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Regional Governance, Institutions and Development

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Regional Governance, Institutions and Development

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Synopsis

Across the world, the regional level is becoming increasingly important in economic development with a proliferation of regionally-based initiatives. This has important consequences for how institutional capacity is able to take and influence decisions with regard to the long-term future development of particular localities: in short the patterns of regional governance. Two aspects are central to this: (i) the question of governance - how does the ongoing process of institution-building affect the ways in which the regions and localities are governed, including questions of democracy, participation, regional self-determination, public-private partnerships and accountability; and (ii) what are the consequences of new modes of governance and institutional change for regional development strategies and policies, particularly in the context of large-scale industrial restructuring and city-region and urban regeneration.

To address these issues, we draw upon a number of disciplines and link critically to several of the other themes in the overall set. We explore questions related to the relationship between governance, institutional change and regional development:

- on a micro-level the relationship between individual economic actors, development bodies and their environment is examined. This considers both the concepts underpinning industrial districts and networking between private and public economic players, and also the links between agencies under the heading of “Partnership and regional development”. Building strong relationships with private sector firms and organizations has been seen as a priority for public and semi-public development agencies, and the experience in North America and in the European regions, both the difficulties and the successes, is covered and subjected to critical and theoretically informed analysis
- on a meso-level the role of government bodies, various forms of development agencies, both within government structures and beyond, in the political make-up of their region is examined under the heading “Networking and regional governance”. The increasing reliance on individual agencies or networks of development bodies raises important questions about the relationship between functional efficiency and democratic legitimacy, not least when the European dimension in the form of Structural Funds programmes is involved
- on a macro-level the relationship between regionally-based initiatives, federal levels of governance and the emerging European system of governance in Western Europe is discussed under the heading of “Regional Development and Multi-level Governance”. The last few decades have seen a decreasing role for the traditional regional subsidy programmes of central government and a veritable explosion of bottom-up development bodies and initiatives, and through federal or European Union Structural Funds these two levels have been linked together in an intricate pattern spanning across continents e.g. the USA and Europe. In the search for knowledge about the new developments on the regional and continent levels, the transformed role of central government has been somewhat overlooked and therefore considering the relationship between the national, regional and European levels of governance is very much a worthwhile task.

Much of the material is drawn from European examples, and particularly from Scotland. Of all the areas of Europe, Scotland looks most readily to North America for policy initiatives, with many being adopted subsequently based on this experience across the continent. With the re-establishment of the Scottish Parliament in 1999, it therefore provides a valuable comparator to the US based material in the other parts of this course.

1 Introduction

1.1 Context

Many areas of the industrialized world, and especially in Europe, are currently experiencing two parallel developments: the increasing political importance of the regional level and the proliferation of regionally-based initiatives in economic promotion. Both have important consequences for the distribution of the institutionalized capacity to make and influence decisions regarding the long-term future and development of a particular locality. In short these developments will affect the patterns of regional governance.

These developments can be placed in the context of the wider interests in regional governance and institutions which came to the fore in the 1980s in both the literature of economics and geography, when attention began to be given to such factors as institutional capacity, thickness, the invisible factors in regional development, networking and [industrial districts](#) .. This set of learning materials represents a timely and critical reflection on the prominent role of governance, institutions, institution-building and institutional change in regional development at the start of the new millennium. Although institutions, [networks](#) and [partnerships](#) rather than policies often seem to be the answer to regional problems, they have also been stimulated by the general acknowledgment across the social and regional sciences of the importance of [governance](#) ..

Two issues are central to this set of learning materials:

- The question of governance - how does the ongoing process of institution-building affect the ways in which the regions and localities are governed? This question encompasses questions of democracy, participation, regional self-determination, public-private partnerships and accountability
- The consequences of new modes of governance and institutional change for regional development strategies and policies, particularly in the context of large-scale industrial restructuring and city-region and urban regeneration

1.2 Developing Regional Governance and Institutional Capacity

In addressing the emerging issues of regional governance and institutional capacity this section draws upon material in a number of disciplines and links critically to a number of the other themes in the overall set. It is based on current research as well as the existing literature and a number of networks concerned with the analysis of institutions, governance and regional development.

The new institutional environment is characterized by agencies dedicated to the promotion of the regional development of their areas. A recent book (Halkier, Danson and Damborg 1998) found that institutions such as [regional development agencies](#) (RDAs) are beginning to evolve into organizations which do not aim to deliver economic development services directly as much as they try to coordinate the delivery. By acting as catalysts, these agencies have moved beyond simple bodies engaged in development themselves by working in partnership with other players in the regional economy.

Much analysis has been done of these agencies and that of federal, national and regional partnerships within different environments in Europe and the United States. These analyses have focused on their policies, programs and performances, utilizing traditional economic evaluation techniques. But these analyses reflect the traditional form of RDAs. The evolution of RDAs into new forms of development institutions suggests that new theoretical approaches and assessments are needed to analyze them. These institutions are significant in the delivery of regional economic strategies across the developed world, with RDAs having been established in most developed countries and regions. But there is a clear need to consider their position within the overall structures of regional governance.

The trend towards decentralization, albeit uneven across continents, is often primarily analyzed from the perspective of an increase in democracy, often with the national level being seen as an inherently centralizing force only reluctantly giving way to the rising tide of regionalism, with its demands for enhanced levels of self-determination. While this is an important part of the story, there is also another side to the trend toward decentralization, that of the federal or central government relieving itself of responsibility for policy areas that have become a liability. This can arise either because the federal or central government lacks the resources to

manage them effectively, because the economic burden can be off-loaded by passing them onto lower tiers of government, or because the political burden of being responsible for unsuccessful policies is deemed to be high.

1.3 Structure of this Set of Learning Materials

This set of materials discusses questions related to the relationship between governance, institutional change and regional development under a number of main headings:

- **SECTION 2:** This section considers the theoretical bases for the study of regional governance, institutions and regional development. It follows with an exploration of the origins of much of this study in the work of Alfred Marshall in the late nineteenth and early twentieth centuries. Focusing on Marshall's analysis of industrial districts, the section argue that certain aspects of Marshall have been ignored in standard texts. In particular the section contends that Marshall can be seen in a different light than as the neo-classical "father of economics"
- **SECTION 3:** This section extends the theoretical bases to look at some of the approaches to analyzing regional governance and development. It discusses the application of economic and organizational theories to the study of different forms of strategy, introduces the concept of the RDA, and discusses the links between partnerships and networks
- **SECTION 4:** The strategic approach to dealing with the regional economic problem has increasingly become dependent on the RDA. This section explores the nature and rationale for such an institutional form of intervention in the market economy at the level of the region. How such agencies perform under different forms of regional governance is examined against a set of guiding principles
- **SECTION 5:** We explore the relationship between individual economic actors, development bodies and their environment on a **micro-level**. The section considers both the concepts underpinning industrial districts and the mechanics of networking among private and public economic players. Building strong relationships with private sector firms and organizations has been seen as a priority for public and semi-public development agencies; this section reviews the experience that North America and the European regions have had in building such relationships
- **SECTION 6:** On a **meso-level** we examine the role of government bodies and various forms of development agencies (both within government structures and beyond) in the political make-up of their regions. The increasing reliance on individual agencies or networks of development bodies raises important questions about the relationship between functional efficiency and democratic legitimacy
- **SECTION 7:** On a **macro-level** the relationship between regionally-based initiatives, federal levels of governance and the emerging European system of governance in western Europe is discussed under the heading of "Regional Development and Multilevel Governance". The last few decades have seen a decreasing role for the traditional regional subsidy programs of central government and an explosion of bottom-up development bodies and initiatives. Through federal or European Union Structural Funds these two levels have been linked together in an intricate pattern involving nations on different continents, such as the United States and Europe. In the search for knowledge about new developments on the regional and continent levels, the transformed role of central government has been overlooked
- **SECTION 8:** The final two parts of the section use case study materials to examine the arguments around governance and institutional structures in the encouragement of economic growth and development
- **Bibliography**
- **Glossary**

2 Theoretical Background

2.1 Regional Development and Innovation

Ever since the establishment of industrial society, economies have been faced with the problem of industrial renewal. Economists have attempted to deal with this problem amid increased competition and changes in consumer demand. Renewal can refer to innovation and development within established industries, the attraction of new industries through such measures as direct foreign investment, the formation of new indigenous firms, or a combination of all three strategies. The success of a particular strategy is usually measured by the economic indicators of low unemployment and high levels of gross domestic product (GDP). Given the fact that this set of materials discusses industrial production within specific locations, there is an obvious spatial element that we need to address in our measuring of the success of various strategies.

While the problem of industrial renewal can be traced back to the establishment of industrialization¹ the scale and pace of renewal has grown over the last two decades in what can be described as “mature” economies. The need for industrial renewal is tied specifically to the decline of traditional manufacturing and extraction industries within these “mature” economies.² This section will deal with problems associated with industrial renewal within mature economies over the last two decades, focusing on governance structures, namely industrial districts, networks and partnerships.

The changing nature of innovation within industrial production can be cited as the principal cause of the accelerated need for policies to tackle the problems associated with industrial renewal. This changing nature has affected “mature” economies in two ways. First, the “Fordist” techniques of production and “Taylorist” methods of scientific management have been replaced with new production methods such as flexible specialization.³ This has led to firms and industries which have not adapted to these new methods of production becoming uncompetitive. Not all industries and firms are developing on the lines of flexible specialization or variants of flexible specialization such as just-in-time. However, firms in the more dynamic sectors of the economy are developing on these lines. Second, the increasing internationalization of business organization has led to the growth of mass production methods in low-cost countries or low-cost regions. Typically, the mass production low-cost firms that locate their branch plants in “mature” economies are attracted, through incentives, to regions that have suffered from industrial decline of traditional manufacturing and extraction industries.

The development of new methods of production such as flexible specialization has coincided with a growth in the small medium enterprise (SME) sector in the “mature” economies. According to Stanworth and Gray (1991) between 1979 and 1986 the total number of business enterprises rose from 1.791 million to 2.471 million in the United Kingdom. “Of the 1986 total number of enterprises, only 12,000 had 200 or more employees and only 4,000 had 500 or more. The share of enterprises with fewer than 500 employees increased from 57.3 to 71.3 per cent of total private sector employment between 1979 and 1986” (Stanworth and Gray, 1991, 6).

This growth in importance of the SME sector can be attributed to a number of factors such as a reaction to a downturn in the economy, with people whose jobs have been made redundant turning to self-employment as a means of earning a living. According to Pyke and Sengenberger (1992, 9) “A surge of small businesses, and a loss of employment in large firms, occurred during the Great Depression in the 1930s. It recurred in the 1970s and 1980s following the recession after the oil shocks. Yet, when the national economies expanded again more strongly during the 1980s, the trend to small firm employment continued, suggesting that small firm expansion is more than a transitory, cyclical phenomenon.” Pyke and Sengenberger are unconvinced by the usual arguments cited for the growth in the SME sector, such as sectoral shift, avoiding “red tape” and cost reductions. They argue that the growth in SMEs has occurred across sectors and ask why the avoidance of red tape and cost reductions has only become important in the last two decades. According to their argument the main reason for the growth of SMEs in “mature” economies is changes in the organization of production.

¹In the case of the UK economy Hobsbawm identifies the beginnings of decline of industry “between the middle of the century and the 1890s” (Hobsbawm 1968).

²Principally, the economies of Western Europe, the United States and Japan

³See for example the 1988 UK White Paper on Competitiveness

TABLE 2.1 Percentage of employment in enterprises with fewer than 100 employees, European Union countries (early 1980s)			
	Manufacturing	Services	Whole economy
United Kingdom	22.0	NA	NA
Italy	58.9	NA	NA
Germany	NA	NA	NA
France	44.1	72.1	55.1
Netherlands	37.8	65.0	57.5
Belgium	32.8	55.7	45.9
Spain	43.4	59.7	58.6
Greece	NA	NA	68.7
Portugal	43.8	78.8	57.6
Luxembourg	19.2	NA	NA
Denmark	39.8	NA	NA
Republic of Ireland	38.1	NA	NA
Source: Commission of the European Communities (1987a)			

This material analyses the impact of these new types of methods of organizing production, namely industrial districts, networks and partnerships. Although SMEs are not the only units of production within these new methods of production, recent policy initiatives in mature economies have placed an increased emphasis on SMEs that reflects their growing importance. Industrial districts, networks and partnerships are regarded as new methods of production, but it has to be remembered that some of these methods of production have a long history. Industrial districts were noted by Marshall in *Principles of Economics* in 1890. They have recently been “rediscovered” in many regions of mature economies. Industrial districts can now be analyzed as “new” types of industrial productive systems, because they transcend the neo-classical notion of the firm. One finds an increased awareness being placed on institutional capacity, governance and institutional change in regional development. Within the existing literature Becattini (1990, 38) provides a useful definition of industrial districts... “a socio-territorial entity which is characterized by the active presence of both a community of people and a population of firms in one naturally and historically bounded area. In the district, unlike in other environments, such as manufacturing towns, community and firms tend to merge. The fact that the dominant activity is an industrial one differentiates the industrial district from a generic ‘economic region’” Becattini argues that the surplus generated from production within a district necessitates the development of trade which “excludes the possibility of accidental placing of the products of the district on the external market, and requires instead the development of a permanent network of links between the district and its suppliers and clients” (Becattini 1990, 38).⁴ What Becattini clearly identifies is the importance of socio-political factors, the links between suppliers and clients, and the impact of the community in enhancing the performance of firms within industrial districts. In essence the governance structure of the type of productive system is of crucial importance. The importance of the governance structure necessitates an economic analysis that transcends the strict neo-classical economic approach for the identification of the economic gains accruing to businesses organized in specific types of organizational structures.

Within the existing literature three broad approaches have been adopted to analyze these “new” forms of industrial productive systems. First, there is the transactions costs approach, a neo-classical framework developed by Williamson through Coase. The second approach focuses on “embeddedness.” The “embeddedness” school is critical of the neo-classicists, believing that they fail to capture the essential dynamism of the districts. Harrison (1992) introduces the idea succinctly: “Whatever their purported stability, the ‘historical and cultural vestiges’ that contribute to the ‘localized “thickening”’ invite references to another whole intellectual stream that has fed the writing on the industrial districts. This is the idea of ‘embeddedness’, and it is quite different from the modes of theorizing to be found in conventional regional economics

⁴A discussion of this White Paper is found in [section 8](#) of these learning materials. Reference to institutional/evolutionary approaches to regional governance structures can be found in [section 3](#).

- or to any other branch of standard (neoclassical) economic theory, for that matter.” The third broad approach begins from an empirical policy perspective and typically involves the citation of case studies and identification of key characteristics of production organized through differing governance structures. From there it proceeds backwards to establish some insights into a theoretical perspective whereby policy initiatives could be forthcoming. This third approach relegates any economic analysis to a minor role, citing the political and social aspects of the individual case studies. These three approaches are broadly defined, and many researchers would argue that they represent “false” boundaries.

These three broad approaches to analyzing new productive systems further reflect the importance of the concept to academics and policymakers from a wide variety of backgrounds.

- The spatial aspect and emphasis on agglomeration economies has attracted interest from regional economist.
- The development of trust and cooperative relations evident in many of the industrial districts has caught the attention of political scientists
- The specific nature of the industrial process has similarly been analyzed by researchers and commentators involved in the debates over flexible specialization and post-Fordism
- The apparent “success” of the regions containing and developing industrial districts has, for obvious reasons, attracted the attention from policymakers from the European Union down

All three of these approaches to understanding new types of productive systems owe a debt to Marshall. From this common starting point, however, the three approaches quickly diverge, stressing different aspects of Marshall. The “neo-classical” approach stresses the acceptable face of Marshall found in his static equilibrium analysis in *Principles of Economics*. The standard critical appraisal of Marshall, too, employs a selective reading of Marshall. Harrison, for example, neglects recent developments within the discipline of economics that may lend themselves to better analysis of new productive systems, most pertinently game theory and evolutionary economics. Harrison is correct to identify the problems of a neo-classical approach along the lines of traditional analysis of industrial economics, following Coase, Williamson et al. Their approach, however, risks “throwing the baby out with the bathwater” by ignoring important sections of Marshall, as does much of the existing literature. Researchers using the empirical policy approach emphasizes the socio-economic side of Marshall’s work. Because of this, they often fail to identify the role of custom, habit and the achievement of cooperation and trust within industrial districts as outlined by Marshall. Though their work stresses these points as being crucial to the success of current industrial districts, it generally fails to identify them in the original Marshallian analysis. This is somewhat surprising, given the credit that much of the literature gives to Marshall for outlining these points. Shove, for example, states that Marshall “recognized more fully than Mill and much more fully than Ricardo the influence of social customs and institutions on economic behaviour; and he tried to weave it into the fabric of his system.” (1942, 308). A reading of Marshall can identify him as an institutionalist/evolutionary economist; recent developments within regional economics are better understood from this perspective. Understanding the gains from organizing production within spatially specific regions either through a partnership, network or industrial district structure requires an institutional/evolutionary economic approach.

The idea of encouraging cooperation between firms as a policy instrument is not new; it has underpinned Japanese industrial policy for the last four decades. Within the European Union, the earliest formulations of an industrial policy, for example the ESPRIT program, made cooperation between firms a major objective. However, the difference between these types of cooperative ventures and what is being discussed in these learning materials is the spatial aspect of promoting industrial development within specific regions. Elements of a strategy leading to the promotion of a more spatially specific industrial policy is observable within the European Union’s White Paper *Growth, Competitiveness, Employment* (CEC 1994) “The proliferation within the Community of ‘clusters’ that combine industrial, technological and geographical advantages may hold one of the keys to job creation. This requires the active involvement of all the actors concerned, something which can be greatly facilitated by structural measures taken at Community and national level” (79). This promotion of “clusters” is only one of several measures identified by the European Union. By promoting this type of policy the European Union is falling into line with many member states in two ways; first, by recognizing that SMEs are the potential main source of new employment, and, second, by recognizing that

one way to encourage SMEs to develop and prosper is by the promotion of them through cooperation in spatially specific areas. Industrial districts composed of SMEs have been identified in Southern Germany, Italy, Spain, Denmark, and France among other European Union states. But successful policy requires a real understanding of the economic advantages of organizing production in spatially specific industrial districts. The ideas at the heart of clustering and networking are developed in [sections 5, 6, 7 and 8](#) of this set of learning materials.

2.2 Marshall and Marshallian Industrial Districts

2.2.1 The Origins of the Industrial District

In part 2.2 we explore the debt that contemporary analysis of governance structures such as networking, partnership and industrial districts owe to Marshall. We move beyond the standard approach to Marshall by looking at notions such as trust and cooperation, which are rarely credited to Marshall. From there, we develop the notion that Marshall needs to be observed beyond the neo-classical framework with which he is usually associated. In particular we explore the possibility that Marshall can be observed as an institutionalist/evolutionary economist. If this is the case then a further debt to Marshall should be acknowledged. Recent work on “knowledge based” economies discusses the establishment of the institutional framework to develop such an economy in an evolutionary way.

Much of the contemporary research on industrial districts notes a link with Marshall, but the richness of these districts in Marshall’s original writings is often ignored. A fuller interpretation can be found in Loasby (1986), (1990), O’Brien (1990), Jensen (1990), Foster (1993) Hodgson (1993) among others who discuss an institutional reading of Marshall. The reason for such a reading has already been outlined, namely that Marshall is observed as being nothing but “the father” of neo-classical economics. To fully appreciate the significance of Marshall in relation to the original analysis of industrial districts, we initially outline his analysis of them. We then identify what we believe to be a significant contribution made by Marshall in his analysis but missed by contemporary researchers: the notion of “[constructive cooperation](#)”.⁵ Extrapolating from this notion, we then argue that there is more to Marshall than a narrow, neo-classicist, equilibrium interpretation would suggest and that an evolutionary reading is required to fully appreciate the significance of Marshall’s industrial analysis.

2.2.2 Industrial Districts and Marshall

Marshall’s ‘discovery’ of industrial districts arose primarily out of his empirical studies of the steel and textile industries, principally in the United Kingdom. Building on Adam Smith’s recognition of the benefits of specialization,⁶ Marshall established that within these industries, the greater the opportunities that existed to split up the production process, the greater the chances were that specialist firms would develop. In discussing the nature of production in *Principles of Economics* (1916),⁷ Marshall saw the benefits of production accruing to the individual large firm as being differentiated between internal economies of scale and those arising to the industry as a whole, or external economies: “We may divide the economies arising from an increase in the scale of production of any kind of goods, into two classes -firstly, those dependent on the general development of the industry; and, secondly, those dependent on the resources of the individual houses of business engaged in it, on their organization and the efficiency of their management. We may call the former external economies, and the latter internal economies” (266).⁸

Which of these two economies Marshall perceived as more important varied from industry to industry. Because of this Marshall’s works sometimes stress the importance of internal economies, and other times they stress external economies. In *Industry and Trade* (1932), for example, he says that “with the growth of capital, the development of machinery, and the improvement of the means of communication, the importance

⁵An exception to this is Bellandi in Goodman et al. (1989) who discusses constructive cooperation in relation to Business Associations, which is where Marshall makes first reference to the concept. Our point is that the organization of a Business Association formalizes the institution of constructive cooperation.

