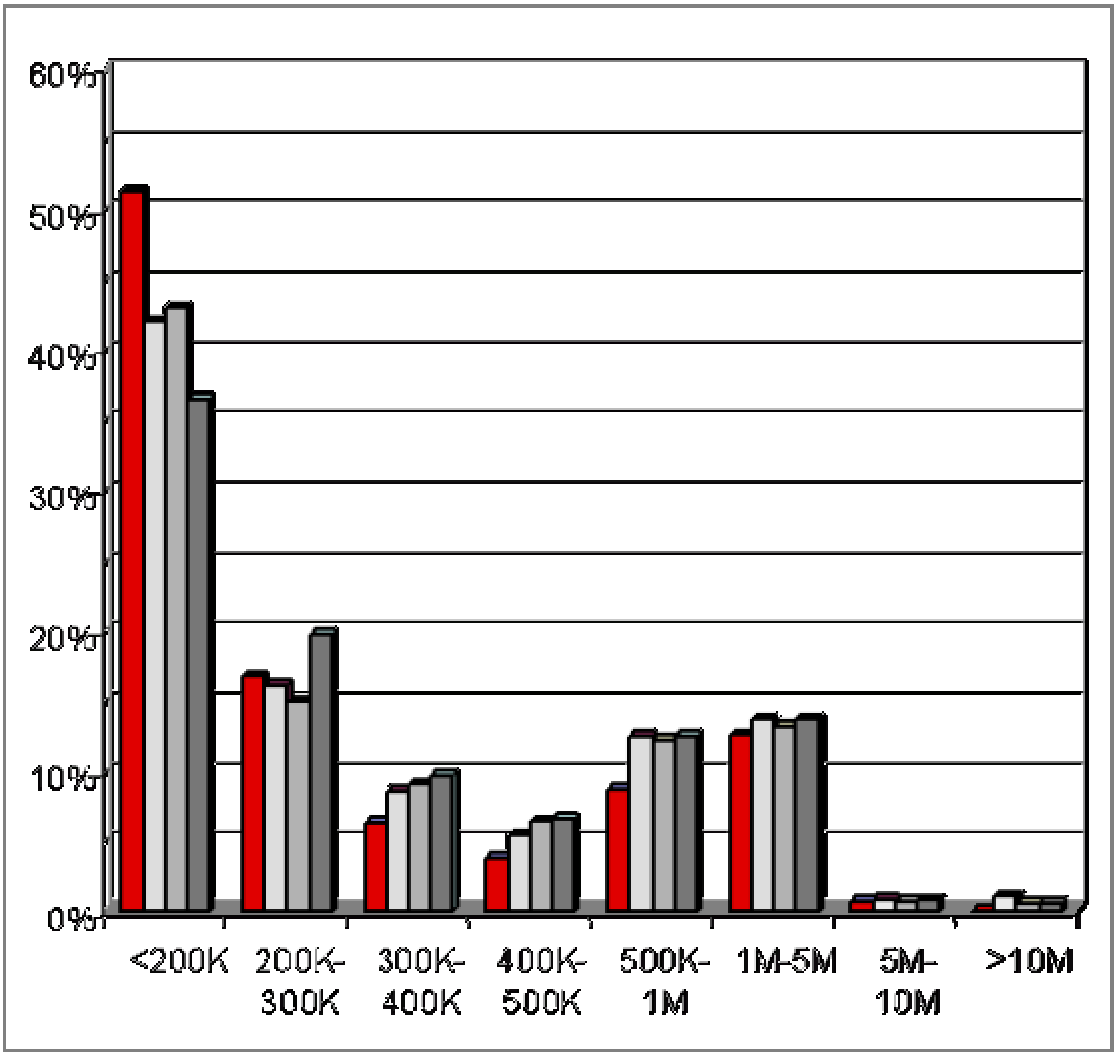
Source: World Bank World development Indicators (World Bank 2005)

Much of the growing urban population has been concentrated in large agglomerations – often, but not always, coinciding with the capitals of states – that, in many cases, have become true megalopoli. This phenomenon, known in the literature as the rise of the primate city (Henderson, 2003) is prevalent throughout the world, although more evident in upper-middle income countries. Many low-income countries, especially in Sub-Saharan Africa, have nevertheless witnessed a rapid concentration of population in their largest cities, often at the expense of rural areas and even intermediate cities.

