REGIONAL DEVELOPMENT AND REGIONAL DEVELOPMENT AGENCIES

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EXECUTIVE SUMMARY

1. INTRODUCTION

Global economic developments of the last three decades, the advance of globalization and the growth of trade brought forward the region as an economic unit and a crucial element of economic policy. Competition and inequalities began to be discussed at the regional level. The concepts of regional growth and development, various approaches to regional policy and various instruments to implement them gained importance. Regional development agencies as a regional policy implementation tool also came into prominence in the discussions.

In line with the changing interests of both decision makers and academia, the aim of this report is to provide a comparative analysis of regional policies and the conditions in which regional development agencies as regional policy implementation instrument can best answer to the problems of regional development and growth. The regional development agencies are expected to have a direct impact on the development of the institutional infrastructure and increase the regional competitiveness permanently and sustainably. Hence, while other factors influencing regional development and growth are also investigated, the focus of the study is chiefly regional competitive power. On the other hand the contribution of these agencies to the growth and development of the disadvantaged regions may also contribute to the reduction of the regional inequalities. One of the objectives of this report is to contribute to the efforts of the regional development agencies and to provide a framework to help generating new ideas in this topic. The study consist of three main parts. The first part opens with the regional structure and growth in Turkey. The subject is examined in a framework taking into account regions in OECD and BRICS countries. This is followed by a discussion of a general framework of to examine regional growth and development and regional policies. The paradigm shift in the regional policies provides important clues to understand the currently employed regional policies in Turkey and in other countries. The second part of the study has a narrower focus and concentrate on the position and function of the regional development agencies in regional policies using a number of country studies. In this part first the structure and the conditions of efficiency of the regional development agencies are discussed. Then the implementation process and the legal setup of the development agencies in Turkey are evaluated. The theoretical and applied framework developed in the first part is used in the assessment of this implementation process and the legal setup. The third part includes an overall evaluation and propositions. The evaluation about the legal setup incorporates opinions and proposition of TÜRKNFED members. The following is summary of the analyses, data and result of this study.

2. REGIONAL COMPARISON

International comparative studies of the regional differences use generally gross domestic product (GDP) as an indicator; this is also the approach adopted in this study. Various economic and social indicators may be used in these comparisons. There are two reason for the choice of GDP frequently as the fundamental indicator. First, it is widely available in a common standard form, for all countries for a long period of time. Second, it is an indicator representing economic activities as a whole. The possibility of changing definitions of regions and methods of distributing GDP to the regions is taken into account and a common database to minimize this kind of problems is utilized. This database is OECD Regional Database, which has a common standard and common definition of regions and includes BRICS countries (Brazil, China, India, Russia and South Africa) as well as the members of OECD. The comparison is made at the Level-2 regions and GDP, surface area and population neutral two criteria are used. The first criterion
is the ratio of the regional GDP of the richest region to that of the poorest region, and the second is the coefficient of variation calculated as (standard deviation) / (arithmetic mean). Both criteria, the first simple, the second rather more technical, increase with the increasing regional differences. A cross-section analysis of the current situation is done with the differences of per capita income, and regional growth disparities is used to provide a dynamic dimension to the study. The comparison results reveal the following properties:

1) Domestic regional income differences are lower in the developed countries compared to the middle income countries. The ratio of the regional GDP of the richest region to that of the poorest region is around 2 in the selected countries of North America and Europe. In Mexico and Chile this ratio is almost 5. Turkey with its ratio slightly exceeding 4 show a structure similar to Mexico and Chile. The coefficients of variation support this conclusion.

2) International comparison includes 295 Level-2 regions. With respect to the per capita income, the richest region of Turkey is Istanbul (TR10) and the poorest region is Level-2 region consisting of Van, Muş, Bitlis and Hakkari (TRB2). The poorest region of Turkey (TRB2: Van, Muş, Bitlis and Hakkari) ranks also lowest among the 295 regions. The richest region of Turkey Istanbul (TR10) is 196th. Near the position of Turkey there are Mediterranean, Central and Eastern European regions. Below Istanbul there are some Southern regions of Italy, certain low income regions of Portugal and a number of regions from Central and Eastern Europe. Some regions from Italy, Spain and Portugal are just above Istanbul. 20 regions with lowest income among the 295 regions are from Mexico, Chile and Turkey, three countries where regional income differences are most pronounced. (8 regions of Turkey's 26 regions are among these 20 poorest regions. 20 regions with highest income are from the rich countries, except Prague.