⁶See for example A. Smith (1976) vol. 1, p. 13-24.

⁷All references to the *Principles of Economics* will be to the 7th edition 1916.

⁸Principles p. 266

of internal economies has increased steadily and fast” (167).⁹ In *Principles of Economics*, though, he argues that “external economies are constantly growing in importance [relative] to internal in all matters of Trade-knowledge” (284)¹⁰ This apparent contradiction can be attributed partly to the growth of joint stock companies taking place at the time Marshall was writing and partly to the empiricist methodology he adopted. O’Brien, in discussing the relationship between small firms and joint stock businesses in Marshall, argues that Marshall, realizing the enormous advantages that internal economies brought to joint stock companies, believed that “the path of economic development offered few long-term portents favourable to the small firm” (1990, 75).¹¹ Hints of Marshall’s empiricist methodology can be observed within the subtext of *Industry and Trade*. Marshall himself defined the work as “A study of industrial technique and business organization” and O’Brien argues that it is precisely that, a study of different types of firm organization and production.¹²

Loasby (1990) argues that the problem in discerning which industries accrue greater advantages from internal economies and which from external economies is compounded by “Marshall’s discussion of localisation (which) cuts across his distinction between the organisation of businesses in the same trade and the organisation of various trades relatively to one another, being concerned sometimes with relations between similar firms and sometimes with firms whose activities are complementary” (112). Loasby argues that “localisation,” along with specialization (which means the production process¹³ can be broken up into smaller stages, thereby allowing small specialized firms to fulfill a part of the total production process) are ways in which small firms can accrue external economies of scale and thus overcome the disadvantages which arise due to their size. Though Loasby’s point is well taken, there is no doubting Marshall’s belief that the achievement of external economies “can often be secured by the concentration of many small businesses **of a similar character** in particular localities: or as is commonly said, by the localisation of industry”.¹⁴ In effect this localization of industry can be an alternative to larger size for the individual enterprise.¹⁵ This point is reinforced by Marshall’s view of the organization within particular industries: “For instance,” he says, “in cotton spinning, and calico weaving, a comparatively small factory will hold its own and give constant employment to the best known machines for every process: so that a larger factory is only several parallel smaller factories under one roof; and indeed some cotton spinners, when enlarging their works, think it best to add a weaving department”.¹⁶ The various economies of scale arising from the different methods of industrial organization within Marshallian industrial districts have been highlighted elsewhere (Oughton and Whittam, 1997).

To Marshall, specialization “in large measure dispensed with the necessity of any complex arrangements in each individual business, since the external economies, which even a small business thus obtained, were generally far more important to it than those which the largest business in the world could obtain by its own efforts...”.¹⁷ It was the coupling, then, of localization and specialization that gave rise to the notion of industrial districts. To Marshall, industrial districts are not exclusively the preserve of small firms; indeed, he comments: “The largest industries, and especially those that need massive plant, are located increasingly in industrial districts...”.¹⁸ But small firms, by providing inputs and specialist finishing, can also accrue external economies from being located in industrial districts, as the first of the two quotes makes clear.

In addition to external economies arising out of production, Marshall identifies benefits arising out of agglomerations, such as skilled labor, capital and infrastructure. In his observation of one industrial district, he noted that “the trading functions of the city developed. Warehouses for the products of the district took the place of factories: shops for the accommodation of the district were enlarged; and banks and mercantile houses of all kinds became prominent”.¹⁹ A further benefit coming from the location of industry

⁹Industry and Trade p. 167

¹⁰Principles p. 284

¹¹O’Brien (1990, 75)

¹²“One year passed much like another. In vacations, either at home or abroad, we spent some time in towns, seeing factories and workshops...One year we would go to the pottery district with its problems of localisation of industry and changing fashions...Another year it would be the light metal trades.” (M.P. Marshall, 1947, 42-3) quoted in O’Brien 1990 p. 65.

¹³Loasby (1990, 112)

¹⁴Principles p. 266

¹⁵Loasby (1990, 111)

¹⁶Principles p. 281

¹⁷Marshall “Industry and Trade” the 1932 of the Third edition of Industry and Trade will be used throughout this paper, p. 600

¹⁸Marshall (1932 284)

¹⁹Marshall (1932, 285)

in a particular district is what Marshall describes as an “industrial atmosphere.” In *Principles of Economics* he describes how such an atmosphere develops: “When an industry has thus chosen a locality for itself, it is likely to stay there long; so great are the advantages which people following the same skilled trade get from neighborhood to one another. The mysteries of the trade become no mysteries; but are as it were in the air, and children learn many of them unconsciously”.²⁰ The establishment of an industrial atmosphere thus takes on the appearance of a public good, with skills being constantly developed and interchanged. The interaction that leads to children achieving skills leads in turn to the exchange of ideas, which results in innovation within the district. Marshall continues: “if one man starts a new idea, it is taken up by others and combined with suggestions of their own; and thus it becomes a source of further ideas”.²¹ The “**industrial atmosphere**” leads to a long-term commitment of an industry to a particular district. Marshall identified this trait in his description of industrial atmospheres in Sheffield and Solingen. The two areas, he said, “yield gratis to the manufacturers of cutlery great advantages, that are not easily to be had elsewhere: and an atmosphere cannot be moved”.²² Once industrial districts become established they are relatively stable productive systems. Marshall concluded that “an established centre of specialised skill, unless dominated by a guild or trade-union of an exceptionally obstructive character, is generally in a position to turn to account quickly any new departure affecting its work; and if the change comes gradually, there is no particular time at which strong incitement is offered to open up the industry elsewhere”.²³

But industrial systems are also dynamic systems, the dynamism being created by the constant interaction of the actors involved. Marshall argues that merchants not only purchase goods but also “discuss with the manufacturer himself any suggestions which may occur to them for modifications in detail, to suit their individual judgments, or to meet the special tastes or requirements of localities with which they are connected”.²⁴

Much of what has been stated in this paper so far merely establishes Marshall’s analysis of industrial production. Our comments regarding industrial districts are typically cited by researchers of contemporary industrial districts in arguing that they are Marshallian. Some researchers, have, however, argued that contemporary industrial districts differ from industrial districts as identified by Marshall in the degree of cooperation, trust and networking relationships that they exhibit. We argue instead that much of the current research fails to note that Marshall himself identified the significance of cooperation within his analysis of industrial districts.

2.2.3 Marshall and Constructive Cooperation

The continual interaction of buyers, sellers and producers resulted in more than an industrial atmosphere, Marshall coined the term “constructive cooperation” to identify one of the factors which gave industrial districts a competitive edge. In examining Britain’s strengths in comparison to Germany and the United States he argued “that the strong individuality of the British race may find its highest development under the guidance of the spirit of constructive cooperation”.²⁵ This cooperation enables even “moderate sized” businesses to compete with much larger competitors “provided these qualities are united with a frank willingness to learn from others; and to cooperate genially with others in matters in which unfettered association has large opportunities”.²⁶ The economies which accrue to medium sized businesses, enabling them to compete with larger competitors, arise out of the evolution of new organizations which are directly the result of the development of constructive cooperation, which arose out of the constant interaction within the industrial districts.

According to Marshall this constructive cooperation was counter to the negative aspects of cartelisation, which resulted in the price fixing identified in many branches of German industry. In Britain It was not deliberate policy that gave rise to constructive cooperation, rather the organization of production gave rise to it automatically: “Britain was indeed the chief home of the automatic cooperation of many industries; as

²⁰Principles p. 271

²¹Principles p. 271

²²Marshall (1932, 284)

²³Marshall (1932, 287)

²⁴Marshall (1932, 286)

²⁵Marshall (1932, 577)

²⁶Marshall (1932, 584)

it was also of reasoned analysis of the ‘natural’ tendency to such division and organisation of labour as is needed to make it collectively efficient”.²⁷ Marshall cites the textile industry as being typical of this natural development: “The high automatic organisation of these industries, is in great measure due to the fact that their plant is made in their own districts, with constant intercommunication of ideas between machine makers and machine users”.²⁸

This constructive cooperation led to the establishment of new institutions to further the potential advantages which could arise out of cooperation. Marshall cites such examples as “The British Pottery Manufacturers’ Association,” which had among its purposes “To deal with the quality, supply, purchase, and control of raw materials and stores, where desirable, in the interests of the members; to deal with all questions relative to cost and conditions of transport; to consider means of facilitating the extension of export trade; to bring about closer cooperation with the technical arts, and designs sections of the pottery schools; to promote general propaganda, and to undertake advertising in connection with the industry; to consider the best means of encouraging and utilizing improvements, inventions, and patents for the general good and advancement of the industry; to deal with all matters connected with more economical production, including costing; to watch national and local legislation affecting the industry ...Experts are to be appointed, and assistance given to members in overcoming the technical difficulties which constantly arise in so complex an industry; and the Federation has power to purchase, work, and exploit any patents, secret processes, or other improvements in the general interests of the members”.²⁹

Other similar organizations cited by Marshall include The Bradford Dyers’ Association and the ‘Fine Cotton Spinners’ and Doublers’ Association, which also employed skilled personnel “for dealing with every part of a cotton spinning mill, who are too expensive to be employed by a single firm; but are in effect available for all”.³⁰ The services being provided by these three associations are extremely similar to those being provided by the “Industry Specific Service Centres” of the Third Italy over half a century later and which have been identified as being of crucial importance to the success of the industrial districts in the regions making up the Third Italy. Although we focus on the [Third Italy](#) in section 6 it would be pertinent to briefly highlight some of the cooperation occurring in these contemporary industrial districts there.

Quasi private-public service centers, such as the Regional Board for Economic Development ([ERVET](#)) supervise the development and upgrading of the region of Emilia-Romagna as a whole by such measures as infrastructural improvements and the provision of training and research facilities. Furthermore, an examination of the services provided by an organization such as CESMA, which is a service center for farm machinery organized by ERVET, reveals the following: research, technological consultancy, products quality assurance, quality systems processes and certification. (ERVET 1990). Further support services can be obtained from individual industrial sector centers, specific to their own industry, to assist with such activities as exporting, technical developments and provision of access to computer aided design (CAD) systems, for example. Associations such as the Confederation of Artisans (CNA) typically provide accountancy services for member firms. These democratically elected and accountable bodies enable participating firms to achieve external economies of scale. Elsewhere we have identified the different types of external economies accruing within the industrial districts of Emilia-Romagna (Oughton and Whittam 1996).

There is a spatial dimension to the organizations cited by Marshall that gives them a further similarity with the “Real Service Centres” found in the Third Italy. Although Marshall believed there was a lot more to be done, he identified “constructive cooperation” existing in the promotion of exports through organizations such as chambers of commerce: “there remain great gaps in the work to be done: and accordingly the ‘Federation of British Industries’ has set itself to promote the formation of representative Associations for particular industries; ‘to collect them their leading members into a central federation for dealing with matters of common interest to all industries, and for mutual support’: to allot to each industry or trade a duly proportionate ‘voice in the discussion and decision of questions of promotion and development of British trade’”.³¹

This overview of the establishment of industrial districts in Marshall leads us to an examination of the existing

²⁷Marshall (1932, 600)

²⁸Marshall (1932, 603)

²⁹From the ‘Trade Supplement’ to ‘The Times’ Dec. 1918 quoted in Marshall (1932 p. 604)

³⁰Marshall (1932, 606)

³¹Marshall (1932, 612)

literature on contemporary industrial districts and to identify its limited interpretation of Marshall. Although all researchers in the field of what can loosely be called industrial districts recognize the establishment of cooperation and trust as being essential for the success of these districts, it is argued by some that cooperation and trust signify a difference between these districts and the industrial districts identified by Marshall Harrison³² for example, while providing a comprehensive account of the literature on Marshallian analyses of industrial districts argues that the districts of Emilia-Romagna are more than “old wine in new bottles”. In particular, he uses Becattini’s phrase “localized thickening”³³ to explain how the “new” theories of industrial districts differ from “neo-classical economic theories of externality and agglomeration (which) seem to miss important -perhaps the most important- elements of the construct” (Harrison, 1992, 475). Thus Harrison argues that standard neo-classical economics is not sufficient to deal with the concepts of industrial districts. A reading of Marshall does in fact lend itself to an analysis of industrial districts using “new” as well as “old” theories. Such a reading is possible because there are what Jensen (1990) refers to as “institutional signposts” within Marshall, particularly, in Marshall’s analysis of industrial production within industrial districts outlined in *Principles of Economics* and perhaps more pertinently in *Industry and Trade*.

What Harrison does not make clear is how the “localised thickening” differs from the “constructive cooperation” between key players that Marshall identified as occurring within industrial districts he observed. We have already noted the similarity in services provided by differing organizations, notably the British Pottery Manufacturers’ Association and the “Real Service Centres” of the Third Italy. “Constructive cooperation” requires the establishment of trust. The constant interaction of the actors within Marshall’s industrial districts, leading to innovation and the sharing of skilled personnel and machinery, must rely on the development of trusting relationships and the “localized thickening” of community relations identified as being of crucial importance in contemporary industrial districts.

In a similar vein Wilkinson and You, while noting Marshall’s reservations regarding various types of organizations,³⁴ fail to comment on Marshall’s emphasis on the benefits of constructive cooperation which may exist “without any apparent drift to use it as a means of maintaining prices at higher levels”.³⁵ They do note the different emphasis placed by contemporary analyses on concepts such as trust and cooperation. We would argue, though, that the difference between contemporary analyses and those of Marshall is in the emphasis they place in trust and cooperation rather than in whether they see trust and cooperation as valid principles. Similarly, Becattini³⁶, in exploring “The Marshallian industrial districts as a socio-economic notion” notes the establishment of a common value system, within the industrial districts of the Third Italy, but argues that it is necessary to use disciplines rather than economics to fully understand the nature of this phenomena. Becattini fails to draw on evidence that Marshall readily identified the role and function of a common value system and the beneficial impact this can have on the production process and the facilitating of exchange. In discussing industrial districts within Marshall, Zeitlin³⁷ similarly fails to discuss the nature of constructive cooperation found within Marshall. He refers to the usual establishment of an “industrial atmosphere” as being one of the features typically found within the industrial districts identified by Marshall. The “thickening process” of rich networking relationships, typical of industrial districts, which we have argued exist within Marshall, is only noted, according to Zeitlin, by contemporary researchers of industrial districts. A possible reason for this oversight within the existing literature could be that researchers observe Marshall merely has a neo-classical economist.

In part 2.2 of the learning materials we have observed the production process as outlined by Marshall, with specific references being made to his industrial districts and the limited interpretation of Marshall by contemporary researchers. Regarding the development of industrial production as observed by Marshall, we have highlighted the link between greater specialization and the development of the organism as a whole, that is the synergy effects of industrial organization, summarized by Marshall in the following quote: “This central unity is set forth in the general rule, to which there are not very many exceptions, that the development of the organism, whether social or physical, involves an increasing subdivision of functions between its separate

³²Harrison B. (1992) Industrial Districts: Old Wine in New Bottles? *Regional Studies*, 26, 5, 469-483

³³Becattini (1989, 132)

³⁴Wilkinson and You (1992 footnote 10. p. 7)

³⁵Marshall (1932, 604)

³⁶Becattini (1990)

³⁷Zeitlin in F. Pyke and W. Sengenberger (1992)

parts on the one hand, and on the other a more intimate connection between them”.³⁸ It is to a more detailed examination of this link which we now turn to highlight the function of **trust and cooperation** within Marshall which leads to an institutional/evolutionary reading of Marshall, which, if adopted, would prevent the misinterpretation of Marshall by current researchers in the area of industrial districts.

2.2.4 Marshall and Institutional/Evolutionary Economics

Part 2.2.3 examines Marshall’s analysis of industrial production places Marshall within the existing **evolutionary economics** literature, indicating that there is more to Marshall than a static equilibrium reading of *Principles of Economics* could imply. In particular, Foster (1993), provides a convincing argument of “time irreversibility” which leads to an evolutionary approach to be observed within Marshall. This approach is reinforced by Hodgson (1993) and Jensen (1990), whose identification of “institutional signposts” within Marshall has been mentioned. In terms of industrial production specifically, Loasby (1990), suggests that the emphasis placed on organization by Marshall leads to a consideration that organization “might be identified as a distinct factor of production” (Loasby, 1990, 111). It is precisely the organization within industrial districts both in the original Marshallian sense, and the contemporary usage of the term, which gives these regions a competitive edge, and makes them of interest to contemporary researchers and policymakers.

Organization is the general rule which underpins Marshall’s analysis of the entire production process. Cooperation in the sharing of knowledge (which leads to increased innovation) and the development of an industrial atmosphere (which results in the establishment of new organizations that facilitate production and trade, namely constructive cooperation) both derive from this general rule. Implicit in Marshall is an evolutionary approach to industrial organization; this approach, we would argue, underlies the whole of Marshall’s economic analysis. It is by adopting an evolutionary reading that links between Marshall’s original industrial districts and contemporary industrial districts can best be understood. The intimate connection is the development of trust and cooperation that we have identified within Marshall’s original industrial districts.

The trust underlying constructive cooperation develops through relationships that evolve through interaction within markets, as the following citation makes clear: “Everyone buys, and nearly every producer sells, to some extent in a ‘general’ market, in which he is on about the same footing with others around him. But nearly everyone has also some ‘particular’ markets; that is, some people or groups of people with whom he is in somewhat close touch: mutual knowledge and trust lead him to approach them, and them to approach him, in preference to strangers”.³⁹ It is through everyday market relationships that situations of trust are established. Industrial districts consist of particular markets where producers and consumers cease to be strangers. Within the industrial district systems of production this trust evolves into an institution transcending strict market relations, that of constructive cooperation (Gambetta 1998). This new institution paves the way for the evolution of new organizations such as the British Pottery Manufacturers’ Association.

This identification within Marshall’s industrial districts of evolving social institutions leads to a reading of Marshall which takes account of the role of tradition, custom, habit and legal restraint. In other words, we are arguing that there is more to Marshall than a narrow neo-classical reading will permit. The establishment of the social institutions facilitates the development of economic relations which enable SMEs to exploit external economies of scale and to reap an economic advantage from being organized in close-knit, geographically specific economic units.

In analyzing trust in industrial districts for facilitating exchange, Dei Ottati (1994) distinguishes between cooperation and trust as collective and as personal capital. We would argue that the quotes we have provided above indicate that within the strict Marshallian industrial district trust and cooperation are observed to be both personal and collective. They are personal in that individual traders and producers engage in discourse to improve innovation, collective in that the establishment of an industrial atmosphere results in the achievement of “public goods.” For trust and cooperation to succeed requires an effective enforcement mechanism, whether formal or informal. Within any organization such as The Bradford Dyers’ Association, members who broke the rules could be excluded. Similarly, in specific communities where there is a particular set of informal

³⁸Principles p. 241

³⁹Marshall (1932, 182)

rules and norms, that is, institutions, actors who do not comply can be shunned. However, it would be beneficial not to have to rely on enforcement mechanisms to safeguard the cooperative outcome. Within Marshall we can observe the potential of trusting relationships evolving out of cooperation. Initially this cooperation develops through the market mechanism, “the general market” but in “particular markets”, in our case the productive systems of industrial districts, “mutual knowledge and trust” evolve. The establishment of cooperative behavior and trusting relationships develops into beneficial outcomes in terms of product innovation, the sharing of knowledge, information, productive capital and personnel to such an extent that Marshall can describe the achievement of an “industrial atmosphere” and the establishment of “constructive cooperation.” The informality of these phrases suggest cooperation and trust being achieved without resort to formal enforcement mechanisms.