If we take Sub-Saharan Africa as an example, the rapid pace of urbanization in the region as a whole hides important internal differences; countries such as Rwanda, with an urban population of 6 per cent of the total, are still barely urbanized, while in other African countries, like for instance Gabon, the proportion of the population living in cities exceeds 80 per cent. Variations in the speed of urbanization are also noticeable; while the urban population of Gabon has increased by 64 points since 1960 or that of Nigeria by 30 points, the urban share of Rwanda or Ethiopia, have only increased by 4 and 9 points respectively (World Bank World Development Indicators 2005).

In some Sub-Saharan African countries, urbanization has lead to the emergence large megalopolis, which, in the cases of Abidjan, Kano, Cape Town, the Witwatersrand, Kinshasa, and, above all, Lagos, exceed the 3 million people mark. The lure of the big city is, however, not homogenous across the Continent and as Figure 6 shows, the majority of the urban population lives in relatively small cities.

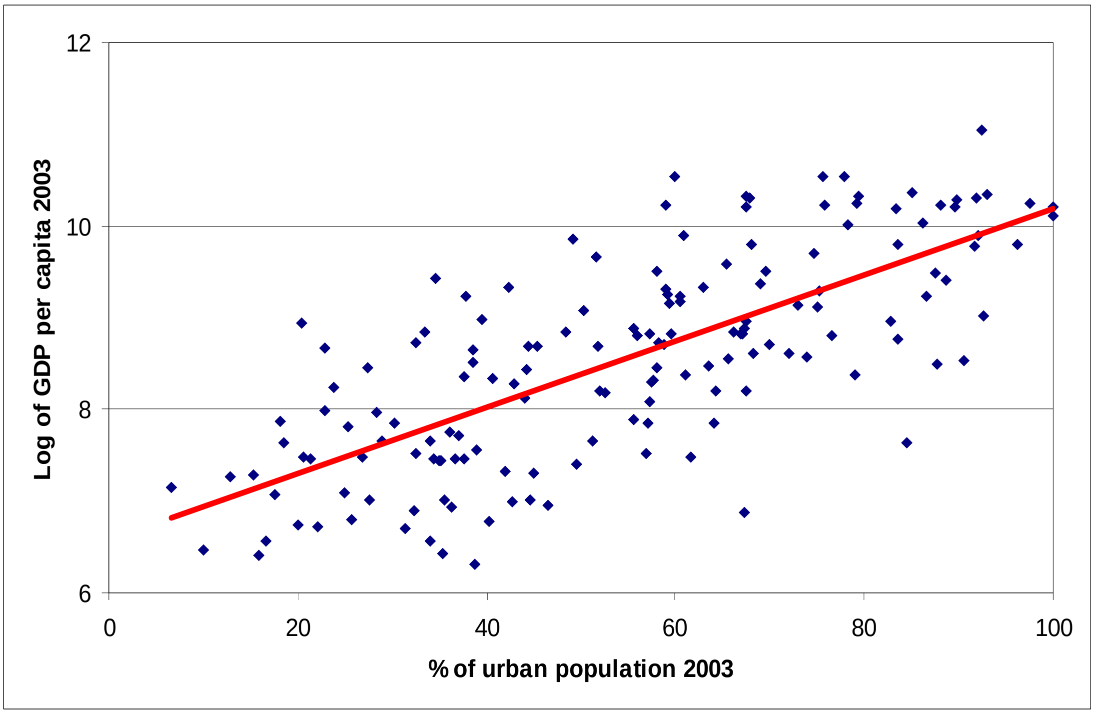
Figure 6 Urban population by settlement size in Sub-Saharan Africa (2000)