3) Structural factors are the root of the regional disparities. The developed country where the regional inequality is highest is Canada. It can be said that in this country large surface area with low population is a more important factor than economic and social conditions. Regional disparities in industrialized countries can be attributed to geographical, historical ad social factors. In lower income countries such as, Mexico, Chile and Turkey the list of determinant of the regional disparities should include the level of economic development as well as geographical, historical ad social factors.

4) With regard to unemployment rate, labor force participation rate and regional differences about production of goods and services in Turkey, the following results should be emphasized:

   i) As the per capita income increases, the unemployment rate decreases. The unemployment rate in the richest regions are near the average regional unemployment rates. The inverse relationship between the unemployment rate and the per capita income (decreasing unemployment with increasing per capita income) emerges in the case of middle and low income regions. This can be explained with the attraction of the high income regions for the labor force supply and rich regions consequent rise as destination of domestic migration.

   ii) In high income regions labor force participation rate increases.

   iii) Regional differences affect production quality visibly. New development theories assume technology and knowledge as the fundamental factor of growth. The relationship between the income and the employment shares of middle and high technology industries and knowledge intensive services sectors are examined. The rise of the value of these indicators point to an improvement of the average levels technology and knowledge. It is observed that as the regional income levels increase, the share of the activities of high technology industries and knowledge intensive services sector increase.

5) With regard to unemployment rate, labor force participation rate and regional differences about production of goods and services in all the examined countries, the following results should be emphasized:
i) The results for Turkey repeat themselves qualitatively in all the examined countries. As the regional income level increases, the regional unemployment rate decreases and the labor force participation rate increases.

ii) Because of the heterogeneity of the industrial structure of the countries, the direction of the relationship between the regional income and the employment shares of middle and high technology industries is undetermined.

iii) Regional income and the employment share of the knowledge intensive services sectors move in the same direction. In other words, as the per capita income level of the region increases, the share of the knowledge intensive activities in the regional services sector increases.

6) The analysis shows that in Turkey, the regional differences in unemployment rate, labor force participation rate and regional differences about production of goods and services, regional income level is a more decisive factor than regional growth rate. However considering other countries, this result derived from the Turkish data cannot be generalized. The results derived from the Turkish case blur when various countries are examined together. Therefore, at least for the indicator used, attempts to find general results about the dynamics of the regional disparities, valid for all countries may be deceptive. Consequently, it should be emphasized that in designing measures to reduce regional disparities specific conditions of the country must be taken into account carefully.

3. REGIONAL GROWTH, DEVELOPMENT AND POLICIES

The report discusses the framework of the regional growth, development and regional policies after a short review of the recent developments in the methodology of the regional growth and development. The concept space as the distinguishing feature of the regional growth and development methodology from the general methodology of the growth and development is assessed. The new theories explaining the emergence of agglomerations and clusters are evaluated in broad terms. Regional policies and regional policy instruments were examined within the framework of a number of basic questions: When the regional policies emerged? What are their main objectives? How they differ in countries of different income levels (developed and developing)? In countries of different income levels do the nature of the regional problems change with time?

The so called new economy which merge growth theories with spatial concepts forms the basis of the current modern paradigm of regional development. An important argument of the new economy asserts that knowledge diffusion is geographically constrained and affects productivity gains and hence regional development. Therefore space plays an active role in regional development and in knowledge creation to enhance the regional development.

Regional policies are influenced from the developments in the theories of growth and development and have changed in time. The beginning of the regional policies is dated with the Tennessee Valley Authority Act of 1933. However systematic use of regional policies began in the 1950s. In the half century since then the scope and the instruments of the regional policies modified to a great extent. They were first intended for the underdeveloped regions or for regions with industrial structure severely damaged in the Second World War. Today the scope of regional policies includes all regions. Institutionally, top-down regional policies were prominent, however today bottom-up policy making is preferred. Top-down policies are similar to the development policies of the post 1950 planning era. Bottom-up approach is a reflection of the mindset of the post 1980 liberalization policies. As indicated above, globalization and liberalization policies brought the region into a more prominent position. With the adoption of the bottom-up approach institutionally, local dynamism became more essential in regional growth and competition.
4. REGIONAL POLICY INSTRUMENTS AND DEVELOPMENT AGENCIES

One of the most important instruments in implementing regional policies is the development agencies. The first wave of establishing development agencies aimed to eliminate the effects of the destruction of the Second World War. In the 1980s and 1990s, fighting de-industrialization was the primary objective. In the third and fourth wave, they were mainly instruments to solve regional problems of the developing countries. The fundamental objective of regional development agencies is to encourage local development and growth.