The achievement of a productive system based on cooperation and trust undoubtedly leads to economic efficiency and “is an important lubricant of a social system.” (Arrow, 1974, 23). In this role of lubricant of the social system Arrow discusses how lack of trust can lead to inefficient outcomes. “Collective undertakings of any kind, not merely governmental, become difficult or impossible not only because *A* may betray *B* but because even if *A* wants to trust *B* he knows that *B* is unlikely to trust him”.⁴⁰ The achievement of an “industrial atmosphere” and “constructive cooperation” can overcome these inferior outcomes. Furthermore, Hirschmann makes the point that trust, cooperation, collective action and the like, are different than other goods and services in that the more they are used the greater they become, although there is a limit to goodwill: “they atrophy when not adequately practiced and appealed to by the ruling socioeconomic regime, yet will once again make themselves scarce when preached and relied on to excess”.⁴¹ So within Marshall’s industrial districts we would argue that through individual action the actors developed an atmosphere in which cooperation and trust developed to such an extent that they became the norms of behavior. The establishment of such a culture led to the achievement of public goods and the creation of dynamic efficient economic systems. These systems led to the formalization of the institutions into organizations to facilitate the evolution of the industrial districts. This interpretation of industrial production found within Marshall, we would argue, requires reading Marshall in the light of an institutional/evolutionary framework. We have argued that reading Marshall merely as a neo-classical economist can lead the reader to miss many important concepts that have only recently been observed by researchers in contemporary industrial districts.

⁴⁰Arrow (1974, 26)

⁴¹Hirschmann (1984, 94)

3 Theoretical and Discipline Underpinnings to Governance, Institutional Change and Regional Development

3.1 Background

The study of governance and institutional change has come relatively recently to regional science. A range of methodologies is being applied to this study by researchers and commentators. Without recourse to a range of disciplines, it is not possible to gain an understanding of the matrix of forms and structures that have been implemented across the developed world. Theoretical bases for the critical assessment of case studies and the variety of institutional frameworks to be studied are essential for the researcher trying to compare and contrast the different frameworks. A corollary is that no one discipline or approach has been adopted universally to explain the development of governance and institutions within or between countries.

The above discussions on the origins of the concepts of the industrial district, networking and partnerships, and in particular the role of Marshall in identifying and developing these concepts, should serve to stress the need for caution in studying governance and institutional change. Much of the literature of the last twenty years has failed to acknowledge what earlier analysts have uncovered. Adopting a narrow discipline route to enlightenment can be damaging and wasteful, therefore, with critiques and self-critiques following the initial flush of enthusiasm. Below, the need to address a broad range of material is suggested, and the reader is encouraged to consider the arguments of a range of disciplines and paradigms.

In material on regional governance, institutions and economic development, a number of theoretical approaches have been applied which owe their origins to American studies. Although some of these translate well to the European environment, including the organizational theories of DiMaggio and Powell, others are less able to travel successfully. A good example of this problem has been demonstrated by Wong (1999, chapter 4) who shows that urban regime theory contains predictions that do not do particularly well once they have crossed the Atlantic.

Other researchers have used developments of institutionalism/network theory, combining aspects of organizational theory with traditional themes in political science to examine the evolution of partnerships of organizations and authorities. The increasing concern with the competitiveness of small and medium enterprises (SMEs) and the promotion of intelligent regions in the (re-)generation of the economies of particular areas has been particularly popular. The literature on SMEs often places institutional thickness and capacity at the heart of the analysis of the economic development process, reflecting a preoccupation with a paradigm popular in the 1980s (Macleod 1996).

In discussing multilevel governance, a growth industry in its own right within politics, the “actor-centered” approach that specifies the role of particular individuals and institutions in the decision-making process (Marks et al. 1996, 346) has frequently been adopted in explaining some of the developments within Europe. In contrast, at the national level, the “power-dependence” approach has been applied to aid understanding of the relationship between central government and sub-central public bodies (Rhodes 1988). To an extent, the “policy network” approach addressed by such economists as Halkier (1999) goes some way toward highlighting the associations between these two theories in its recognition of the importance of a multitude of actors exchanging information, expertise and other resources at both the national and supra-national (e.g. European levels).

With the apparently contradictory movements towards both greater powers for supra-national bodies such as the European Union on the one hand, and enhanced devolution to sub-national levels on the other, the theme of this set of learning materials will become ever more crucial. A better understanding of the underpinnings of successful regional governance structures and regional institutions will be an essential feature in determining the sustainable development of communities across the developed world, and of Europe especially.

3.2 Partnership and Regional Development

Over the last two decades, it has become increasingly apparent that to promote the development of a region requires not only intervention from the state at the supra-national (e.g. European, national, or sub-national/local level) but also reliance on more than one particular agency. Regional economic development is

no longer considered the responsibility of just one organization, be it central government or a regionally-based development agency or organization. Instead, a range of institutions have become involved, some of them local, some regional, and others again acting on behalf of national or European institutions.²⁸ In the main, these agencies work collectively in partnerships or networks on a more or less regular and formalized basis, and many of them will be involved in partnership arrangements with private sector organizations and actors. This is in contrast to the 1970s and 80s, when regional development usually involved one agency deciding the appropriate strategies and undertaking the necessary steps to implement such initiatives. As the millennium approaches, regional development bodies appear to be essentially networked organizations, achieving their objectives by working in partnership with other public and private actors.

Given this background and the emphasis put on trust and cooperation in industrial and regional policies, one can see why it is consistent with the political economy of the current period that partnerships have become the preferred mode of regional development. Indeed, the partnership approach is perceived as being so favorable that any self-respecting development agency adopts it as an integral part of its mode of operation. It could be argued that this form of delivering regional economic development activities has come to be hegemonic simply as a consequence of its having become ubiquitous. The mantra-like status of partnerships may obscure the fact that operating through them could involve disadvantages (Halkier et al. 1999; Danson et al. 1997).

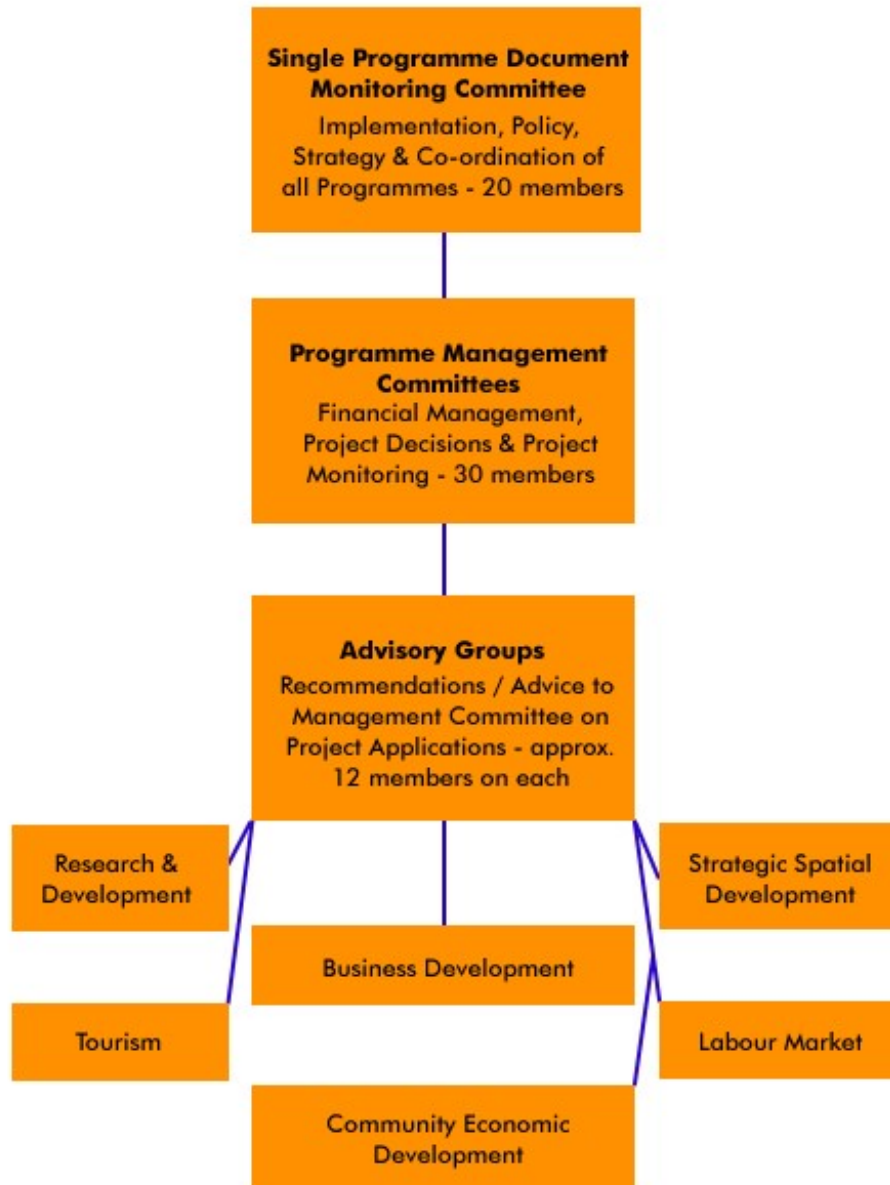
A more balanced view of regional development is needed. Just looking at the possible reasons for engaging in partnership arrangements would seem to suggest the need for caution. Building consensus and pooling resources to ensure coordinated efforts and efficient implementation will in many cases entail very real advantages, and may well be an important part of the real reasoning behind the growth of the networked development agency (Halkier and Damborg, 1999). But it is also clear that the current popularity of partnership arrangements is rooted in the specific historical circumstances of the last decade. The decline of central government regional subsidies that fueled the growth of bottom-up initiatives into an uneven web of regional and local development organizations, and the 1988 reforms of the Structural Funds, made partnership a general requirement in European regional programs. In addition to this decline, public-sector bodies with limited resources have been constantly searching for ways of enhancing their capacity to promote development. Meanwhile, the experience of the *Third Italy*, where consensual networking appeared to be the secret behind a thriving regional economy, has been well publicized. It is easy to see why partnership is construed as the new panacea. The motives of a development agency for linking up with other public and private bodies may be a combination of push and pull factors: on the one hand the search for functional advantages, on the other hand a constant quest for additional resources from other public and private actors.

There are two aspects of partnership which can be highlighted. First is the question of the motives and interests of the partners involved. These can be expected to differ between public and private actors and various tiers of government, and between divergent economic interests, different time perspectives, incompatible strategies, and territorial politics. These differences could all make it difficult for partners to gain the potential benefits of collaboration. Second, once partnership arrangements have been established, the question of their consequences for the participating organizations arises. The short-term effect for most participants is, they would hope, access to additional resources, and perhaps synergies in delivery and monitoring. However, as the links and associations between the partners become institutionalized, there are questions over the influence the participating organizations will have on each partner in the medium to long term.

Cameron and Danson (1999) have argued that by looking at partnerships and networks among agencies and institutions within a region from the perspective of organizational theory, using Scotland as a case study, insights can be gained into how these bodies are affected by new forms of cooperative governance. Exploring especially the effects these new forms have on development bodies and the ways that partnerships may challenge traditional perceptions of the advantages of both regional development agencies (RDAs) and networking leads one to see that there is a possibility of significant problems for these institutions and their political sponsors.

²⁸The emphasis on the European experience follows from the particular institutional and political environment on this continent. Because the member states of the European Union operate neither as a single entity - as a political body or nation state, federal or otherwise - nor as a set of totally independent countries, the paths of evolution of their institutional structures of governance can demonstrate a range of experiences. They each are restricted by the overall regulatory framework of the European Union, but they have acted as a laboratory for alternative forms of institutional intervention in the regional economy.

**FIGURE 3.1: Committee Structure
1997-99: Strathclyde European Partnership**



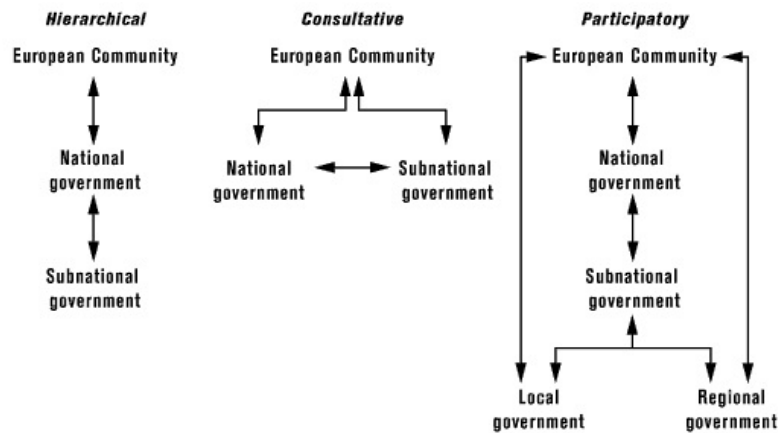
Others, in their analysis of the process of consensus building and strategy development, highlight the importance of communicative aspects of regional development activities. Jud and Steiner (1999) do so in considering recent experiences in the Austrian region of Styria.

By exploring the workings of partnerships in the English context, Wong (1999) has questioned some of the central assumptions of urban regime theory about the role of private and public actors in partnerships. She has undertaken extensive analysis of the views of development practitioners in the organizations involved in regional and urban economic development, and raised doubts about urban regime theory itself. In doing so, she has also confirmed the need to consider the particular economic, political and social environments within which governance structures and institutions operate.

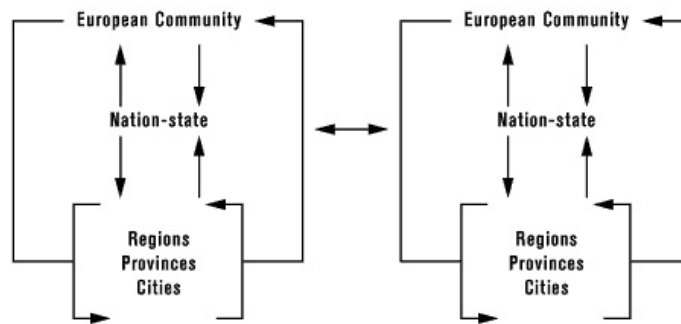
3.3 Networking and Regional Governance

Across the European Union, if not the developed world, over the past two decades there has been an expansion in the reliance on joint actions between institutions and between different levels of government to address many of the issues facing contemporary society. Looser than many formal partnerships, and often based on perceived mutuality of problems and policies, local and regional organizations increasingly have been coming together to address issues that face them individually and collectively. The association of traditional industrial regions (RETI) was an early example of this in the European Union, with joint intelligence and lobbying efforts funded through its member councils and authorities. Sector-specific bodies have been created with similar remits, one of the best examples being MILAN - the network of European regions involved in the vehicle industry.

In a national context, such associations have been long established. One example is the Convention of Scottish Local Authorities (COSLA), which has provided a platform for debate and the defining of common agenda and best practices. In Germany, the Federal Ministry for Spatial Planning, Building and Urban Development has prompted the construction of eleven city networks under the ExWoSt program over the period 1994-97 (Eser 1997). However, although these organizations and initiatives are fairly formal structures, the reality for many networks is that they are often ad hoc ways of addressing the problems of policy coordination, destructive competition among agencies, or a lack of institutional capacity at the local or the regional level. Improving accountability, albeit often indirectly, and adopting an integrated approach to policy administration and delivery are two of the main areas where networks have been embraced. Rhodes (1986) and Leonardi and Nanetti (1990) have explored some of the possible forms of relationships among the supra-national state (the European Union), the nation state, and lower levels of governance. (see Figure 3.2)



Different forms of EC state - regional/local authority relationships
(source: Rhodes, 1986, page 46)



Linkage networks for subnational governments after the creation of a single market (source: Leonardi and Nanetti, 1990)

Figure 3.2

By considering the practices and experiences across a range of very different environments it is possible to examine the role of looser governance structures. For instance, using an institutionalist framework Halkier and Damborg (1999) explore the attempts in North Jutland to enhance the patterns of business development support by the matrix of agencies in the region. Considering the developments there, they suggest how this networking approach could be applied to the study of regional governance in other parts of Europe.

In an area trying to come to terms with a poorly developed governance structure, Kafkalas and Thoidou, basing their work on the case of Central Macedonia, assess the importance of European structural funds for the emergence of specific RDAs. They have analyzed the significance of the competitiveness of SMEs and of the gradual establishment of RDAs in the promotion of regional intelligence, and so place institutional thickness and capacity at the heart of the economic development process.

The United Kingdom, the most centralized state in western Europe, presents a live experiment in significant changes in governance within a country. Britain has been undergoing [the devolution of power to a Parliament in Scotland](#) - 300 years after Scotland agreed to a union of parliaments with England - and to regional assemblies in Wales and Northern Ireland. The possibility also exists for devolution of power to regional assemblies in the English regions. Garside, among others, has critically examined the present plans for new forms of regional governance in the constituent parts of Britain, contrasting the proposals for Scotland and Wales with those for the English regions. Basing much of his discussion on the importance of democracy and inclusion, he points out the key role played by networks in the success of the Celtic nations, in comparison with the limited devolution existing and promised for the sub-national parts of England. The recent edited volume by Newlands and McCarthy (1999) is one of the few but growing attempts by regional scientists to address the economic implications of such developments; till now they have tended to be the domain of political scientists and commentators.

Bennett and McCoshan (1993) have suggested a typology of networks (Figure 3.3) which describes a range of relations between agents at the local or regional level. As they note, the networks A-D are derived from management science, and each has advantages and disadvantages in delivering economic development activities efficiently and sustainably. The introduction of the fifth form, E, is meant to be flexible and responsive to the needs of different agents.

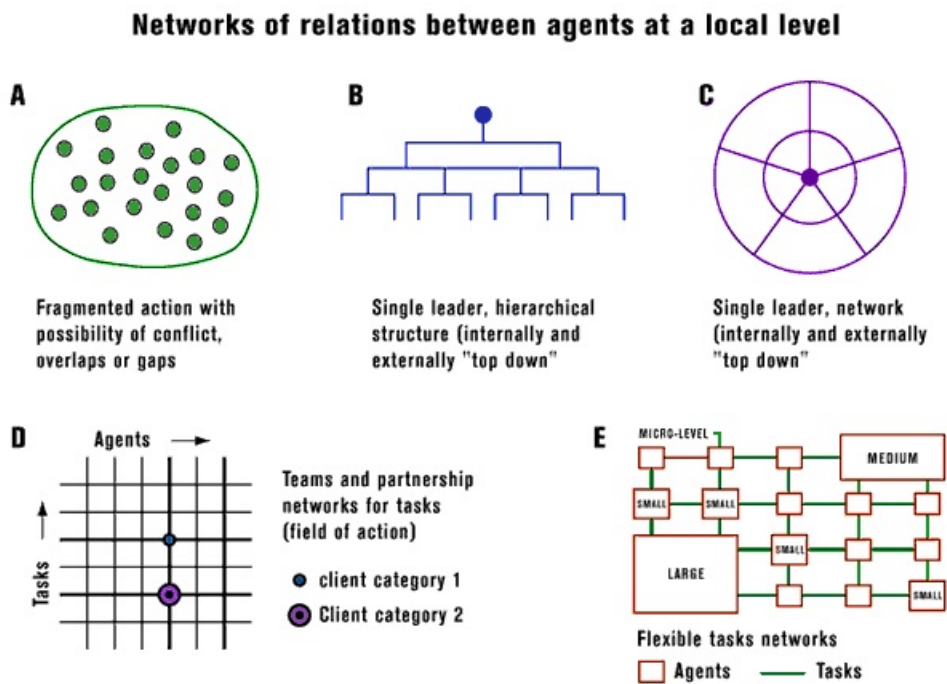


Figure 3.3

Two Swedish researchers, Jensen and Leijon, have adopted a very different approach to the study of developments in regional governance structures. Drawing from experiences in West Sweden, they apply

rhetorical analytical forms to describe the social construction of this particular region, explaining how some of the actors used imagery and “persuasive storytelling” to create a region. Their examination of regional networks and institutional landscapes, the creation of artificial regions and the inevitable consequent inconsistencies with perceived realities provides a stimulating way of considering the importance of regional structures in the development process. They stress the significance of political dialogue in persuading and forming the debate over not only the nature of governance institutions but also the very existence of regions themselves. This raises the age-old but critical question “what is a region?”, a problem for regional scientists that has presented itself at various times and with varying strengths over the decades.

3.4 Regional Development and Multilevel Governance

As demonstrated widely in individual country and continent-wide studies over the last few decades (see Yuill et al., 1998 for instance), the role of traditional central government regional subsidy programs has been gradually replaced by bottom-up development bodies and initiatives. The changing structure of regional policy throughout Europe has been assisted and encouraged by the increasing importance of the European Union system of governance, with the structural funding programs critical in this process. There is a need to identify and delineate the development of the governance structures in each country and in the European Union to understand and to explain the emerging pattern of change towards a multilevel system of governance. Such research is best conducted using a variety of applicable theories.