Source: Kessides (2005)

In many areas of the world, the process of urbanization has also been associated with an increase in wealth. The emergence of cities as centres of economic activity and trade, with their diversity, their agglomeration of firms, and their relatively more skilled individuals is regarded as a guarantee of greater economic dynamism (Duranton and Puga, 2000; Henderson and Wang 2005; Venables, 2005). From this perspective, the trend seems to be the higher the percentage of urban population, the higher the GDP of a country (Figure 7). In Sub-Saharan Africa, however, this link is less strong. The region has been urbanizing at a pace that greatly exceeds the relatively sluggish economic growth of recent decades (Kajumulo Tibaijuka 2004).

Figure 7 The global link between urbanization and wealth



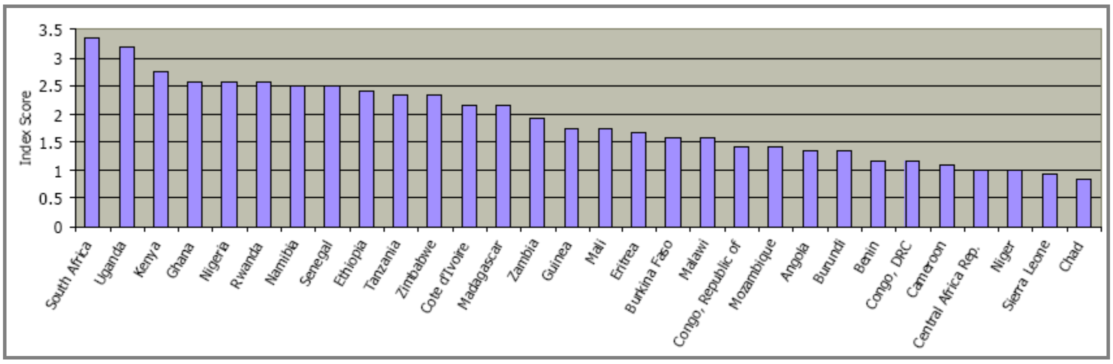
Source: Own elaboration World Bank data

3.3. Decentralization

The move towards decentralization, or the transfer of power and resources to subnational tiers of government, has also been evident since the 1970s across the developed and the developing worlds. A study by the World Bank in the early 1990s already indicated that sixty-three out of seventy-five developing-world countries with a population in excess of five million were actively pursuing decentralization policies (World Bank, 1992). Since then, the trend towards regional devolution and decentralization has accelerated in many parts of the world. The decentralization drive has been most pronounced in Europe and Latin America. Changes across Asia – and especially in countries such as China, India, Indonesia, Korea, and the Philippines – have also been noticeable.

In Sub-Saharan Africa the process has overall been more modest, but again great variation exists. A recent study (Ndegwa, 2002) shows that all Sub-Saharan African countries show some degree of decentralization and far-reaching decentralization has taken place in some of them. Figure 8 shows the decentralization index for selected Sub-Saharan African countries. A value of zero represents no decentralization while a value of 4 would depict complete decentralization.

Figure 8 Decentralization in selected Sub-Saharan African countries



Source: (Ndegwa 2002: 12)

The process of decentralization – which has been paralleled in many part of the world by a greater protagonism of international organisations and donors – also represents a shift in the scale for development strategies. With their increasing powers and resources, sub-national actors are becoming more and more prominent in the design and implementation of development policies, often to the detriment of the nation-state. In any case, the decentralization of powers is not always accompanied by a similar decentralization of resources, leading often to the emergence of subnational governments that are power rich, but resource poor.