What are development agencies?

There is no common definition of regional development agencies. A number of distinguishing properties of the regional development agencies established to encourage local development and growth are listed below:

i) **Institutionally**, they are an important instrument of the bottom-up approach. In practice their institutional structure is designed to integrate a broad spectrum of policy tools.

ii) **Organizationally**, they are semi-autonomous public institutions designed by the governments. Following the instances in the European Union, the extent of their autonomy can be defined in three ways: They may be governmental or an independent public body or they may be designed as Private Corporation. The freedom of their operation is expressed with the term "arm's length principle". Within this framework the constitution of their board of directors and the level of political supervision may differ.

iii) **Strategically**, they prefer guiding soft policies (such as counseling services on technology and marketing, financial problems and education, supporting local firms) instead of hard policies such as financial measures or dealing with infrastructure. Therefore they are flexible, innovative, pragmatic instruments encouraging local development. However there are also instances where regional competition, regional growth, growth problems of small and medium sized enterprises, foreign investment, environmental improvement, industrial infrastructure and venture capital are included in the scope of operation of development agencies.

What other countries did?

Great Britain is an interesting example for the regional policy implementation and it has a strong tradition of regional policy. This country implemented regional policies involving a wide array of instruments in the region abandoned by the industries in order to fight the problems of de-industrialization. It also executed active policies to meet the requirement and improve the housing conditions in the destructed urban areas during the post Second World War era. The "new towns" program shows that even before the end of the war, measures to heal the destruction were considered. Great Britain established development agencies in the year of 1998 and carried on the tradition of active regional policy in the 2000s. Only a short while age the agencies were discontinued and Local Enterprise Partnership (LEP) were established without the public involvement. The impact of the politics is obvious in the dissolving the development agencies, but it is also argued that they were not efficient and they failed to eliminate regional differences. The definition of the regional problem in Canada shows similarities with the regional disparity problem of the developing countries instead of the problems of the developed industrial regions of Great Britain. Development agencies are the policy instrument to deal with these problems. In this country also the operation of the development agencies are criticized and various demands are articulated. One such demand is about the cancellation of unnecessary programs by intervention at a federal level. A second criticism points to the need of federal coordination for the integration of the small business assistance program as this assistance is supplied by more than one development agency. Finally it is argued that the
information sharing and collaboration about planning require federal coordination and this should be done within the framework of a national strategy. All of the three proposals implicate the importance of a central coordination. These proposals may help designing the strategy and operation of the development agencies in Turkey as they are relatively young. The need of coordination among the development agencies has already began to be voiced in Turkey as well.

In the United States regional policy objectives manifestly regional growth oriented, rather than eliminating regional inequalities. In this respect United States is different from the two countries examined above. With this lack of targeting elimination of regional differences regional policies of the United States contrasts with the other North American country Canada, as well as all the European countries. Brazil has a regional policy going hand in hand with a quite diversified poverty policies. It is widely believed that all these policies failed, excluding a few exception before the year of 2000. Four reason are given for the lack of success in this period. First, the incentives and subsidy instruments are too strong. Second, the national economic integration creates scale and agglomeration economies benefiting rich regions. Third the investments in rich regions counteracts the attempts at decentralization. And fourth, large scale, important investments in rich region directly increase concentration.

This assessment of the Brazilian experience reveals a dilemma of the developing countries. National completion, economic growth and development require the use of scale and agglomeration economies. However this causes the concentration of the economy in certain regions of the country.

**What Turkey did**

There are three basic trend behind the failure of regional policies in Turkey. The first is the outcome of Preferential Regions for Development (PRD) policy. The second is the asymmetry between the investments and the needs of the regions. And the third is the single-minded concentration on macro policies particularly in the post 1980 period, because of the problems of economic instability, the prominence of opening up and export policies and the protracted use of resource mainly for financing foreign trade. Development agencies are rather new institutions in the regional policies system of Turkey. After decades of classical top-down regional development policies, these new institutions generated a great interest from all stakeholders and created great expectations. Whether the regional development agencies are predominantly public or private oriented is a question of public choice. The development agencies of Turkey are public enterprises. With regard to the execution of authorities, Turkey can be classified among the countries aiming at "de-concentration" of authorities. Even though development agencies are institution representing the bottom up approach, de-concentration of authorities here means giving the responsibility of local implementation of policies designed by the central government to the local authorities within the central hierarchy.