Since the inception of the [European Regional Development Fund \(ERDF\)](#), the role of the European Commission has become increasingly important in the development of the regions within objective areas. The impact of the European Commission’s method of stimulating regional development through bottom-up initiatives and programs has not only affected the assigned areas but also has had direct implications for national regional policy developments throughout the European Union. A similar process of change can be identified outside the European system. It may be important, then, to consider where the process of change originated. Has the change towards bottom-up regional policy been brought about by the desire of national governments to empower the regional agents and reduce their own direct role in regional development, and/or has the European model been accepted elsewhere as the most effective and efficient method of regional development?

The relationships between different tiers of government may be studied from a number of different perspectives. On the *European Level* the so called “multilevel governance” approach proposes that “decision-making competencies are shared by actors at different levels rather than monopolised by state executives,” and that it is therefore necessary to adopt an “actor-centered” approach that specifies the role of particular individuals and institutions in the decision making process (Marks et al. 1996, 346).

On the *National Level*, parallel arguments can be found in the “power-dependence” approach, which was developed to aid understanding of the relationship between central government and sub-central public bodies (Rhodes 1988). The multilevel governance and power-dependence approaches both identify the mutual dependence between different tiers of government based on their respective control of resources important for the development and implementation of public policy. Adding weight to the debates on “multilevel governance” and “power dependence” is the “policy network” approach. This approach also recognizes the importance of a multitude of actors exchanging information, expertise and other resources at both the national and European levels.

Discussion of the approaches that are implemented or can be implemented is continued at the *Regional Level*. Analyses of the recent suggestions for change in the electoral system have evoked debate over whether democratic principles and regional government are necessarily a more beneficial system for the effectiveness and efficiency of regional policy, or whether current agents may in fact be superior.

Consideration of the work of several academics allows an understanding of how the debate has developed and gives a thorough explanation of policy implementation at a number of levels. For example, in his evaluation of Norwegian regional policy Bukve notes the change from a system in which there was a high degree of autonomy for the political bodies at the county level to one in which governance, rather than government, has become increasingly evident. By doing so, he demonstrates the need to look at the particulars of a region’s environment. Because Norway is not a member of the European Union, Bukve’s work lends insight into governance across the European continent. Likewise, Halkier (1999) has considered the consequences of

recent radical change in Danish regional policy toward regional governance and empowerment and shown how experiences can differ even between near neighbours - such as Denmark and its Nordic associates Sweden and Norway. And Downes (1999) has assessed the Austrian system and the way in which joining the European Community has affected the regional policies and actors of the strongly consensus-oriented political environment.

3.5 The links between networking and partnerships

As is apparent from above, within the regional economic development structure of the late twentieth century, there appears to be a dominant partnership model approach that stresses the possibility of realizing synergies and capturing positive externalities through formal networking. In many regions, the form of institution favored to address regional market failure, the RDA, is being encouraged to relate more closely to the other economic actors in regeneration and restructuring. Some have argued that this points them toward a role as a facilitator, enabler or catalyst in the regional economy (Morgan 1998), rather than the multifunctional all-embracing organization of the 1970s. In the following section, the role of RDAs in differing regional governance structures is analyzed in more detail. As an introduction to that discourse, we consider below the links between networking and partnerships.

There is an essential transmogrification implied in the incorporation of the RDA into such partnerships. Whether there are conflicts and disadvantages to these developments does not appear to have been addressed in the literature. For instance, it has been suggested that the advantages of partnership include:

- Increasingly innovative policies and better operational decisions arising from dialogue and interaction among organizations with different responsibilities and perspectives on problems
- Increased continuity and consistency in policy within individual organizations as a result of the building of trust and understanding with others
- Resolution of conflict and disagreement through widespread consultation and involvement in decision making
- Coordination and integration of disparate actions and aggregation of separate budgets, to enhance policy impacts
- High level of strategic planning and decision making through shared agreement reached on essential needs and priorities (Danson et al. 1997)

To assess these claims, and especially the second advantage, suggests applying a theoretical framework appropriate to the analysis of organizations working in partnership and through networks.

3.6 Networks and Partnerships

Traditional research in organizational theory has tended to concentrate on intra-firm rather than inter-firm relationships; however, with the increased interest in networking (Nohria and Eccles 1992) and indeed partnership, it has become necessary to consider the relationships between organizations in a more structured way. In addition, the impact that the external (networking) environment may have on the structure, culture and functioning of the individual organization should have increasing importance as decentralized decision making, indigenous development and collaborative working in regional economic development become more common (Cooke and Morgan 1993; Garmise and Rees 1992; Mackintosh 1997).

The Importance of Local Networks

A basic assumption of the relationships formed to provide a network is that the organizations in a network are mutually dependent upon resources controlled by each other, and that there are benefits to be gained by pooling their resources. Thus in network forms of resource allocation, organizations do not operate on an individual basis but relative to all the organizations in their network (Nohria and Eccles 1992; Cooke and Morgan 1993). In many ways the analysis of cartels and oligopolistic behavior is analogous to this.

Networks are the intricate links based on trust and reciprocal patterns of communication and exchange between producers and clients that are necessary to ensure economic capability and responsiveness (Grabher 1993).

Ideal networks enhance market and location decisions; in economic terms, they facilitate the externalities of decisions becoming internalized to the members. Networks mean that key agents have to work more closely together to fulfill the needs of those included in, and affected by, the network.

Networks established to deliver economic services are fundamentally local affairs (Bennett and McCoshan 1993). They depend upon the way in which businesses are served by local community and business leaders and elites, the way in which local networks perform, and the way in which participation in networks takes place at a local level. However, the character of local networks, their leadership and elites, are also fundamentally determined by the economic structure and layout of their economies, which in turn depends on the relationship of the local economy to the national and global economic system. As a result, different types of areas possess very different types of networks of relationships. For example, there are strong contrasts between older and newer industrial areas, between areas concentrated on urban settlements and those in more dispersed urban or rural areas, and so on.

The contrasts of networks between areas create very different possibilities for development. In some areas networks allow a strong positive lead to be taken which allows the rapid economic change and adjustment on which service quality is founded (Ricard 1997). In other areas, the absence of an effective network, or a network tuned to former circumstances, can be a strong inhibition to economic growth. Local networks thus can be strong supply-side factors that raise or lower the economic growth potential for different parts of the country (Bennett and McCoshan 1993; Doeringer, Terkla and Topakian 1987).

From Networks to Partnerships

Networks are the essential means for linking one group of agents to others whom they affect and are the mechanism for the exchange of information and services in support of business development. Beyond simple networks, partnerships require the commitment of the agents to work fully together. This means:

- Accepting long-term structures that work towards sustained commitment to change and achievement of quality
- Accepting an active commitment to changing the internal operations of each agent, and helping other agents also to change to achieve an improved system overall (WMEB Consultants 1995)

Hence networking alone is largely passive, whereas partnerships require active participation (Mackintosh 1992). Partnerships are based on firm agreements by agents to work together. They extend far beyond network flows of information to offer a system that ensures that the problem, or the client, is fully addressed. Partnerships can range from agreements between actors to work together toward a common end, to agreements which form a legal contract through which specific targets for performance are defined by the contracting parties. Over this range of possibilities the parties may act as relatively equal partners, but frequently the partnership is not equal. In some partnerships, the arrangement is more important to one party than to others, or performance is mandated or coerced by one party on another (frequently through financial powers). The description of the need to build up working relationships based on trust and cooperation is represented in the accompanying Figure 3.4.

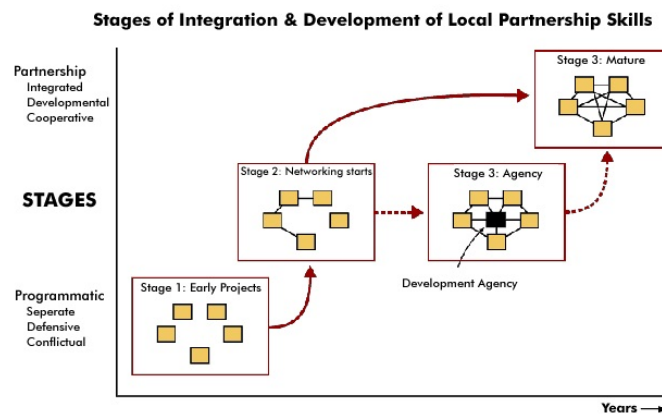


Figure 3.4

Networking and Partnerships in the European Context

The European Commission is considered to be one of the main driving forces in the development of partnership, and therefore in networking behavior, with the aim of achieving the goal of European integration and cohesion (Bennett and Krebs 1994). As a means of encouraging this behavior many of the Commission's initiatives and programs have a pre-requisite that participating organizations must be involved in a partnership or network (Cooke and Morgan 1993). As highlighted earlier, this is evident in the Commission's arrangements for regional policy funding and for accessing structural funds. The aim of these arrangements is to harness the energy, skills and resources of the key actors in the regional development environment and to develop and implement solutions to increase cohesion across the European Union. Given the pre-eminent position of the Strathclyde model in the evolution of this partnership form of delivering structural funds in the European Union (Danson et al. 1997), sections 5 and 6 introduce some consideration of the model in the analysis of the micro- and meso-levels of regional governance.

3.7 Summary and introduction to the following sections

This section has given a brief introduction to the major themes of "partnership and regional development," "networking and regional governance," and "regional development and multilevel governance" and the links between the different levels of analysis. In the following chapters, this analysis is extended, first through an exploration of the RDA under different models of governance and then an examination in greater detail of some aspects of these themes. In each case the material will be illustrated by application of the theories presented to the experiences in particular regions, especially the Third Italy and Scotland.

4 Economic Development, Regional Governance and the Role of Development Agencies

4.1 Introduction

Promoting the opportunity to develop the economy more effectively has always been a significant element in the debate over the future governance of individual regions, especially of regions facing endemic problems. Such factors as high unemployment, low relative incomes and gross domestic product (GDP), net emigration, the collapse of a region's traditional basic industries, and domination by nonlocal capital have all been cited as reasons for seeking increased indigenous control or other forms of intervention in a regional economy. However, for many regional economies, with an open economy dependent on the national, continental and world economic forces (McGregor et al. 1997), there is obviously a constrained policy environment. This inevitably limits the ability of a regional administration to achieve macroeconomic objectives by following traditional policies and ways of delivering such policies.

Further, and even within these strictures, for many communities in the European Union (for example, Scotland under the new devolution arrangements)²⁸ regional levels of governance will have available only a limited range of economic powers. Control over fiscal, economic and monetary policy will be reserved for higher levels. Similarly, the regulation of competition, intellectual property, and research councils will remain under the power of the central government of the United Kingdom, as will policies pertaining to broad aspects of transport, energy, the welfare state, trade and assistance to industry. The abilities of regional levels of governance to intervene at the Scottish level under these constitutional arrangements are not very different from the powers and instruments available to many regional governments across the developed world.

Because the particular history and geography of a country or region are important in determining the effectiveness and efficiency of the firms, markets and policies in the country or region in the present, it is always necessary to have a good idea of such background information. The extended endnote below²⁹ presents

²⁸The House of Commons, 1997

²⁹Scotland has been an independent sovereign country for much of its history. However, in 1603 the Crowns of Scotland and England were united when James VI of Scotland also became James I of England upon the death of Elizabeth I of England. In 1707, the Act of Union finalized the political union between Scotland and England, which followed legislation of that year which united the parliaments of Scotland and England. This Act, passed by the respective parliaments, provided inter alia for the Protestant succession to the throne, for uniform taxation and for free trade between Scotland and England. The legislation preserved the separate Scottish legal, education and ecclesiastical systems. The 1707 Act of Union had a turbulent aftermath. It led to the Jacobite Rebellions under which attempts were made to regain the British throne for the House of Stuart. This ended with the Battle of Culloden, the last battle to be fought on British soil, in 1746, when the uprising was crushed with great brutality.

Immediately after the Jacobite Rebellion came the Age of Enlightenment, an outpouring of philosophical thought, literature, inventions, architecture and industrial advancement. A critical personality in this period was Adam Smith, whose book *The Wealth of Nations*, published in 1776, was a major landmark in the history of economic thought. The period also witnessed the beginnings of the age of Watt and others, which provided the basis for the transformation of Scotland from an agrarian economy to the first industrialized nation in the world. There were also advances in agriculture and textiles, and an expansion of trade in the raw materials needed for Scottish heavy industry.

Although there is a long history of mining of coal and lead in Scotland back to the 13th century, the real development of industry started only after 1750. From this time onwards, increased trade, large scale immigration to the Central Belt of Scotland from the Highlands and Islands and from Ireland, and the introduction of major new industries significantly raised the tempo of Scottish economic life. Clydeside, centered on Glasgow, became the world leader in the production of coal, chemicals, metals, engineering, shipbuilding and textiles, making it the most prosperous region in Britain. Dundee secured a position as a center for the processing of linen and jute, while Edinburgh expanded on the basis of the indigenous financial and legal sectors, and established itself alongside Glasgow as a major center of administration and the arts.

These economic changes led to changes to Scotland's social structure; the population increased from 1.1 million in 1707 to 1.6 million in 1800 and almost 4.5 million by 1900. However, this was accompanied by some of the worst aspects of poverty and deprivation the world has ever witnessed.

Development continued apace in the nineteenth century, particularly in heavy industry, coalmining, shipbuilding, and engineering. The economy also diversified into medicine, science, accountancy, banking and commerce. Its educational provision and achievements were outstanding by any measure, paradoxically leading to high emigration as Scotland exported its skills and labor force. As described in section 6 below, this rapid advance and inventiveness also sowed the seeds of twentieth century decline. While there was some restructuring after World War II, this was not enough to prevent further decline and peripheralization.

Building on Scotland's surviving institutions from the Act of Union, an increasing degree of administrative devolution of power was promoted throughout the twentieth century. Nationalist pressure, however, continued to grow culminating in the

a very brief description of the development of the Scottish economy and institutional structure.

Dow (1997) argues that devolved governments have greater flexibility to intervene in regional economies than the problems mentioned above may suggest. Indeed, some researchers claim that the success of regional governance structures in economic policy terms should not be measured by the level or financing of public expenditure in their region but rather by their impact on the rate of economic growth and development locally (Newlands 1997).

Increasingly over the last two decades, attention has been turned to what Doeringer (1987) called the “invisible factors in ... economic development” as the crucial areas for intervention. In this vein, Porter (1990) has argued for the significance of investment and innovation in explaining the promotion of competitiveness and productivity, highlighting “R&D, learning, modern facilities and sophisticated training” as key factors. More generally “new growth” and “endogenous growth” theories follow the Schumpeterian tradition of stressing the role of competition in creating dynamic change in the economy. Today, an alternative approach that stresses the specific comparative advantages of areas can be reconciled with these growth theories where agglomeration economies built on trust, cooperation and innovation are present.

Similarly, the significant role of an infrastructure conducive to innovation and development has been long associated with the growth pole theories of Perroux. Having fallen out of fashion in policy and research terms in the 1970s, growth poles are being resurrected in the form of clusters and networking; the underpinnings of the successful regional economies of the Third Italy and Baden-Württemberg (Whittam 1997). Indeed these comparators have been cited by the Secretary of State as the way forward for Scotland (Press Release, February 1998).

In all these competing theories of regional growth, a rationale can be identified for a regional government intervening in the economy to establish conditions and institutions to promote economic development. The decline of Keynesian demand management policies and the re-emergence of supply-side concerns has led to factors which affect costs of production, competitiveness, and to the creation and adoption of technologically advanced methods of production (Newlands 1997). In these contexts, regional governance structures can be argued to have the potential to have significant impact on industrial and economic development by introducing and customizing policies in such areas as training, technology, venture capital, new firm formation and the ownership of industry. However, as McGregor et al. (1997) and Newlands argue (1997), intervention will not lead to automatic improvements in such circumstances; rather the need for a policy regime appropriate to the needs of the particular region’s economy can be critical, as the strategies of the national state may be inappropriate.

Many commentaries on specific regional economies tend to stress the uniqueness of the political and institutional environment of that community; in Scotland, for instance, for many years it has been argued that economic development policy has been determined within Scotland by Scottish institutions (McCrone 1994; Danson et al. 1990). In many regions facing endemic structural economic problems, a distinctive element in the evolving picture of their own environments has been the role of the regional development agency (RDA). Within the regional governance structures, it is often to these established institutions that the regional or national parliament will look to deliver key policy options and strategies. This section of the learning materials considers next the typical structural problems of the regional economy, then in parts 4.3 and 4.4 the rationale for development agencies, followed by their functions and performance. Guiding the deliberations over what institutional forms and configurations could be adopted, it is argued here, should be four key principles: accountability, subsidiarity, sustainability, and integration/inclusion. These are defined in part 4.5. Applying these in part 4.6, we propose how RDAs might be evaluated; part 4.7 considers the role of partnerships. The concluding part proposes how the development agencies should be reformed to operate more effectively to meet the aspirations of the community in the region.

re-establishment of the Scottish Parliament in 1999. Although the Parliament has limited economic powers, and less power than state legislatures in the United States, further moves are expected in the coming decade. The dynamism in the Scottish constitutional position suggests that again it is an important indicator of the potential economic implications of political and governance changes. In many ways Scotland has diverged from England over the last quarter century in its political thought (a consensual and corporatist culture has coming to dominate Scotland, taking her closer to the European norms) and in its linkages with the rest of the European Union market. These two developments have made Scotland a critical test case in Europe for the adoption of North American policies and forms of intervention within an increasing embracing of a European social partnership approach to managing the economy.

4.2 The regional economy

For many regional economies, such problems have become endemic as high and persistent unemployment, net emigration, declining local traditional industries, a weak indigenous business establishment with low rates of new firm formation, and a dependence on external investment by multiregional or multinational firms. Together these factors produce a difficult environment for the growth and development of new enterprises, the attraction of R&D facilities, and the promotion of self-sustaining regional growth. Selective migration of the younger, more skilled, educated and enterprising members of the population will exacerbate such problems, instilling positive feedback mechanisms into the local environment and creating vicious circles of decline. Coupled with a reluctance to persevere with traditional Keynesian policies of demand management, restricted in the ability to adopt more interventionist strategies by politics or the regulations of the wider power blocs (nation, European Union, or equivalent), the move to supply-side policies has encouraged the foundation and reliance on RDAs.

4.3 Rationale for regional development agencies

Faced with these endemic regional problems and the need to intervene to address market failure, areas of the United Kingdom have begun to rely on the development agency approach to the promotion of regional restructuring. In the United Kingdom, with its long history of innovative policy development, the establishment of the Highlands and Islands Development Board and the Scottish Development Agency (in the mid-1960s and 70s respectively) and their survival through the Conservative governments of the last eighteen years have had much to do with the corporatist tradition in Scotland (Fairley and Lloyd 1995). They have also helped lead to the divergence of politics north and south of the border over this period (Brown, McCrone and Paterson 1996), and the consensus for intervention in Scotland (McCrone 1994). Many other regions around the world have followed this strategy and established their own RDAs.³⁰ Whether the Scottish Parliament empowers local authorities, reabsorbs responsibilities into the Scottish Office departmental structure, or continues with RDAs will depend as much on political perceptions of the agencies' potential as on objective study of their performance against these alternatives. It is to the rationale, structure and roles for the development agencies under alternative regional governance models that we now turn.

It has been argued that the increased interest in economic development initiatives has helped stimulate greater "bottom up" development and the development of indigenous potential, compared with many former policies that tended to be more dominated by "top down" concerns (see for example Stohr 1989). An important part in this process has been played by semi-autonomous institutions such as RDAs and the European Regional Development Agencies Association (*EURADA*).

An RDA can be defined as "a regionally based, publicly financed institution outside the mainstream of central and local government administration designed to promote economic development." In their studies of such bodies across the European continent, a model RDA is defined by Halkier and Danson (1997, 245) as a body that, first, is in a semi-autonomous position vis-à-vis its sponsoring political authority; second, supports mainly indigenous firms by means of "soft" policy instruments; and third, is a multifunctional and integrated agency, the level of which may be determined by the range of policy instruments it uses.

In the United Kingdom, RDAs have been seen as a method of reducing the level of localized market failure in accordance with and in support of the government's macroeconomic regional policy instruments and objectives. Calling on the literature in this field (Haughton and Peck 1991; Lipsey 1983; Pearce 1977), Fairley and Lloyd (1998) explore the principle of market failure as it applies to development agencies, and again record how the Scottish agencies tended to widen the definition to allow a broader degree of policy intervention than the government envisaged. They also incorporate the evolving concept of "government failure" as a reason posited for restricting intervention; by extension the concept would lead one to support the devolution of powers to a quasi nongovernmental body more oriented to the needs of the market.

³⁰Halkier, Danson and Damborg, eds, 1998, *Regional Development Agencies in Europe*, London: JKP is a collection of essays that elaborate on this topic.