3.4. The rise of inequalities

The fourth phenomenon associated with the process of globalization has been the rise in inter-personal and inter-territorial inequalities. Although the evolution of inequalities across the world is still the subject of heated debates, there is increasing consensus that both inter-personal (Wade, 2004) and inter-territorial inequalities (Rodríguez-Pose and Gill, 2004) are on the rise. The dimension and evolution of inequalities, however, tend to differ between the developed and the developing worlds.

The dimension of inter-personal inequalities and regional disparities within countries is, in general, considerably larger across most of the developing world (Table 1). Inter-personal and territorial inequities tend to be more subdued – although still important – in developed countries. Inequalities have also been rising faster in low- and middle-income countries than in wealthier countries, as shown by the selected countries in Table 1. Finally, the timing of the rise in territorial inequalities seems to coincide with the opening of countries to trade.

Unfortunately it is not possible to assess if a similar trend is occurring in the Sub-Saharan African region, due to a lack of data at the regional level. What little reliable data are available for the Continent generally concern South Africa and give support to the idea that regional GDP per capita in large city-regions and in urban areas as a whole has been increasing faster that in the rest of the country (Naudé and Krugell, 2003). As is the case in other parts of the world, access to markets, proximity to ports, and stock of human capital are seen to be the key factors behind this rise in urban income (Naudé and Krugell, 2003).

Other South-Saharan African countries seem to show the opposite trend, with rural versus urban poverty rates suggesting a trend towards greater equalization of incomes (Kakwani 1993; Grootaert, Demery et al. 1996; Canagarajah and Mazumdar 1997; de Haan, Lipton et al. 1997). A possible explanation for this trend is that the rapid process of urbanization has been accompanied by greater inequality within urban settlements in many countries. In part the reduction of the gap between urban and rural areas can also be attributed to the dominance of structural adjustments, which forced governments to modify the structures of outlays, prices, and institutions which created a so-called urban bias in previous decades.

Table 1 Changes in regional disparities in selected countries (1980-2000)

	Year			% Change		
	1980	1990	2000	1980-90	1990-00	1980-00
Developing Countries						
China	0.578	0.483	0.581	-16.31	20.20	0.60
India	0.352	0.377	0.441	7.10	16.98	25.28
Mexico	0.388	0.383	0.435	-1.29	13.58	12.11
Brazil	0.588	0.488	0.494	-17.01	1.23	-15.99
Developed Countries						
US	0.136	0.152	0.148	11.76	-2.63	8.82
Germany	0.184	0.188	0.186	2.17	-1.06	1.09
Italy	0.265	0.269	0.277	1.51	2.97	4.53
Spain	0.207	0.199	0.222	-3.86	11.56	7.25
France	0.151	0.164	0.163	8.67	-0.29	8.36
Greece	0.156	0.158	0.158	1.21	0.16	1.37

Source: updated from Rodríguez-Pose and Gill (2004)

In addition to the transformations stated above, the process of globalization has generally been associated with a rise of the informal economy, a weak sectoral integration, and a reliance by many households on multiple sources of livelihood to survive. And all this frequently taking place in conditions of insufficient government and fiscal capacity and weak civil society and governance structures.

4. The emergence of a new territorial structure

The combination of the processes that constitute globalization are leaving an important territorial imprint with which many nation-states are struggling to cope. This new, more heterogeneous and fragmented territorial structure is characterized by the emergence of three types of spaces with very different development needs and often within the same national framework.