The protracted regional differences raise the expectation from the development agencies and demands of participation. However regional differences cannot be eliminated in short term with a single instrument. There are structural causes generating these differences. An important cause of the persevering regional differences is the formation of clusters in urban areas and the attraction they exert. The existence of such a structural cause behind the regional differences is a problem beyond the target of development agencies about eliminating regional inequalities. In fact, all regions are affected by other macro and micro policies as well as direct regional policies. Furthermore natural (positive or negative) externalities of a region may be so strong that regional policies are doomed to fail to transform them. In any case, whatever the founding approach is, as is true of any such institution, to survive and to be efficient, development agencies need the determination of both the government and the local powers.
5. EVALUATION AND RECOMMENDATIONS

Evidently, the burden of developing local growth potential cannot be left on the shoulders of development agencies alone. However how the development agencies will develop competition to provide the foundation of the regional growth is an important question. It is futile to compare the function of development agencies with the regional incentive schemes of the past. The crux of the function of these institution is to create a regional competitive environment and to improve investment environment for the regional business community. In this context, what the agency can do for the development of the region and how it can improve its institutional structure to be more efficient are two crucial questions. This study utilized two method in order to approach these two question. The first is the Regional Competition Matrix constructed with the economic indicators of the Part 2 of this report. The second is the assessment of some qualitative indicators.

The results about the aggregate regional competitive power of the Regional Competition Matrix illustrate the dual structure, the basic characteristic of the regional differences in Turkey. The competitiveness of the Level-2 regions located in the Eastern and South Eastern Anatolia or development agency regions of TRA1-KUDAKA, TRA2-SEKA, TRB1-FKA, TRB2-DAKA, TRC2-LKARACAĐAĞ, TRC3-DİKA are weak. In addition to these regions, TR71-AHİKA and TR82-KUZKA also have low competitive power. Obviously this evaluation does not pertain to the agencies themselves but related to the income, growth, employment and sectoral structures of the regions. The burden on the agencies in these regions and the required efforts for the regional development are greater.

The results of the first three qualitative indicators show that Level-2 regions consisting of single province with a high level of competitive power do not need external attempts to activate regional development. As can be expected these are TR10-İSTKA, TR31-IZKA AND TR51-ANKARAKA regions. However for the rest of Level-2 regions, either “more data is needed” or the need of activities to stimulate regional development is evident. In this second group of regions where need of activities to stimulate regional development is evident, development agencies should take more responsibility to determine what kind of activities will be more efficient in order to promote regional development and growth. Evidently, the burden of developing local growth potential cannot be left on the shoulders of development agencies alone. However how the development agencies will develop competition to provide the foundation of the regional growth is an important question. It is futile to compare the function of development agencies with the regional incentive schemes of the past. The crux of the function of these institution is to create a regional competitive environment and to improve investment environment for the regional business community. In this context, what the agency can do for the development of the region and how it can improve its institutional structure to be more efficient are two crucial questions. Based on the recommendations included in the report, three basic proposal should be emphasized:

- First, there is a clear need of coordination. The weakness of the competitive power of certain region and their structure consisting of more than a single province require an effective coordination of the in the design of policies and the operation of development agencies. The development agencies of the developed and developing region have the same organizational structure, while the need for a dual structure is noticeably felt.
- Development agencies have the same scope and focus in all regions. More nuanced approach may necessitate different strategies in weakly competitive regions. The adoption of a leading and steering function in the low income regions while adopting merely a complementing role in the developed regions may be a first step in strategy differentiation.
• The new package of incentive schemes has the potential of having a great impact on the regional policies discussed in this study. On the other hand regional development administrations and development agencies have similar objectives and functions. In relation with the incentives of the new package, the overlapping and conflicting features of the objectives and functions of the development agencies and the regional development administrations should be determined and resolved.

The bottom-up approach to regional policies may not be successful in some cases. However the dynamism of the regional economies in Turkey is strong enough to take initiative for entrepreneurship and development. Therefore local contributions are crucial for the development of the country. On the other hand, there is a critical threshold of growth and development in the low income regions. The critical question is how to support them up to this threshold. The results of the new incentive policy may prove essential to this question.