Figure 4.1 Growth strategies and policy areas		
Strategic orientation	Resource	Policy area
Traditional	Advice Infrastructure	Investment attraction Access to grants General factories
New	Advice Finance Infrastructure	General management Markets Production/technology Equity, loans, etc. Science parks, etc. Training
Other	Finance Infrastructure	Own grants Grant administration Land renewal

Figure 4.2 A typology of regional development organizations
Model RDAs
Potential RDAs
Non RDAs

Figure 4.3 Model RDAs : subgroupings
<ul style="list-style-type: none"> • relatively large organizations with mixed-traditional policy profiles • medium to small organizations with mixed-new profiles • relatively small organizations specializing in new policy areas

Danson, Lloyd and Newlands (1993) argue in support of development agencies as the most effective tool for addressing such local market failures as risk aversion in the financial sector, poor market information, externalities in the provision of infrastructure and training, and problems associated with rapid growth and technological change. Their argument rests on several advantages RDAs seem to hold over other methods of policy implementation that have been considered, such as local authorities, central government departments, and private sector-led bodies such as the English UDCs (Urban Development Corporations).

Able to intervene and interact with the economy at the most appropriate jurisdictional level (Armstrong 1997), regional agencies can bring substantial resources to bear on problems of local economic development by combining regional, industrial and training policies and resources on specific projects. They represent the

manageable “bottom-up” alternative, avoiding the bewildering maze of local initiatives now present in many regions, but they are also flexible and receptive to the specific needs of the indigenous industry within their regions. A significant problem in the proposals for the RDAs in the English regions (DTER 1998) is their failure to recognize the difficulties caused by the continued existence of the plethora of bodies and programs in each region; in the Scottish cases, such additions to the institutional infrastructure were introduced after the Highlands and Islands Development Board and the Scottish Development Agency were established. A number of responsibilities which otherwise may be split between different departments or quasi-government agencies - such as the provision of sites, attraction of industry, environmental improvement, sector strategy, and urban development - could be located within a single organization to reduce costs and realize synergies (Moore and Booth 119). In the words of the Trade and Industry Committee, local enterprise companies in Scotland (LECs) are ‘able to deliver national schemes and programs flexibly, in response to local needs and circumstances’ (Trade and Industry Committee 1995).

Operationally RDAs frequently combine area and sectoral strategies as opportunities arise, and offer comprehensive business services, both functions that could be more difficult to deliver if they were spread across departments and agencies. More crucial perhaps, as they are at arms’ length from government, RDAs can develop a degree of operational freedom and credibility that regional departments of government may lack. They may be able, therefore, to have potential leverage over significant private funds, representing a strong advantage that an agency will have over the Scottish Parliament itself. In times of high mobility of multinational capital, such compromises may be necessary to attract and retain jobs, incomes and technologies. As Halkier and Danson (1995) have noted, because RDAs work “outside the mainstream government,” they may be able to facilitate the pursuit of public policies without direct government intervention (1). This can make the development agency approach to regional economic development more acceptable to the full range of social partners, without necessarily undermining accountability.

Although RDAs can focus on the particular needs of the enterprises and labor force of their areas, they can also adopt a long-term perspective. Taking a strategic view can allow policies to be followed which are to the long-run benefit of the region, but which may be unpopular in the immediate period. Thus, relatively isolated from short term political intervention and maneuverings, RDAs should have the potential to restructure the economy in a planned way that would lift the development path of indigenous industry onto a higher level, achieving greater endogenous growth. It can be argued that distance from central government could well be fundamental to the success of such a strategy. Although the operating environment may be more closely attuned to the needs of local enterprise, a Scottish development agency can also instill a sense of regional ownership of economic development strategies while demonstrating a political commitment to the long-term growth of the economy as a whole. The potential to promote and encourage trust and cooperation through such an institutional approach can engender further virtuous circles of growth and development, as described below, in ways that a regional parliament and local authorities cannot.

4.4 Structure and roles of the development agencies

In many ways the specific roles and functions of the Scottish development agencies are less important than the balance between their objectives and their priorities. There is a broad consensus over the macroeconomic role of government and over the detailed needs of the Scottish economy. The most significant debate involving RDAs is over how expenditure should be targeted and on which sectors and areas it should be targeted. Yet much of the discussion threatens to be concerned with who should have the powers of intervention. In assessing the present structure and performance of the RDAs we hope to illuminate this debate.

The RDAs for Scotland, Scottish Enterprise ([SE](#)) and Highlands and Islands Enterprise ([HIE](#)) have responsibility for the integrated delivery of economic and business development initiatives, the provision of training and the implementation of measures to secure the improvement of the environment in Scotland. According to a concept long championed by the organization for Scottish trade unions - the STUC, SE and HIE represent a radical initiative within the Scottish tradition of regional planning for economic development by bringing together the key factors of capital, labor and land.

SE and HIE aim to stimulate self-sustaining economic development and the growth of enterprise, secure improvement of the environment, encourage the creation of viable jobs, reduce unemployment, and improve

the skills of the Scottish work force. The delivery of the integrated enterprise and training services is subcontracted by SE and HIE to a network of LECs (Fairley and Lloyd 1998). The function of LECs are to co-ordinate the provision of the supply side of the economic infrastructure of their areas, addressing market failure. They provide the delivery framework for the specific services associated with training, enterprise and business development and environmental improvement. At a higher level, SE and HIE “provide strategic policy guidance and expert advice to the LECs on individual economic sectors; undertake major projects or research activities which extend beyond the areas of individual LECs; provide individual LECs with a range of central support services which include administrative, accounting and property services; undertake marketing and inward investment programs for the areas in question; undertake major environmental improvement and land renewal programs, in consultation with the LECs involved; and monitor the progress of the LECs in implementing their plans and achieving their objectives” (Fairley and Lloyd 1998). It should also be noted that HIE has been given a social aspect to its developmental responsibilities, raising questions over the potential imposition of an all-Scottish departmental approach to economic development. Such an approach would be supported by a framework that categorizes the Highlands and Islands into different priority areas: “fragile remote areas,” “areas of employment deficit,” “intermediate areas,” and “Inverness” and its hinterland.

Following the tendency for corporatist and consensus politics and policy institutions to be more acceptable in Scotland, as argued earlier, these arrangements are clearly and distinctly Scottish and offer the potential for securing an integrated development framework in each area. Before discussing whether any of the functions of the RDAs should be centralized to the new Parliament (in particular the headquarters of SE and HIE) or brought under the control of the local authorities (the LECs), two key dimensions need to be explored: partnership and principle.

A key element to the operations of the LECs and the RDAs is that they work in partnership. This is especially relevant in discussions over the future of the development agencies under a devolved Parliament. They are not the “all singing, all dancing” monolithic multifunctional agencies envisaged in the early 1970s. SE and HIE must work with other organizations, including local authorities, government departments, academia and training bodies, the community and voluntary sectors, as well as the private sector, to develop and deliver such things as skills training, business development and inward investment. This is important, but it is also important that other organizations in turn recognize that the RDAs themselves bring a good deal of experience and expertise to local and regional development strategies and programs. Whatever configuration of powers and institutions is proposed, partnership will be an essential feature not only because it is rational to share best practice and to realize synergies, but also because the European Commission insists that across the European Union, Structural Funds be delivered through the Scottish European Partnership model (Danson et. al 1997).

4.5 Principles

• Accountability
• Sustainability
• Subsidiarity
• Integration and inclusion

In the assessments of the roles and performances of the RDAs in Scotland, a number of areas of criticism have been raised over the years. It has been difficult to discern any scientific approach to an evaluation of development agencies as such anywhere, though much has been written about their programs and strategies.³¹

³¹However see Chapter 1 of Halkier, Danson and Damborg 1998, for a discussion of this neglect.

To make proposals on the future governance and functions of SE and HIE in this critical vacuum suggests a need to return to first principles, and indeed an appreciation of the critical criteria against which the mode of delivery of economic development policies should be measured. In proposing these principles, we are calling upon a evolving field of literature that the Regional Studies Association, among other organizations, has debated and addressed in recent years. The four principles, which are inevitably interrelated, are accountability, sustainability, subsidiarity, and integration/inclusion.

That RDAs should be *accountable* is self-evident. Indeed this theme exercised the Scottish Affairs Committee when it examined SE and HIE in 1995/6 and, despite the heat generated around this issue, there were but few recommendations on improving democratic accountability. Others have thought otherwise; the Macfadden Committee, for instance, argued for the powers of the LECs to be transferred to local authorities, though the promised “bonfire of the QUANGOs” has not been as great an issue in Scotland as in Wales. What seems clear from the experiences with the Scottish RDAs and others elsewhere (Hughes 1998) is that control over the strategic long-term objectives and priorities of SE and HIE is necessary, but crucially there should not be day-to-day interference in delivery mechanisms and projects. These latter should be assessed through appropriate techniques and forms such as annual reports, monitoring frameworks, targets, and performance criteria.

Much of the debate over the effectiveness of RDAs in the European Union and of economic development agencies more generally across the world has concerned displacement. In other words, there is often a belief that such agencies merely shift jobs and economic activity from urban areas in need of revitalization to greenfield sites, and similarly from areas in need to other preferred locations. The trade-off between the efficiency and the equity of policy regimes therefore impacts accountability. In the evaluations of the “enterprise zone” experiment in the United Kingdom (where very specific locations were able to offer tax breaks and other subsidies to mobile manufacturing plants), much was made of the need to demonstrate a net benefit associated with local economic development efforts within the spatial context of the wider region.

The concern within the United Kingdom, and the European Union as a whole, over the promotion of the simple redistribution of plants by local, regional and central government policies has led to a series of regulations and controls over this aspect of policy intervention. These regulations appear to be in contrast with the United States, where authorities are more able to invite investment and so to persuade companies to change their location decisions. Within the United Kingdom there is a series of protocols over who can become involved in the attraction of mobile investment. Only central government agencies can talk to potential new investors in an area, and then only within tight guidelines. The range of inducements and assistance available to local and regional development agencies is likewise strongly constrained by higher levels of governance. Above the national controls lies the European Commission, which periodically sets the monetary and spatial limits and types of policy instruments allowed for nations under the Commission. This regional policy environment is far more constrained than are similar environments under the federal system of the United States.

Although certain states within the European Union have used tax incentives to attract firms, this form of intervention works differently from how it works in the United States. In most cases in Europe, local governments will not benefit directly from an increase in economic activity in their areas. Equalization grants (Kellerman and Schmidt 1997) and unified local tax systems mean that local income and property taxes do not follow firms from one local government jurisdiction to another. This means that there is less benefit in RDAs and other regional institutions involving themselves in the enticement of mobile plants. There are, of course, other advantages in the attraction of firms, most noticeably employment generation and the possibility of increased wealth creation for local companies through supply chains. In the United States, the federal system allows local municipalities to benefit from an enhanced tax base in both payroll and property terms, without having to subsidize firm relocation.

For development to be *sustainable*, it must involve the whole community and be accepted across all the social partners - TUs, small and medium enterprises, community and voluntary sectors. Operationally there are questions over the strategy of promoting a branch plant economy through inward investment at the expense of long-term indigenous development (Ashcroft and Love 1996). There is a degree to which the new dependencies created in the Scottish economy identified earlier are unsustainable and so unsuitable in the Scottish context. On this criterion, the role of Locate in Scotland, the inward investment body for Scotland,

would be called into question. A greater emphasis on clustering and networking is a potential change that could be made in Locate in Scotland's remit.

In the 1990s, *subsidiarity* was introduced into the evaluation of many policy areas. Following the approach of Armstrong (1997), we define subsidiarity here as taking and delivering policies at the most appropriate jurisdictional level. In other words, for certain functions the "local" level will be the most efficient level for the development of such things as training policies, while for other functions it will be the regional or Scottish levels. Training of software engineers would be more appropriately organized across the nation's universities rather than in the locality; there are important economies of scale and scope to be realized at all levels. The benefits of a flexible yet strategic and objective approach can be considerable and will undoubtedly occupy the boards of the development agencies and the committees of the Scottish Parliament; but these deliberations could be at the expense of efficient operations on the ground.

Finally, *integration and inclusion* have become important themes for policies at the end of the millennium. The need to maximize the value added by the Scottish economy and to capture the benefits of the higher functions of national and global corporations operating here in any capacity suggests that greater attention has to be paid to the linkages between plants, offices and services. The fixation of SE and other commentators on the leading high-tech industries of today is in many ways as destructive as the focus of debate in the past on steel, shipbuilding and coal. Thus traditional sectors such as textiles have suffered relative neglect because of their image as a declining industry, compounding their inherent conservatism and under-capitalization (Danson and Whittam 1998). The potential of such key areas of the Scottish economy is being dismissed in current SE plans for clustering despite the successes abroad in turning around older staple sectors. Locate in Scotland has tended to follow an implicit policy of promoting certain locations in Scotland (especially New Towns, suburban and greenfield sites, latterly in enterprise zones in Lanarkshire) to maximize the opportunities of attracting inward investment, regardless of the impacts on other markets - labor, training, and property for instance - and of the damage it causes the remainder of the country. Old industrial and rural areas, inner cities and peripheral estates have seen precious few manufacturing or service jobs directed their way in the past twenty years, and they have received minimal consideration of their access to the new industrial sites. This raises questions over the potential to enhance the role of structure plans in the economic development process, and over the limitations on such power that is threatened by the multinational agreement (MIA), being negotiated through the World Trade Organization. The agreement could restrict the ability of the Scottish Parliament to impose greater controls over the supplying and sourcing policies of inward investors.

The inclusion of SMEs in the development and the administration of economic policies has been a perennial problem in the United Kingdom. With a weak Chamber of Commerce system and with a dual economy that excludes most indigenous entrepreneurs from decision making within trade and employer associations, there is a real need to ensure that the interests of the mass of locally owned concerns are heard in the LECs and industry networks. Without a strong Scottish presence among the commanding heights of the economy and in the leading sectors especially, there is a danger that plans for improved networking and clustering will fail.³²

Much of the debate over integration has inevitably centered on the need to reduce social exclusion of the long-term unemployed, women, the young and ethnic and peripheral communities. While initiatives, programs and partnerships over the years have been established to address some dimensions of the lack of inclusion of many in society, that the scale and depth of inequality has continued to increase is without doubt. Broadening the remit of SE to encompass the social aspect of its developmental responsibilities, as HIE is charged to undertake, would go some way toward meeting this division. However, a multi-agency, multi-annual, and multifunctional approach will be necessary to overcome the obstacles to improved living standards for all in Scotland. Partnerships between local authorities, LECs, Scottish Homes, employers, trade unions and local communities are showing some promise of advancing the position of the excluded. Critically, LECs cannot have an implicit slogan of "our business is business" if such progression is to become fundamental and irreversible.

These principles suggest a need for the objectives, programs and actions of LECs, and others involved in economic development, to be transparent, as the production and criticism of structure plans must be. Further,

³²As discussed here and in Danson and Whittam 1998.

linkages between sectors, enterprises, markets, locations and organizations can be key to the improvement in the economy as a whole and to its parts. The Scottish Affairs Committee noted how crucial mandatory consultation by LECs of local authorities could be, at least to secure greater legitimacy for the enterprise networks in Scottish local governance and communities (Fairley and Lloyd 1988).

4.6 Evaluation and performance

As described in the introduction to this section, across the competing explanations of economic growth and performance are certain common features. The creation and encouragement of specialized skills and services, and the exploitation of research, technologies and innovation are considered to be critical drivers of a successful strategy for regeneration. Mechanisms to ensure the commercialization of science and technology from higher education and other institutions, the growth of new firms, the development of existing indigenous enterprises, and the transfer of technologies and processes into the wider economy are recognized as areas where market failure may demand significant intervention to secure advantages for the nation as a whole.

There has been relatively little analysis of the performance of development agencies since the merger of the former agencies and the training agency in Scotland. Much attention has focused on their individual programs and policies, and on issues of accountability. There have been calls for the boundaries of the LECs in the SE network to be coterminous with those of local authorities or subregional groups of authorities, all the more necessary given the abolition of the regional councils in 1996. Minor changes have been made towards reducing some of the anomalies caused by the lack of congruence among these boundaries, but further modifications could usefully be made to make the LECs' jurisdictions closer to both local administrations and local labor, industrial, and property markets and networks. Addressing the need for efficiency and legitimacy, SE has recently been involving a broad range of organizations and partners in a wide ranging and comprehensive review of its skills strategy. The full range of social partners has been consulted in this ongoing process and perhaps illustrates the potential for local, regional and Scottish consensus under the Scottish Parliament.

When the Scottish Affairs Committee proposed that this comprehensive skills strategy could be linked to sectoral targets in partnership with industries (Fairley and Lloyd 1998), they were perhaps pointing to the continuing need for such integration but using one of the characteristics of RDAs given above: their allowance of public policies to be pursued "without evoking the ghosts of interventionism or state dirigisme" (Halkier and Danson 1995, 1). Balancing this need to be acceptable to private enterprises with the need to be accountable has been recognized as of major significance more generally in Scotland, according to a report on selected members of the Scottish Council (SCDI 1997). Undoubtedly the desire to control QUANGOs and reduce the democratic deficit are strong factors in support of the Scottish Parliament's showing a closer concern with the RDAs in Scotland, but without losing the advantages of the form of intervention that QUANGOs provide.

The efforts to be more inclusive with regard to the development of skills reflects concerns over the lack of a central strategic overview of the problems of the Scottish economy and the problems of coordination described above. In other markets, such as land, continuing and expanding calls for reform lend evidence to the criticism that the RDAs have failed to change the culture of business and economic players. This stands alongside criticisms that their existing policies have been inappropriate with regard to such matters as employment creation and business starts.

Although employers in Scotland continue to be reluctant to meet the cost of training in modern times (Danson et al. 1990), there remains a strong economic argument in favor of employers being obliged to invest in training. Reconfirming a long-held commitment, the Scottish Trades Union Congress has argued that businesses should be required to fund a training program equivalent to 0.5 per cent of payroll costs (Scottish Trades Union Congress 1992). Meeting the training needs of a competitive economy suggests intervention in the market far beyond the proposed minimum wage and the maintenance of a flexible labor force. Reincorporating the trade unions and invigorating the employers' involvement will be two of the principal priorities facing the Scottish Parliament; given their restricted powers, the RDAs may prove the most efficient mode of intervention in the labor market.

In the literature on industrial clusters, networking and [learning communities](#), the issues of technology policy, innovation, new firm formation and the ownership of industry are all closely connected and provide prime

examples of the way in which the Scottish Parliament could in the long-term increase the dynamic efficiency of the Scottish economy (Danson, Lloyd and Newlands 1990; Newlands 1997). Yet there has been an undercurrent of concern over the feedback among these issues, and in particular over the implications of a reliance on foreign direct investment for the promotion of indigenous growth. A major concern of the Scottish Office and SE (and of their joint agency Locate in Scotland) has been the regeneration and diversification of the Scottish economy through the attraction of plants owned by corporations outside the United Kingdom, and especially corporations in the United States and the Pacific Rim countries. Much evaluation and analysis of the operations of the Scottish development agencies has focused on the effects of this attraction of inward investment to Scotland. It has been noted above that Scotland has become dependent for much of its dynamism on the overseas owned electronics industry, with all that entails for control over the economy and the potential for indigenous development. Recent indications are that these restraints should be addressed by seeking to locate major R&D plants here to embed these leading sectors into the Scottish industrial environment. This would certainly build on the comparative advantages of the economy, not the least of which are the high level of skills and the research facilities and traditions of the educational system.

However, whether a real Scottish presence in the new technologies - and beyond just the electronics sector - can be established without significant venture capital investment is doubtful. Well established arguments for a Scottish industrial investment bank are returning to discussions on the Scottish economy. While the financial sector in Scotland is significant in global terms, it remains less than effective in the provision of funds for indigenous enterprises. Dow (1997) especially has argued for the closer involvement of the Scottish banking sector in the Scottish economy, to address some of the limitations of the underdeveloped industrial structure and to redress past neglects. Without the industrial banks of such competitors as the German *länder*, the Scottish Parliament will have to be innovative in its use of indigenous resources; the land that invented investment and unit trusts should be able to mobilize such funds more effectively than at present. Many believed that the establishment of the Scottish Development Agency in 1975 would create such a financial vehicle; it took several years to conclude that its attention was focused elsewhere - primarily on being Europe's largest industrial landlord.

Concerns over the role of Locate in Scotland and of inward investment (Standing Commission on the Scottish Economy 1989, 47), despite the benefits of introducing new technologies, investments and management skills to Scotland, have focused on the deepening of the branch plant syndrome. Because most product and process innovations are developed in the plant in which they are first designed, and because there is little interregional transfer of such innovations, Scotland's low rates of new firm formation and innovation, and its under-representation in high technology growth sectors, is understandable. Employees at branch plants do not acquire the skills, business contacts or ideas to enable them to set up their own firms or mount a management buy out.