The key spaces in this three-tier structure are:

a) **Primate cities:** Large urban agglomerations that have not only managed to attract massive rural-urban migration, but also a greater concentration of economic activity. This is mainly because of their greater accessibility, their larger economies of scale, scope, and agglomeration, their greater presence of skilled labour and markets, and, their better capacity to compete in open markets. These growing urban conurbations – in many cases becoming true megalopoli – attract large numbers of rural and small-town workers seeking to improve their personal conditions. However, the other side of the coin in these cities are serious problems of poverty and social exclusion, as well as violence and the rise of large slums.

b) **Intermediate city-regions:** Medium-sized cities, outside the direct area of influence of the primate city, that often articulate large rural hinterlands. These cities are generally growing (especially in the developing world) and attracting population from rural areas. But, given their size and frequent endowment deficiencies, they frequently struggle to find market niches and become competitive. In the developing world, many of these intermediate city regions are often becoming increasingly dependent on international aid.

c) **Rural areas:** Generally remote, with poor accessibility, and with weaker endowments in human resources and firms, the problems of rural areas differ significantly from those of urban areas. Across the developing world, many of the problems of rural areas are exacerbated by global restrictions to trade in agriculture and by the greater volatility in the price of agricultural produce and raw materials

5. Problems for traditional development strategies

This more heterogeneous and complex territorial structure has undermined the ability of the nation-state to manage national economies, increasingly rendering traditional top-down, supply-side development policies, which are often based on the promotion of industrial sectors or on improving accessibility, less and less efficient.

Traditional development policies have normally been cut from the same cloth in different parts of the world. These were normally supply-side strategies, based on a sectoral rather than a territorial dimension. Decision-making was mainly top-down, with mixed or bottom-up approaches virtually ignored and with a tendency to rely on financial support, incentives, and subsidies as key elements of the strategy. Frequently, these policies relied on the imitation of successful development strategies applied in very different contexts (Storper, 1997).

Most strategies were based on two axes:

a) **Development of infrastructure:** Infrastructure has frequently been perceived as the panacea for economic development. Solving the accessibility problem of remote areas or addressing congestion in core ones has traditionally been popular with politicians and the public at large and generally regarded to yield high returns to investment. Development policies thus often relied almost exclusively on the provision of roads, railways, sanitation, and water, at the expense of other policy areas that required intervention. While the provision of these public goods is necessary to trigger development, it is not sufficient when other development bottlenecks are not addressed. Hence, many of these policies have not delivered the expected returns. Box 1 briefly presents the case of the Italian Mezzogiorno, where a strategy based on infrastructure and the attraction of inward investment did not manage to cut the development gap between the Mezzogiorno in the South of the country and the rest of Italy.

Box 1 Top down development strategies in the Italian South

The Mezzogiorno, in southern Italy, has traditionally been the poorest part of the country, with levels of GDP per capita that in 1950 were around half the Italian average. From the end of the 1940s the Italian state set up a series of co-ordinated policies aimed at establishing the bases for sustainable development in the South. These policies were fundamentally structured around the provision of transport infrastructure and the establishment of large industrial complexes, by attracting capital primarily from the North of Italy.

However, after fifty years of sustained intervention – and despite a huge improvement of the quality of life in the whole of Italy – the GDP per capita gap between the North and the South of the country remains virtually untouched.

The reasons behind the low returns of the development strategy for the Italian South have to be searched in the lack of adaptation of top-down, supply-side policies to the local contexts of the Mezzogiorno. Greater accessibility, rather than guaranteeing greater access to the market for local products, facilitated the arrival of more competitive products from the North of Italy and other parts of Europe that took a large portion of the market share of local firms. Large industrial complexes set up in the South with the aim of generating development poles, often ended up in isolation, relying on subsidies and suppliers from elsewhere. They became what is popularly know as 'Cathedrals in the Desert'.

b) **Industrialization and attraction of inward investment:** Industrialization strategies and the attraction of large firms to territories with weak industrial fabric have been as popular a strategy as infrastructure investment. However, setting up or importing firms to areas where few or no synergies with the local economy can be established may create a situation is which many of these industries remain detached from the local environment, yielding little or no direct benefit to the local population and often relying on subsidies or incentives to remain active.

The Italian Mezzogiorno or, more recently, the strategies applied to try to develop the regions of the former East Germany, represent two cases where this sort of policies have not yielded the expected results.