As Newlands (1997) argues, the Scottish Parliament could promote "a shift in the priority given to the attraction of inward investment and in the issues raised in Locate in Scotland's discussions with potential inward investors." Reflecting Dow's arguments, he suggests that stronger commitments could and should be sought on such issues as the location of higher corporate and research functions, technology transfer, and corporate recruitment, sales and purchasing policies. The Scottish Parliament might also pursue the suggestion that the Scottish public sector and financial institutions combine to establish a "White Knight" fund to strengthen existing Scottish businesses and enable those wishing to maintain their independence to resist external takeover (Standing Commission on the Scottish Economy 1989).

Without necessarily raising public expenditure and within the powers granted to the devolved Parliament, efforts could be made to strengthen cooperative networks further, and with them the culture and behavior of enterprises and people in Scotland. This would reflect both the economic underpinnings of clustering and the role political institutions can play in shaping economic performance more effectively by influencing the rules and norms of behavior (Hodgson 1989; North 1994).

4.7 Partnerships and Europe

The rationale for the establishment of RDAs as argued by researchers such as Danson, Lloyd and Newlands (1993) and Halkier and Danson (1997) is based on the idea that they are not only "the 'manageable' bottom

up alternative, avoiding the bewildering maze of local initiatives” but they also allow “for flexibility and receptiveness to the specific problems of indigenous industry within the region” (Halkier and Danson 1995, 1). Consequently, as has been noted, “a position outside the mainstream government *apparatus* appears to make it possible to pursue public policies without evoking the ghosts of *interventionism or state dirigisme*, and so to make it easier to adopt a *long-term perspective*, while the *distance from government* frequently generates an operating environment more closely attuned to the needs of enterprise” (Halkier and Danson 1995, 1, emphasis added). In other words, the perceived advantages of RDAs as a form of regional policy delivery institution could well be compromised by increasing moves to strong control over the day-to-day operations by a parliament. Similarly, whether the costs of closer involvement of the RDAs in partnerships and formal networks under both national and European Union programs would be worth bearing will depend on the benefits realized and the synergies released by these alternative models of economic development.

4.8 Conclusion

With restricted powers and a hostile and limiting European and global economic environment, the Scottish Parliament will face a need to balance aspirations against its capabilities. It will need and have a powerful desire “to do something” in economic development and do so more directly than institutions do at present, although Newlands (1997) has maintained that the growth function and the efficiency of intervention is significant already. There will be a strong temptation to reabsorb SE especially, and perhaps HIE, back into government, with some pressure to devolve the powers of the LECs to local authorities.

Given the rationale for RDAs and on the basis of the principles adopted here as applied to this form of intervention, we would argue that such moves should be resisted. There is a need for improved democratic control at all levels, and of better accountability of the strategic functions of the agencies particularly. It is a source of worry, therefore, that the Labour government has failed to legislate for the statutory inclusion of local authorities, trade unions and the community on the boards of LECs, European partnerships and equivalent institutions.

We would also not support the transfer of the powers of the LECs to the local authorities. After reorganization, many LECs are too small to deliver business and training services effectively and efficiently, while consortia or joint boards appear to be a second-best solution. Experiments in partnership, such as the [Ayrshire Economic Forum](#), the Ayrshire Engineering Group and the networking of the HIE Community Land Unit, illustrate the advantages of improvements to cooperation and trust across the economic landscape of Scotland. In many fields, especially business services and certain types of manufacturing, the agglomeration economies enjoyed by the metropolitan regions such as Barcelona, Frankfurt and Milan point to the need for a higher rank of development agency operating at least at the Scottish level. Calls for more revolutionary reforms threaten to be a distraction in the short term. Continuity and confidence will be fundamental to fulfilling longer-term objectives, especially at a time of devolution to the new Scottish Parliament, compensatory changes in England, European Union enlargement and reductions in Structural Fund support. The experience of successful regions elsewhere in Europe provides evidence that an evolution of the Scottish model of partnership is desirable, if the advantages of this tested approach are applied to economic links as well as to institutional relationships. Maintaining this model will involve the Scottish Parliament in radical intervention in the Scottish economy, especially if it incorporates the principles of accountability, sustainability, subsidiarity and inclusion into its activities. Anything else will appear to be mere posturing.

The experiences of the RDAs in Scotland have been examined under the current regime and under the new Parliament for two particular reasons. First, the Scottish agencies are the models for many of the development institutions across Europe and beyond. Scotland’s extended history of economic problems has meant it has been at the forefront in the establishment of and experimentation with many such initiatives.³³ Scotland’s experiences in the area can be seen as a good indication of the likely impacts of the moves to more catalytic and coordinating institutions. Second, and leading from this, the move toward greater autonomy for Scotland will allow a better analysis of the implications of securing control over differing forms of regional governance structures in a way that is not being proposed for the English regions.

³³See Morison, 198*, and McCrone, 196*, for comprehensive accounts of these developments.

Critically, though, the institutional arrangements in other parts of the world, especially the United States, are significantly different. In the United States, local municipalities may enhance payroll and property tax revenues by intervening in the location decisions of firms, and there are much looser controls over the policy instruments of their economic development agencies. This contrast in governance structures and policies can have profound implications for the effectiveness of regional economic interventions. It suggests that attention has to be paid to aspects of the regional economic environment other than cost and physical location factors.

5 Clustering, Innovations and Trust: The Essentials of a Clustering Strategy

5.1 Introduction

Many areas around the developed world are adopting the clusters approach to regional economic regeneration, with the United Kingdom-wide government Department of Trade and Industry (DTI) suggesting that this could be a key element in re-establishing the competitiveness of national businesses in the future.²⁸ As we demonstrate throughout this section, many of the regional initiatives in the United Kingdom and indeed in Europe, have originated in Scotland. There has been explicit reference to the Scottish approach to clusters in a recent DTI report. In this section we examine how Scottish Enterprise (SE), the development agency for Scotland, has recently launched a “clusters approach” for its key industrial sectors, arguing that if regions and nations are to be competitive in the next century they must be at the forefront of knowledge production. In order to compete, SE readily acknowledges that the information and ideas created and developed through clustering are reliant on strong partnerships and that if synergy is to be maximized then the whole process of the knowledge-based economy is dependent upon “working to build trust and a shared vision” (SE 1988a, 1). The envisaged strong partnerships will ideally consist of customers, suppliers, competitors, universities, colleges, research bodies and utilities; in other words, they will be a private/public sector mix. This is hardly surprising given the nature of the output produced, namely information, and the notoriety of the private sector for underinvesting in research and development. This underinvestment occurs because of the large element of fixed cost associated with the development of a new product or process, the inability of the innovator necessarily to reap the benefit of the innovation, and the uncertainty attached to whether a new product or innovation is to be successful. Given that knowledge production creates spillovers, and that much of the knowledge produced is tacit, and further, that new products and processes will benefit from critical commentary from all the players involved in a partnership, there is a spatial element attached to the idea of achieving a competitive advantage through the establishment of a “learning economy” within the globalized economy. The spatial dimension can be at a regional or a national level or indeed can transcend state/regional boundaries. Much of this is readily accepted within the existing literature and is acknowledged within part 5.2.

Of equal importance to the creation of new products and processes is the ability for members of a cluster to communicate efficiently. Because learning economies consist of partnerships, the ability for efficient communication between the members of a cluster is essential. Efficient communication will be assisted if the partners within a cluster can trust one another so that fears of one member appropriating the new idea or innovation can be reduced. The adoption of an appropriate institutional framework would greatly facilitate communication. This is recognized within the current literature on learning economies, but the nature of trust and cooperation is rarely discussed within this context. The ideas of trust and cooperation, however, are acknowledged to be the key to the success of some of the most well known regional economies of recent times, the industrial districts of the Third Italy being an example. We believe that if a regional development institution is to be successful with a clustering strategy, the nature of trust and cooperation within a partnership framework needs to be fully understood. We focus on the need for trust and cooperation, therefore, along with some brief commentary regarding the role of trust and cooperation within the industrial districts of the Third Italy in section six.

Within the European economies, there already exist examples of partnership frameworks that could be adopted to assist the success of individual regional clustering strategies. The most successful of these partnership institutions is the Strathclyde European Partnership (SEP). The SEP has received widespread acclaim (Danson et al. 1997) as a model for bringing together the key players - both public and private - for the delivery of regional economic development. In this section we examine the evolving partnership governance structures within Scotland at a regional and county level, highlighting both good and bad practice. We then conclude with policy implications and warning signs for the development of a clustering strategy based on the learning economy within Scotland.

²⁸This initiative is discussed further in section 8

5.2 Innovation and Learning

In its desire to establish a clustering strategy, SE is acknowledging the long-held view that European firms and industries are losing their competitive advantage in the main to the United States and Japan (CEC 1993). This loss is attributed in part to the lack of innovation within the European Union: “Among the factors having a major impact on the competitiveness of the Community economy, Member States point particularly to the following[:] ...inadequate assimilation of new technologies combined with failure to exploit properly the results of research and technological development, leading to difficulties in concentrating the production of goods and services in leading-edge and high value-added industries” (CEC 1993, 72). Yet conversely within the European Union, certain regional economies have been successful in terms of the usual economic indicators such as job creation and GDP growth. The reasons for success within these regions is partially attributed to the ability to be innovative. The role of knowledge and the innovation process has been identified by economic growth theorists as being a significant factor in endogenous growth theory and in accounting for the Solow residual (Boltho and Holtham 1992; van der Ploeg and Tang 1992; Scott 1992). The key component of the innovative process is the creation of knowledge, a point recognized by theorists and practitioners alike (see, for example, Gregersen and Johnson 1997; CEC 1993). The recognition of this point has focused attention on how firms, regions and indeed nations innovate. In researching this phenomenon, regional scientists have utilized the methodology of the evolutionary economists Gregersen and Johnson (1997), Morgan (1997), Grabher and Stark (1997), Storper and Scott (1995), Storper (1992 and 1995) and Lundvall and Johnson (1994). A major contribution to the discovery and utilization of knowledge is attributable to the institutional framework that evolves to facilitate the process. Institutions in this sense include both formal and informal organizations. Formal organizations include RDAs. An informal organization can be defined as “a social organisation which, through the operation of tradition, custom or legal constraint, tends to create durable and routinised patterns of behaviour” (Hodgson 1988, 10). The emphasis from the regional science perspective is that due to the nature of knowledge - much of it being *tacit*, it is not easily transferable - the system or region that creates it will develop the advantages associated with innovation.

Storper (1995) highlights the importance of what he describes as “untraded interdependencies” to firms’ use of knowledge. For Storper the interdependency arises because of the way technology is developed. Utilizing the evolutionary approach, he focuses on the path dependency nature of technological development. “Technologies, for one thing, are subject to a variety of user-producer and user-user interactions” (Storper 1995, 204). Where clustering occurs because of some commonality of technological development, “untraded interdependencies” arise, such as common coded language, norms, customs and practices. These common institutions lead to easier communication and facilitate trust and cooperation. Similarly, Freeman comments “Firms learn both from their own experience of design, development, production and marketing and from a wide variety of external sources at home and abroad - their customers, their suppliers, their contractors...and from many other organisations - universities, government laboratories and agencies, consultants, licensors, licensees and others” (Freeman 1994, 470). This list is not unlike those institutions identified by SE as making up a typical cluster: companies, customers, suppliers, utilities, research institutes, education (see Figure 5.1).

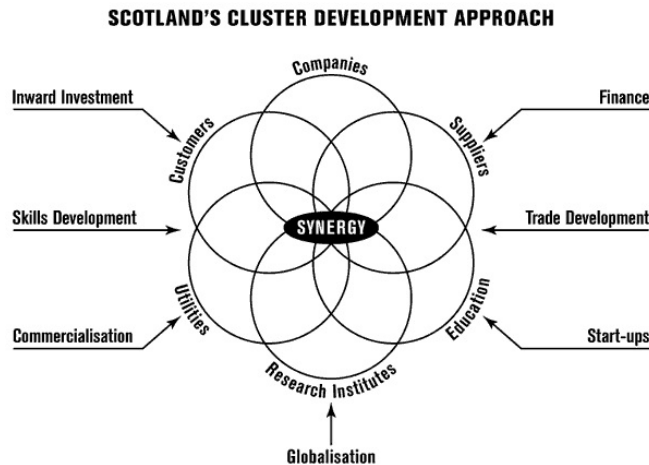


Figure 5.1

Although original ideas may be learned from sources beyond their specific localities, their implementation and innovation can be achieved most efficiently within an area with sympathetic institutions, that is, an area where “untraded interdependencies” have developed. Gregersen and Johnson (1997) make a distinction between “the production of knowledge and the utilization of knowledge”. What is significant for Gregersen and Johnson is that “learning has become increasingly endogenous. Learning processes have been institutionalized and feed-back loops for knowledge accumulation have been built in, so that the economy as a whole is learning by interacting in relation to both production and consumption. When economies learn how to learn the process tends to accelerate” (Gregersen and Johnson 1997, 481). This would be the ultimate aim of a clustering strategy based on the learning process: the acquisition of new knowledge and the processing of the new knowledge into innovative methods of production resulting in new learning for all the participants in the cluster.

Surprisingly, as we mentioned in [part 2.2](#), many of the regional scientists already cited fail to identify the locational aspects of learning regions with the earlier studies of Marshallian industrial districts, Storper (1992) being a notable exception. Implicit in this discussion is the idea that there is an ongoing interaction between the key players in a spatially specific area, including what Marshall would call an industrial district. Marshall provides a useful summary of the learning process that is analyzed by Gregersen and Johnson (1997, 481) and Lundvall and Johnson (1994, 26). In addition to the usual list of agglomeration economies and external economies of scale that are gained through organizing production within spatially defined areas, we have seen that learning economies also develop norms and practices that enable the key players to interact in an efficient manner: “The idea that lies at the centre of the concept of innovation systems is that the overall innovative performance of an economy depends not only on how specific organizations like firms and research institutes perform, but also on how they interact with each other and with the government sector in knowledge production and distribution” (Gregersen and Johnson 1997, 482). In a similar vein Lundvall and Johnson comment “knowing how to do things in isolation is not the decisive type of knowledge any more. Knowing how to communicate and cooperate becomes much more important than before” (Lundvall and Johnson 1994, 25). Storper (1995) notes that all production systems involve uncertainty and that “The main way that such uncertainty is resolved is through *conventions*, which are taken-for-granted rules and routines between the partners...” (Storper 1995, 208). The most important of these conventions, we would argue, are trust and cooperation. Although theorists of the learning economies identify the need for communication, and although the method to produce efficient communication (establishing conventions of trust and cooperation) is acknowledged, the nature of trust and cooperation is not widely discussed. The issues surrounding the establishment of trust and cooperation are examined in [section 6](#). For the remainder of section 5 we will examine the development of clustering within the Scottish economy.

5.3 The Development of Clustering Within Scotland

It has been claimed that Scotland has given the European Union the model approach to regional economic development, with its strategic partnerships of central and local government, RDAs, QUANGOs, and other players in the public, private and voluntary sectors (Danson et al. 1997). These partnerships have been established over the last twenty years, especially in West Central Scotland, through the progressive development of multi-agency, multi-annual, multifunctional initiatives, task forces and area agreements (Randall 1987; Moore and Booth 1986). While there have been criticisms of individual partnerships (Boyle 1989; Collins and Lister 1996), their durability and transnational acceptance have been testament to the perceived effectiveness and success of these forms of comprehensive intervention in the regeneration and redevelopment of communities.

Labour Party-dominated local authorities, such as Strathclyde Regional Council and Glasgow District Council, have been able to work closely on a common agenda with the market oriented Scottish Development Agency (Danson et al. 1980), and the private corporation-based Enterprise Trust movement (albeit their sponsorship was predominantly derived from the public purse). Their work, which has involved a series of partnerships at the local and subregional levels, suggests the building of trust through cooperation and experience. This has been critical in producing a model of intervention which is now adopted across the European Union.

The advantages of such partnership working can be discerned in the move toward a cluster approach to regional economic development within Scotland. It is becoming accepted at the national and regional levels

that partnerships are not only a legitimate and effective way of coordinating and focusing the resources of a number of agencies onto a problem, but also the favored approach. Local further education colleges, housing agencies, health boards and others have joined mainstream economic development bodies in stressing the need to work in formal partnerships with each other to meet economic and social challenges, as well as in their commitment to participate in these formal arrangements. The clusters strategy stresses the need to position Scotland at the high value end of the market, with enterprises active in the cluster operating within “a local economic environment geared to innovation, investment and upgrading” (SE 1998, 4). The strategy will be advanced by flexible partnerships of public and private sectors, which will include industry, education and government. These partnerships will devise action plans around which all economic players will cluster to promote an integrated development policy. Integration will be extended to the critical issues identified elsewhere by SE: “the need to capitalise better on Scottish scientific and technological expertise; to help companies build up their research, design and development capacities; to stimulate entrepreneurship; to encourage companies’ international ambitions and to build a high-performance transport infrastructure” (SE, 1998, 4) [for how to define clusters see Bergman and Feser, Chapter 3, “Cluster Morphology of Regions: Analytic Options.”]

See Figure 5.2 and Figure 5.3

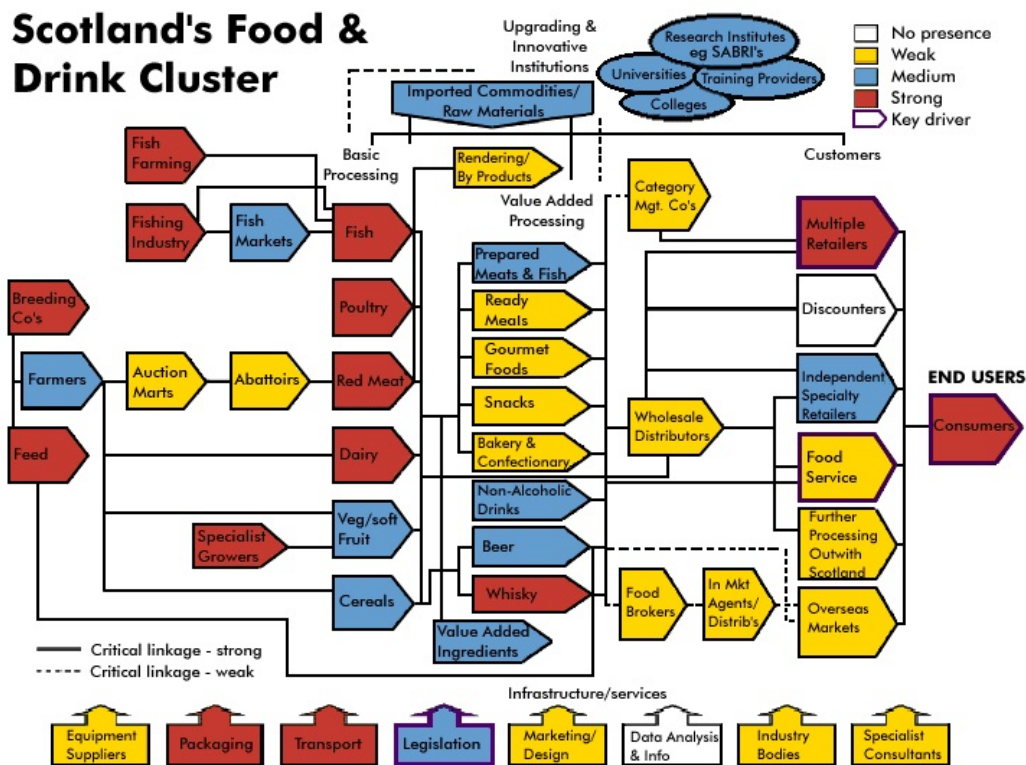


Figure 5.2

SCOTTISH ENTERPRISE

Food Cluster Strategy Development

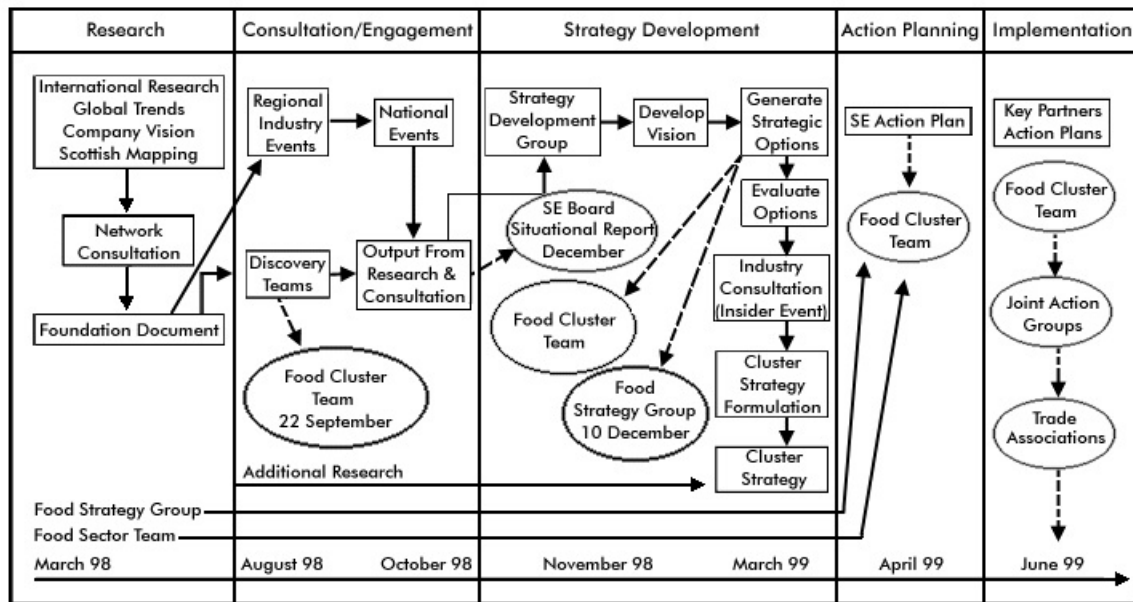


Figure 5.3

The strategy is to be underpinned by these other objectives and agencies, therefore. It will be holistic, acting upon synergies and linkages. The clusters will include both indigenous and inward investment. The strategy stresses technology, innovation and sustainable economic growth and development, suggesting the transmogrification of SE back into the RDA envisioned in the 1970s, rather than the business agency it has become over the last few years (Danson et al. 1980). This approach is being applied in many geographical and functional contexts, with reliance on a single agency forsaken in all areas of (re)development. Although clustering is usually applied to industrial organization, the concepts on which it is built can be found in other forms of governance structures, namely partnerships. In the remainder of this section we examine an attempt to promote the clustering strategy in one industry in Scotland, namely the electronics industry, and then analyze how the concepts that lie at the center of networking and clustering can be found in one particular area in Scotland, Ayrshire. These two case studies will highlight the contrast between differing governance structures. One consists of a trans-public agency partnership, built on trust and cooperation established over many years. The other comes from the emerging clusters approach to industrial regeneration and development. It is based on a model promoted by SE but does not seem to reflect recognition of the full implications of the philosophical underpinnings of the industrial district.

5.4 Implementing the Clustering Strategy

Scottish Enterprise has identified the electronics sector as a key industry in Scotland, which is hardly surprising given the importance of the sector to the Scottish economy. There are problems fully embedding the sector in the local economy, and SE is aware of them. Clarke (1996), in his study of the Scottish software industry, reported on a sector that displays many of the characteristics of a high technology sector, requiring particular forms of support within a general program of assistance. Although sector-specific programs are seen positively, Clarke questioned the concentration of state business development agencies on a minority of export-oriented, product-based companies. In like manner, Turok (1993a) examined the development of the printed circuits industry in Scotland. Unlike much of the electronics sector here, it is dominated by indigenous enterprises that are growing strongly. He argued that the main reasons for this buoyancy are the local concentration of firms within Scotland, the avoidance of direct competition between companies, the particular demand conditions facing the sector - based as they are on batch production of customized products for technically close customers, and the need to satisfy just-in-time manufacturing processes. Turok recommended closer

connections between enterprises and so the “growth of a Scottish industrial cluster in electronics,” as the sector tends to supply original equipment manufacturers (OEMs) in a dedicated chain with few external economies obvious from enhanced linkages between companies. It is not clear, however, how agglomeration economies would be promoted through improved networking and why, by extension, the industry would support such moves.

In line with the clustering strategy, SE is attempting to encourage more local sourcing through a Strategic Alliance with the major electronics firms who are organized through the Scottish Electronics Forum. The objective is to provide “vital support and infrastructure” (SE 1998a) so that the industry can maintain its competitive edge. This is to be achieved by making sure that the electronics industry exploits developing markets by concentrating on more knowledge-intensive activities, enabling the development of a “value-added logistics hub.” The Alliance identifies four ways to achieve this aim: commercializing academic and industrial research, increasing the level of Scottish content in electronics products, developing the skills base of the Scottish work force, and attracting R&D investment into Scottish plants (SE 1998b). The Alliance has now been adapted to fall in line with the clustering strategy of SE. This has resulted in a group of singularly functional operational departments combining to form the Information Industries Group. The information industries clusters team has a dominant role in working closely with the Electronics, Optoelectronics, Software, Multimedia and Information Society partners. The problems facing this cluster in the electronics industry concern job creation, local sourcing and technology transfer. “The Scottish electronics sector’s total output has nearly doubled in the past decade. But total direct employment today, despite some growth in the late 1980s is roughly where it was in the mid 1980s.... Nearly 80% of all components and sub-assemblies which go into Scottish-produced electronics output is sourced outwith Scotland” (Young 1997, 14).

In a study of linkages within the electronics industry in Scotland, Turok (1993b) suggested that there are opportunities for much higher levels of local sourcing by the foreign owned original equipment manufacturers (OEMs). Even where these do exist, he described them as corresponding to a “dependency model” rather than to a “self-sustaining economic development scenario.” Linkages are seen as weak or based on dependency, therefore the industry is not embedded into the regional economy. With few high technology linkages between indigenous supplier and OEM, there are no effective clusters because connections are founded on market strengths, not trust and cooperation. Few cases of transfers of staff or technologies have been recorded. Classically, the retention of higher order functions (R&D, marketing, strategic management, financing) elsewhere limits the ability of the local economy to establish business services externally to the multinational enterprises themselves, and to furnish spin-offs, transfers, and the other components of a successful milieu.

5.5 Local Economy Regeneration Partnerships

In Ayrshire, through an initiative which is being replicated across lowland Scotland, the local enterprise company Enterprise Ayrshire (the locally managed government agency established to coordinate the delivery of training and business development services and infrastructure), the three local authorities (East, North and South Ayrshire Councils), the Ayrshire Chamber of Commerce, the government housing agency Scottish Homes, the trade unions through the Scottish Trades Union Congress, and SE have come together as Ayrshire Economic Forum to prepare a collective Ayrshire Economic Development Strategy. Over the last year, the Forum has discussed the issues facing the county in the next half century to produce a Consultative Document “A Vision for Ayrshire” (Ayrshire Economic Forum 1998). This has been used to include the whole community in a period of reflection and debate over the future development of the area. This “Challenge for the 21st Century” repeatedly stresses the need for partnership, cooperation and cohesion with a recognition of “our identity,” “our collective voice,” “our common cause,” “our Vision” and “community.”

Such phraseology and sentiment are supported by independent reviews of the local economy and local market. The report “Labour Market and Skills Trends in Ayrshire” claims to be “tangible evidence of the commitment to a partnership approach to identifying and addressing economic issues in Ayrshire” (Ayrshire Economic Forum 1998, 3), with again use of self-containment in the county labor market, integration and “a strong partnership amongst local agencies” promoted as evidence of a cohesive economic community. Social inclusion runs through the policy recommendations subsequent to the report and on into the plans and philosophies of the other agencies separately.

Thus, Scottish Homes in the region promises that “the majority of our [future] investment ... delivers against existing multi-agency commitments, with specific initiatives already identified and being prepared with partners” (Scottish Homes South & West 1998, 29). In a similar vein, South Ayrshire’s strategy document “2020 Vision” is built on the idea of partnership and cooperation with the other agencies operating in the area, and beyond. Joint campaigns in favor of infrastructure improvements (extension of the motorway system into the county) and in response to economic challenges (redundancies and closures) are strengthening. Within council areas, at a lower level of community, the former government’s programs for “Priority Partnership Areas,” “Regeneration Areas” and “Smaller Urban Renewal Initiatives” are continuing to attract the support of a range of organizations and demonstrate a significant degree of cooperation to deliver synergies and effective performances in economic development delivery.

At a higher scale, the members of the Ayrshire Economic Forum are cooperating to secure enhanced levels of inward investment, European Union funds and central government resources. These initiatives illustrate a maturing of the partnership approach established under the Scottish Development Agency (SDA) and Strathclyde Regional Council in the 1970s, and nurtured over the intervening years. It is notable that they are still present after the dislocations precipitated by the creation of the local enterprise company network (as part of SE, to replace the SDA) in 1991 and the reorganization of local government in 1996. The trust secured and developed between organizations, and critically between the personnel of the successor bodies to the former SDA, District and Regional Councils, allows cooperation and partnership to survive and to be deepened in this environment.

By way of contrast with these developments, the recently promoted cluster approach in Scotland has shown less promise. Part 5.6 assesses the form and likely success of this approach to the economic development problems facing the Ayrshire economy.

5.6 The Clusters Approach at the County Level

In a development of the traditional industrial concept, the SE cluster approach calls on companies to establish strong partnerships to build trust and a shared vision. These specialist networks or clusters will “fuel innovation and generate synergies” that will enhance their international competitiveness. These clusters will “mean encouraging competition, co-operation and strong networks right across the community and between the public and private sectors” (SE 1998a, 1). The rhetoric, therefore, is very similar to the regional economic development partnership model described above.

Part 5.6 is not intended as a complete assessment of this sectoral reorientation of the SE economic strategy (see Botham (1997 unpublished) for an analysis). Rather, it is an analysis of those key components of “Scotland’s Cluster Development Approach” that illustrate the connectivity between the theory and practice.

The accompanying diagram (Figure 5.1), taken from the SE strategy document, suggests a coherent, inclusive partnership of all relevant development organizations. The approach focuses on “some of Scotland’s most important value-creating clusters”: food, biotechnology, software, electronics, optoelectronics, and multimedia. Leaving to one side the geographical distribution of these sectors (most are under- or unrepresented in Ayrshire, for instance) and the dependence on foreign domiciled multinational corporations, one may see a number of divergences between the strategic approach as seen by SE headquarters and the attempts to create clusters more locally.

Within Ayrshire, traditionally two of the most significant sectors in terms of employment and gross value added have been textiles and engineering. Although both have a long history in the county, they have also seen major periods of restructuring, with new firms and products entering the economy locally and well established enterprises disappearing. Past forecasts for these sectors and an assessment of their respective prospects led to the creation of formal networking arrangements under two initiatives: the Ayrshire Textile Group (ATG) and the Ayrshire Engineering Group.

As is noticeable elsewhere in Europe, but especially in the United Kingdom, the clothing and textile industry has been considered a “sunset industry” since at least the late 1970s (Totterdill 1992, 22). Structural adjustments in Scandinavia, Germany and northern Italy to changing patterns of consumer tastes, competition from non-European countries and trading agreements prompted a reconsideration of the future for the industry

in Scotland, and in Ayrshire in particular. Research suggested that the industry's successful adaptation to these changes would require:

- Intensive market intelligence linked to continuous design innovation
- High levels of technical expertise, particularly in production planning and problem solving
- A highly versatile system of production
- Effective use of distribution networks (Totterdill 1992, 24)

The idiosyncrasies of the United Kingdom's relations with Europe are mirrored here in the response to the successful restructuring strategies adopted in the other areas of the European Union. Evidence from the regionally important Nottinghamshire sector in England shows a range of local responses, some positive others less so. The need for intervention and the appropriateness of the above conditions pointed to the advantages of the establishment of an equivalent partnership or network in Ayrshire. Totterdill, at least, was arguing generally for a model close to the Emilia Romagna policy in the Third Italy for such areas, representing a complex, multilayered and decentralized model of partnership (1992, 47). The plans for Ayrshire supported such an initiative.

However, problems in the development of the model locally illustrate the failure to achieve a positive restructuring of the industry, despite the creation of a partnership, because of the lack of understanding of the need to promote cooperation and trust (Danson and Whittam 1998). As argued below, this requires a degree of ownership by the constituent firms.

SE identified textiles as an industry in which clustering should be encouraged so that the industry can compete. At the local level Enterprise Ayrshire has been instrumental in trying to implement this policy via the ATG. The textile industry in Ayrshire now represents 25% of Ayrshire's manufacturing industry, employing 9000 people and exporting £60 million per annum. In 1991 a partnership arrangement between Enterprise Ayrshire and the textile sector was established. This led to the creation of the ATG in 1992 with the establishment of a program of assistance leading to the ATG acquiring its own premises in 1994. The commitment to working in partnership with the industry reflects the ethos of Enterprise Ayrshire's approach to local economic development: "it seeks to develop and build relationships with companies rather than superimposing a structure onto a sector" (ATG 1994, 3). The ATG appears initially to have been successful in the "delivery of information advice and programs in response to proven needs ... with more than 60% of local industry participating in some meaningful way" (ATG 1994, 4). This has led to product development, moving products more up-market, increased diversification and marketing Ayrshire textiles as a group. However, there has been a failure to take the project forward to develop a "stand alone resource centre." To become "free standing," it is envisaged that the ATG must recover all its operating costs. In this context, Johnstone and McLachlan (1996) found textile companies reluctant to participate fully in the network. This lack of participation became an obstacle to realizing economies of scale and scope, with "a low level of trust and the strongly adversarial nature of the [local] sector" (755) a significant factor. Unwillingness to pool resources, concern over allocation of orders within the network, apprehension over cooperation, and a failure to communicate were all cited as contributory reasons for the lack of a full commitment to the project by the member firms. The need for training in networking protocol and processes, the key role of the facilitator, and the benefits of contractual agreements between members were identified as necessary elements if the local industry was to create a successful cluster. It would appear that although ATG has attempted to develop a partnership, the companies do not see the group as theirs. There is a tacit recognition of this problem in one of the reasons given for the establishment of the "free standing" facility: "The Ayrshire Textile Industry must view the ATG and its Resource Centre as their own" (ATG 1994, 13). This is one of the essential features of the 'ideal model' of the Strathclyde European Partnership.

Further, few companies were willing to pay for the services of the ATG, and where funds were provided for marketing, training and product development it was difficult to persuade the firms to follow the ATG's requirement to quantify "outcomes." Other problems also became apparent. For example, in the local lace sector, which produces some unique products and occupies significant niche markets, there was a strong reluctance to pass on skills, experience and expertise to younger recruits. This will have inevitable consequences for the industry in Ayrshire. However, a limited number of innovative enterprises recognized

the partnership as beneficial; these companies tended to support joint seminars, the use of CAD/CAM, the potential of linkages with tourism, and technology transfer initiatives.

Another attempt by an LEC to deliver SE's clustering objective can be found in Ayrshire: the Engineering Ayrshire (EA) initiative. Engineering is the largest manufacturing sector in Ayrshire, with over 180 companies employing over 14,000 people. It has a turnover of £1.9 billion and generates £1.3 billion in export sales (EA 1997, 6). The original rationale for the establishment of the group arose because of the perceived lack of sales beyond the west of Scotland. To this end EA has organized trade missions, launched a public procurement initiative and provided individual members with export sales and product/process improvement support. The EA group is now seeking to widen its activities to capitalize on opportunities presented by changing market conditions. Of significance and giving grounds for optimism, vis-à-vis the possibility of the group becoming self-financing and realizing key objectives such as developing a skills base in a collective manner, is the structure of the organization. Unlike the ATG, the aims of EA state that it should "be an organisation run by its members for the benefit of its members and the Ayrshire engineering and electronics sector" (EA 1997, 9). Within its strategic objectives there is a responsibility placed on the membership to work in partnership with the relevant organizations (such as Enterprise Ayrshire itself, local councils, and trade associations) and to attend relevant seminars and programs. The group is managed by a steering committee, comprising senior representatives from six companies and two Enterprise Ayrshire executives, which meets monthly. A full members' meeting is held at least once a year. By placing obligations and responsibilities onto the membership and by having an accountable framework for decision making of the group as a whole, it is hoped that the problems associated with the ATG in attempting to develop its strategy will be overcome. The essentials of an ideal network, outlined in the introduction, can be seen in the EA clustering initiative.

5.7 Conclusion

The above demonstrates that a cluster strategy can be an effective instrument in the regeneration of a regional economy. The synergies and mechanisms for resolving conflicts identified in the case study of the trans-public sector agency partnerships in Scotland have been significant in the adoption of the "Scottish partnership model" across the European Union. However, the lessons from this approach coupled with the theoretical underpinnings in the literature on industrial districts have not been incorporated fully into the strategies for industrial clusters. Trust and cooperation are essential if the advantages of innovation and networking are to be realized by all of the players in a sector, and if clusters are to be effective. In the successful partnerships described here, the long development of working relationships between organizations and between individuals have been critical to formulating a successful approach to regional economic development. However, where networks have been dominated by multinational enterprises or their structures and *modi operandi* have been imposed from the center, there have been significant problems in the perception and appreciation of the benefits of the new clusters, exemplified here by one of the case studies from Ayrshire. Without some sense of ownership over their cluster and network, the SMEs that may have most to gain from the promotion of industrial districts realistically will remain excluded from these partnership activities.

The issue of the distribution of power within the cluster can be critical, therefore, to its acceptance and success. What guarantees are there that all the key players are going to play the game fairly? In other words, how can the cluster ensure that a multinational corporation, which is not necessarily tied into a specific locality because of the relative mobility of capital, is going to share advances in knowledge acquired through the network?

As much of the output of knowledge is information, and given the public good aspect of information, these concerns may be resolvable; evidence from Wales (Morgan 1997) suggests that this is the case. However, given the recent processes of the economic development of the Scottish economy and the special relationship with multinational corporations, these concerns may not always be resolved. As we have argued here, there is a need to create a structure for clusters that meets the desires of regional SMEs, and that allows indigenous companies to regain control over future development and to have a stake in the growth and evolution of the industry.

6 Networking and Industrial Districts: New Types of Industrial Organization

6.1 Introduction

As noted in the sections above, in the recent past the academic literature and the policy strategies of many developed countries have strongly favored the organization of small and medium enterprises (SMEs) through “networking” structures and more spatially specific arrangements, namely industrial districts. This section explores some of the conditions necessary for the establishment of formal organizational structures that will lead to firms cooperating within the process of production. The terminology we employ to describe interfirm relationships is deliberately loose but encompasses all types of relationships that embrace some degree of risk-sharing and information exchange. The section centers on arrangements within the context of the Scottish economy.

The section’s focus is based on the fact the principal agency with the task for economic management of the Scottish economy, [Scottish Enterprise](#) (SE), has recently identified networking arrangements among SMEs as a way to achieve growth and hence job creation among them. According to SE, “Networks are important: many of the solutions will be found in the actions of individual entrepreneurs, backed by their networks of family and friends. An important focus of action for the strategy is to improve the effectiveness of these networks and to make potential entrepreneurs more aware of what they can do themselves to achieve success. Part of this involves improving the support given by the formal support networks in the private and public sectors” (SE 1993, 4). *The Business Birth Rate Strategy* acknowledges that there are problems with existing networking agencies within the Scottish economy and seeks ways to encourage the effectiveness of both formal and informal networking arrangements (SE 1993, 8). See Figure 6.1 :Company birth rate

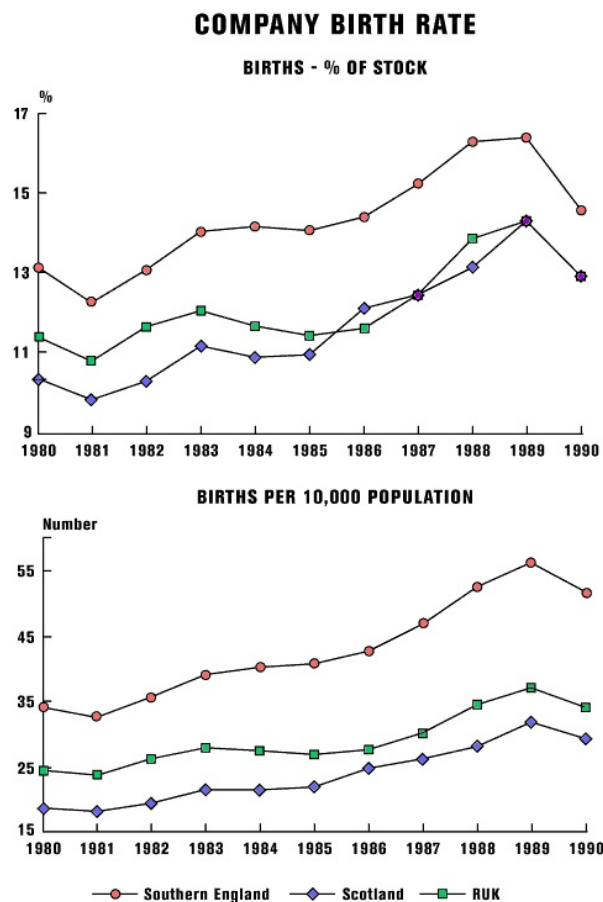


Figure 6.1

As SE's research efforts and strategies were based on an examination and analysis of the international literature and practices of various levels and forms of governance institutions, the work of SE is used here to show an appropriate example of a standard region. The processes of research and strategy development are applicable well beyond the Scottish experience, so we use this case study as a fully legitimate introduction to the exploration of "networking."