The desire to attract foreign investment has also in many cases derived in locational tournaments, where different governments try to outbid each other to attract multinational companies, generally with pernicious effects for the local economy, as was the case of the attraction of car manufacturers to Brazil in the 1990s (Box 2).

Box 2 Zero-sum territorial competition in Brazil

After the lost decade of the 1980s, the economic opening of Brazil at the beginning of the 1990s and greater macroeconomic stability made the country an attractive destination for FDI, especially in the automobile sector. Almost overnight, Brazil became in the mid-1990s the second most important recipient of FDI in the developing world. With levels of car ownership of one vehicle per nine inhabitants, Brazil represented a huge potential market for car manufacturers. However, the setting up of large car plants in the country triggered a bidding war (known in Brazil as the 'fiscal war') involving cities and states trying to lure the European, American, and Asian multinationals to their respective territories.

The typical investment package offered by states and municipalities almost always included the following points:
a. The donation of the land or, at least, of a large percentage of it.
b. The provision of the necessary infrastructure for the preparation of the site. This usually included road infrastructure and utilities, but in some cases it went as far as rail links and the development of port terminals.
c. The provision of state and local tax breaks for periods which in no case were shorter than ten years, and which, in some cases, even included tax breaks on the import of car parts.
d. The provision of loans by the state at fixed rates well below those of the Brazilian credit market.
e. A series of financial and legislative cautions and guarantees.
f. A sundry set of additional benefits, which ranged from providing public transport for workers and nurseries for workers' children to various environmental measures.

This unrestrained territorial competition represented a pure waste of resources for the states engaged in them and for Brazil as a whole, as it deviated a significant proportion of the already scarce public funds to subsidizing multinational companies already interested in the Brazilian market. Moreover, the 'fiscal wars' contributed to jeopardize Brazilian macro-economic stability, and became a huge source of conflict among state and municipal governments.

Source: (Rodríguez-Pose and Arbix, 2001).

Traditional top-down, supply-side development policies have been, and are still, popular because of their simplicity and popularity, but tend to be unbalanced, only relevant to the formal sector, and ultimately incapable of delivering sustainable development and decent work. In addition, these policies are struggling to cope with the more heterogeneous economic reality emerging from globalization and, in some cases may be even contributing to enhance economic agglomeration and regional inequalities.

6. LED as a viable alternative

The general failure of traditional top-down, supply-side development strategies to deliver sustainable development and decent work demonstrates that there is no simple and universal way to tackle the challenges posed by globalization. They also show that there is no unique general solution to the development problems of every area or region, regardless of the local context.

This failure of traditional strategies in an increasingly globalized context has triggered a thorough rethinking of how development problems can be addressed. As a result, a series of tailor-made approaches for the development of sub-national areas has emerged. These approaches, generally grouped under the name of Local Economic Development (LED), highlight the advantages of focusing on the territorial, rather than on the sectoral dimension, and of integrating different development axes in one strategy. They also put a greater emphasis on governance structures and institutions in order to achieve greater sustainability and generate not just work, but decent work.

In short, LED champions a development approach aimed at increasing local economic potential and sustainable employment through giving local governments the tools to devise locally tailored strategies in cooperation with local, regional and international stakeholders and actors.

The nature and principles of LED are more fully developed in successive modules.

Exercise

Globalization	
How did Globalization affect your county/region?	
▪ Volume and composition of trade	
▪ Urbanization	
▪ Decentralization	
▪ Rise of inequalities	
▪ Other	
Development challenges	
What are the main development challenges this poses?	
▪ Under- or Unemployment?	
▪ Degrading work conditions?	
▪ Environmental problems?	
▪ Uneven development?	
▪ Rural poverty?	
▪ Urban poverty?	
▪ Other?	
Strategies to combat these challenges	
In your opinion, have traditional development strategies in your country/region been successful at combating these issues? Why/why not?	
Do you perceive the local economic development approach as a viable alternative to more traditional top-down approaches?	

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