The objectives of the SE inquiry were to provide improved understanding of the role of new firm formation (NFF) in economic development and to explain why Scotland had a lower rate of business creation than other regional and national economies. These objectives made the inquiry international by definition. The SE research program identified two key concepts: the Business Life Cycle and Segmentation. The former concept gave rise to two key questions: Why does Scotland generate so few new ventures, and why does Scotland generate so few new ventures that grow into substantial companies?

In addressing segmentation, the SE program addressed the varying rates of NFF across countries and regions - by structure, product and process. It also analyzed entrepreneurs - by background and circumstances - to investigate the operation of entrepreneurial development in different market milieu. Within this overall framework the program analysed a number of key issues: regional new firm performance, individual and sectoral case studies, business environment, and entrepreneurial potential and cultural issues.

The analysis confirmed the persistent low rates of enterprise creation in Scotland (Figure 6.2), although the growth of surviving enterprises was at least as good in Scotland as elsewhere, if not superior. From this, SE concluded that the problem was the overall birth rate, with the policy implication being that measures to expand the pool were more appropriate than "picking winners."

NEW FIRM EMPLOYMENT IN SCOTLAND

Actual jobs and shortfall relative to the south east

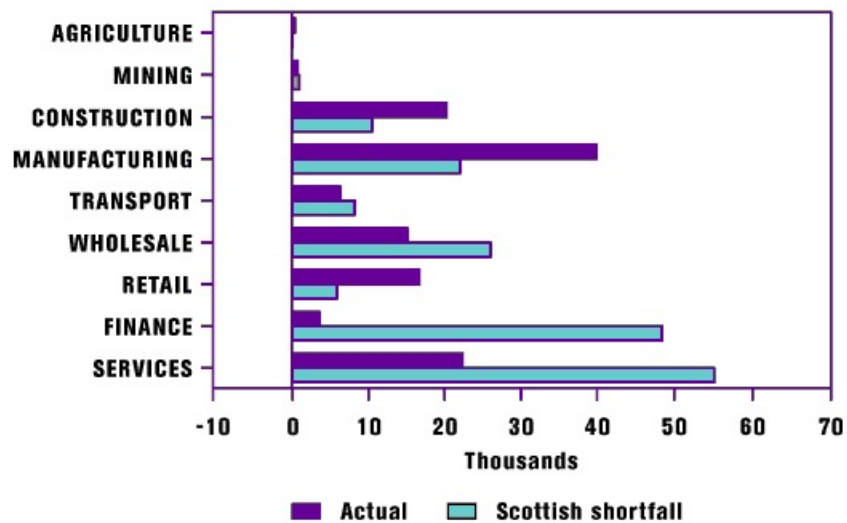


Figure 6.2

If the promotion of "networking arrangements" to achieve the desired objective of new firm formation is to be successful, an understanding of the essential components of successful networking is needed. In this section we focus on the issues of trust and cooperation. The remainder of the section is divided into four parts. [Part 6.2](#) provides a brief history of the Scottish economy, focusing on the significance of the past for present-day policy proposals. The consideration of historical, social, political and other environmental contexts in contemporary economic scientific analysis is typical of the Scottish Political Economy tradition. [Part 6.3](#) identifies the significance of trust and cooperation, highlighting how these critical factors can become established. [Part 6.4](#) analyses how successful SE has been in attempting to establish networking arrangements. [Part 6.5](#) concludes the section by suggesting policy implications in an attempt to ensure the future success of networks within the economy. The economies arising out of organizing production within industrial districts

have been highlighted elsewhere (Oughton and Whittam 1997) and are not a major concern of this paper.

6.2 Scotland: On the Periphery of Europe

Since the United Kingdom joined the European Union, the British Isles's trade and industry have seen a change of focus. In many ways this shift of focus has merely exacerbated a much longer decline in Scotland, Wales and the north of England. Indeed, over "most of this century Scotland has been declining relative to the rest of the United Kingdom and, by extension, the rest of Europe" (Danson 1991, 89). As one of the first industrialized regions of Europe and of the world, Scotland has experienced both an early period of growth and a long history of stagnation.

The growth and development of the economy was built on strong networks. According to Slaven, in the early part of the twentieth century "A community of interests was growing among steelmakers and shipbuilders, and this was a link more strongly developed at a later date.... The demands of the shipyards boosted the growth of steel dictated the changing production patterns of the pig-iron and malleable-iron producers. Marine engineering and shipbuilding lay at the centre of a complex concentration of heavy engineering and finishing trades" (1975, 182).

Behind the development of the Scottish economy, and of Clydeside in particular, were also factors associated with the British Empire. Britain's role as an imperial power, based on naval supremacy, prompted the establishment of the coal and steel industries of central Scotland. The regional economies, and through linkages and migration the rest of the nation, became inextricably dependent on the trading and military position of the United Kingdom as a whole. Clydeside experienced very significant growth in industry and population in the years up to 1914. Records on shipbuilding tonnage (Slaven 1975) confirm that this area was at the heart of the Empire in terms of industrial output and importance. World War I was perhaps the watershed. Although the seeds of external destruction may have been made inherent before then, the decline of British power and controlled imperial markets exposed a rapid and deep structural imbalance in the Scottish economies. Massive unemployment, poverty, deprivation and emigration marked the period up to the World War II, with Glasgow containing what may have been the worst urban slums in the history of the planet (Damer 1990). Since 1930 this industrial legacy has left Scotland subject to a broad set of economic policies targeted at relieving the worst effects of the rundown and closure of its staple industries - steel, coal, shipbuilding, heavy engineering and textiles.

Having struggled to maintain former glories in output and trade through most of the century, Scotland - and the rest of the periphery of Britain - has been in almost constant benefit of various forms of regional development aid. Regional economic policies have been based on the restructuring of old industrial areas and the decongestion of overcrowded housing and manufacturing areas. Increasingly, such policies have been concerned with promoting foreign direct investment and withdrawing the state from direct involvement in production. This has led to an increase in the degree of external control and ownership of Scottish industries. The change has come at times through merger and takeover, through nationalization and privatization, and through differential rates of decline and growth of native and foreign companies. Research suggests that such changes, in complex ways, put a relative brake on the rates of new firm formation and indigenous development (Ashcroft, Love and Schouller 1987). Concomitantly, output, trade and investment have become more narrowly dependent on a few key sectors.

With the regional policy focus on the attraction of inward investment and with low rates of endogenous growth, a branch plant economy has been created to replace the former heavy industrial clusters. With few local supplier or purchaser linkages, and an absence of such higher business functions as R&D, finance, marketing and corporate strategy, branch plants offer jobs to the local economy, but little else. In particular, there are minimal relations established or developed between inward investors and the local SME sector.

Electronics (and computers especially) and whisky in Scotland have accounted for over half of non-oil manufacturing exports (Scottish Council Development and Industry 1997), and about 50% of all manufacturing investment in recent years. Both these sectors are dominated by overseas companies, with over 90% of output by non-Scottish firms. Over a quarter of manufacturing employment in Scotland is in overseas-owned plants,

and much of the rest is controlled by United Kingdom corporations with their headquarters in the southeast of England. This degree of domination is often blamed, in a simple way, for the massive restructuring of the Scottish economy since 1979.

Since 1980, 40% of all Scottish manufacturing jobs have been lost. In key traditional sectors such as coal, steel and engineering the decline in employment has been heavy, with the replacement of some of these jobs in electronic and electrical engineering. In many sectors such as agriculture, fishing, energy and water, manufacturing and construction, employment is at its lowest levels in Scotland, with jobs for both men and women disappearing. Only the service sector is showing any growth over time, and then only in part-time work.

In such past-dominated, narrow economies, NFF and SMEs have been presented as panaceas in the mission statements of many agencies in European regional economic development and regeneration programs. This is noticeable in the European Union in particular. The business birth rate in the European Union has increased since 1980 (SE 1996). However, questions have been raised over the ability of companies dependent on the local market to reverse long-term regional decline on their own. Entering this debate, Malecki and Nijkamp (1988), for example, have suggested that uneven development is endemic and that it is impossible to overcome metropolitan core bias through compensation of the periphery. On the other hand, Vaessen and Keeble (1995) appear to see enough examples of successful SMEs in the periphery to argue that regional divergence need not be inevitable.

In practice, there has been but limited success in replacing traditional major manufacturing employers. Seeing that more prosperous areas of the United Kingdom tend to maintain higher rates of business start-up (Ashcroft and Love 1996) and that real unemployment rates are persistently significantly higher than the United Kingdom average in the problem regions (Beatty and Fothergill 1997), one might conclude that greater levels of incomes and wealth are compatible with the creation of conditions for enterprise development. But analysis of the nature and form of networking and of the wider business environment is also of critical relevance in determining such comparative performances in regeneration.

A key question for the success of the new firm and of inward investment strategies, separately and collectively, is whether they are conducive to the creation of networking and industrial districts. Superficially based on the best practice models identified in regional economic regeneration strategies elsewhere in Europe and in North America, these strategies rely on trust and cooperation. It is to a consideration of these themes that we now turn.

6.3 Trust and Cooperation in Industrial Districts

From the outset it is worth remembering that wherever exchange takes place, either on the market or through firms, a degree of cooperation takes place. The division of labor, so crucial to *The Wealth of Nations*, is dependent on cooperation between the parties involved. Similarly, business deals involving millions of pounds are concluded on the strength of a handshake, and currency deals struck over computer terminals are all based on a degree of trust. Looking at events in the natural world, perhaps we should not be so surprised at the potential for cooperative behavior. We can cite examples from nature (see for example Bateson (1988)) to illustrate there is nothing in the “state of nature” to say that the “survival of the fittest” is the one culture evident in nature, and we can even appeal to the works of anthropologists and psychologists for examples of how human behavior has led and does lead “naturally” to cooperation, as opposed to unrestrained competition. Burchell and Wilkinson, building on these aspects of conducting business, highlight what they see as two dimensions of a business relationship, cooperation and competition: “Trading partners,” they argue, “derive mutual benefits from cooperation in production from which their incomes are ultimately derived, but they compete over the proceeds of production because what one gets the others cannot have. Every business relationship is therefore by its nature both rivalrous and cooperative” (1997, 219). What we observe in systems of production such as industrial districts is a greater emphasis being placed on the cooperative aspects of the exchange relationship. Accepting that there are two sides to a business relationship, we are confronted with the problem of making sure that economic actors who may prefer a cooperative option are not the victims of opportunistic behavior.

One method of attempting to restrict opportunistic behavior is by organizing production within an institution

such as a firm, as opposed to the institution of the market. Coase (1937) observed that there are instances in which it is economically more efficient to do this. The costs of using the market mechanism can be reduced by organizing production within the structure of the firm. Similarly, contracting arrangements can act as a means of reducing the costs of coordination, but there are costs involved in establishing and monitoring contracts (Williamson 1993). Furthermore, it has been observed (Macaulay 1963) that while detailed clauses are often written into contracts they are seldom used: “contract and contract law are often thought unnecessary because there are many effective non-legal sanctions. Two norms are widely accepted. (1) Commitments are to be honoured in almost all situations; one does not waltz on a deal. (2) One ought to produce a good product and stand behind it” (Macaulay 1963, 63). So even when measures are taken to monitor actors’ behavior, it is often the case that an environment develops among those actors in which implicit contracting makes enforcement unnecessary, and the cooperative aspect of trading surfaces once again. These arguments tell us that although there are legal sanctions available for organizations to enforce compliance, these are rarely used. These comments are worth bearing in mind in our examination of the characteristics of trust and cooperation.

Gambetta (1988) in discussing the relationship between trust and cooperation argues that it is through cooperation that trust will evolve. Gambetta defines trust as “a particular level of the subjective probability with which an agent assesses that another agent or group of agents will perform a particular action, both before he can monitor such action (or independently of his capacity ever to be able to monitor it) and in a context in which it affects his own action” (217). This definition raises two important points. First is its implication that individual actors will calculate the probability of an actor behaving in a particular way, suggesting that some of the actor’s behavior can be monitored. Second, Gambetta raises the possibility that not all activities of an individual actor can be monitored. If actions cannot be monitored, what guarantee is there that an actor will behave in the manner expected? How can cooperation be guaranteed? In situations in which behavior cannot be monitored, is it worthwhile calculating the probability that the individual will act in the expected manner? It will be argued below that where exchange takes place within productive systems, institutions will develop which will ensure certain types of behavior. Using monitoring arrangements suggests that there is some way of guaranteeing compliance, or at least some way to prevent opportunistic behavior. In other words, Gambetta is moving beyond a simple transaction cost approach. And, Gambetta’s definition implies that monitoring is not always necessary.

In line with Gambetta’s definition, the literature on industrial districts identifies trust and cooperation in a way that transcends the notion of simply reducing transaction costs. The accepted values of trust and cooperation transcend the productive units of the district and embrace the whole community. On this note, Best (1990) states that “A carefully nurtured collective identity can potentially provide the social fabric which sustains cooperation in an industrial district as in a corporation” (237). The identification of the industrial district encompassing firms and a wider community as a whole, “as in a corporation,” is a point identified by Becattini in his definition of an industrial district: “I define the industrial district as a socio-territorial entity which is characterised by the active presence of both a community of people and a population of firms in one historically bounded area....The most important trait of the local community is its relatively homogeneous system of values and views...” (Becattini 1990, 38-39). This collective identity has resulted in a large degree of trust and cooperation between the SMEs operating in the industrial districts of the *Third Italy*. It is worth reminding ourselves, however, that this collective identity, now acknowledged to be so important to the success of these districts, has not always been present. Indeed the history of the Third Italy, the most famous of the industrial districts, is littered with strife and conflict. While Capecchi (1990) provides a picture of historical uniqueness based on the development of Emilia Romagna it is difficult to imagine that the modern development of the region, which suffered large-scale factory closures immediately after World War II, and witnessed a huge sectoral shift in employment from agriculture to industry over a twenty year period, 1950-1970, could have occurred without social unrest. Sabel (1992), in discussing the building of trust, suggests that the actors within the industrial districts of the Third Italy have developed a selective history of the past: “it is not us outsiders but themselves that the tellers of these stories aim to fool; and it is no fault but our own if their efforts to induce a kind of genesis amnesia in themselves lead us to believe that their history was without conflict” (226). Sabel continues to document various conflicts within northern and central Italy; a more detailed analysis can be found in Sabel (1982). Likewise Brusco (1982) cites the impact of effective unions in the large factories of the industrial districts of the Third Italy as a reason for the

development of SMEs, the large firms deliberately outsourcing as a means of breaking union organization.

The trust and cooperation occurring in the industrial districts of the Third Italy is of a differing order than that occurring in a simple exchange relationship. We would argue that due to the establishment of a culture of trust and cooperation between firms there we are witnessing economic interaction with limited calculation and monitoring. In the literature at least three different types of trust are acknowledged: contractual trust, competence trust and goodwill trust (Sako 1992). Contractual trust is the trust that exists between trading partners and that results in the belief that goods will be delivered on time, be of the required specification and be of the agreed quantity and quality. Competence trust refers to the belief that a trading partner will fulfill a particular task. Goodwill trust occurs when initiatives are undertaken beyond the specific remit of a contract: “the role of goodwill trust extends beyond existing relations and includes the transfer of new ideas and new technology. Thus, while contractual and competence trust mainly benefit operational efficiency, goodwill trust also contributes to the dynamic efficiency of productive systems” (Burchell and Wilkinson 1997, 218). Quite clearly, it is this latter type of trust that is to be found within the established industrial districts. The question then arises, how can contractual trust be developed into goodwill trust? Put another way, how can the cooperative aspect of an exchange relationship be developed so that cooperation and trust become the norm for business undertakings?

This objective can be achieved by two related means: policy delivery and collective action. Policy delivery can be utilized to promote a cultural change. Collective action needs to be developed to guarantee cooperation and trust within the productive system. A pertinent example of policy delivery resulting in a cultural change is provided by Hodgson (1988), who uses the example of the introduction of seat belt enforcement. Hodgson points out that this policy initiative resulted in changed behavior. The policy was accompanied, of course, by a degree of coercion. The chances of detecting that someone was not wearing a seat belt, however, were slim, and the educational campaign highlighting the benefits of wearing seat belts was established long before 1983, when the law enforcing their use was introduced. Hodgson’s argument is that “The authority of the law had the effect not simply of changing behaviour by the introduction of penalties or the perception of costs and benefits. In addition, it changed these individuals themselves and their goals” (Hodgson 1988, 137). In other words, through policy delivery individual behavior can be changed. Change affecting many individuals will result in a different culture being established. Using coercion implies that action can be taken to ensure compliance. Over-reliance on coercion, however, may well lead to distrust. Actors may well question the amount they are actually trusted if they have to be continually monitored. More significantly, if one actor is able to exercise coercion over another this suggests an unequal distribution of power in the relationship. “It introduces an asymmetry which disposes of mutual trust and promotes instead power and resentment” (Gambetta 1988, 220).

To overcome the potential for mistrust that the use of monitoring and punishment strategies to guarantee compliance can breed, the promotion of collective action needs to be encouraged. Potential members need to be aware of the benefits to be achieved from belonging to the productive system: “large organisations that are not able to make membership compulsory *must also* provide some noncollective goods in order to give potential members an incentive to join” (Olson 1971, 17). This promotion of collective action within established productive systems, such as industrial districts, has led to the actors taking on a group identity, as previous citations have indicated. The development of a group identity results in the individual actor placing the group’s interests above his self-interest. However, even in productive systems in which members appreciate that pursuing group interests leads to individual benefits, there is still the necessity for some compulsion. Where elements of public goods are being delivered, there is always the temptation to “free-ride.” Goods and services, such as facilities for engaging in R&D, are typically provided within industrial districts, and contain elements of public goods. Cooperative advertising strategies promoting a region or country as a whole indirectly advertise all businesses within the geographic area and hence suffer from the “free-rider” problem. Within industrial districts the compulsion element resides in the fact that companies have to be a member of the “club” (such as the Real Service Centre or a network) and if they break the rules, they can be excluded. Once established inter-firm relationships develop norms of behavior, custom and practice facilitate trust and cooperation, which can result in “embeddedness” (Granovetter 1985). Being a member of the club leads to established relationships becoming long-term because of the investment a firm undertook to become a member in the first place, and because if a firm did leave, “competitors and customers would ask why” (Arrighetti et al. 1997, 190).

In part 6.3 we have identified the dual nature of business relationships. There are economic gains to be achieved, particularly for SMEs, by the promotion of the cooperative side of the business relationship. In order to promote the cooperative side of a business relationship it is necessary to reduce the risk of opportunistic behavior. This can be done by the promotion of trust and the establishment of inter-firm relationships. We noted three different types of trust and argued that it is goodwill trust that should be sought in establishing networking relationships between firms. We have further argued, by drawing on the experience of the *Third Italy*, that policy delivery can assist in the development of trust and cooperation. While it would be desirable for productive systems to avoid punishment strategies or enforcement mechanisms because of the danger of promoting distrust, such strategies are always necessary, even in best practice examples of inter-firm relationships. Enforcement mechanisms exist in the form of institutional norms and practices and in the development of more concrete organizational structures. Member firms who “cheat” on other member firms can be excluded from the institution or organization of which they are members. This idea of examining firms within a framework of institutions and organizations suggests that SE, with its objective of establishing networks, needs to develop a collective approach to the establishments of inter-firm relationships. We now turn to examine the recent experiences of SE in its efforts to establish networking between firms within the Scottish economy.

6.4 Scotland’s Business Birth Rate Strategy

As suggested above, Scotland could be described as an export-oriented economy, now relatively protected from the United Kingdom’s business cycles, but open to new sensitivities. Scotland is especially locked into the supply needs of multinational oligopolies in the electronics and oil sectors. It is clear that Scotland’s future will depend upon European markets, and also, consequently, in attracting foreign direct investment from North America and the Pacific Rim to enter the European Union. Exports surveys for Scotland show the degree to which the historical patterns of trade have been transformed. According to a well established survey (Scottish Council Development and Industry, 1997), two-thirds of Scottish exports go to western Europe. Electronics products account for 49% of all sales overseas, most going to Europe and to a lesser extent the Middle East and Africa (See [SCDI](#) and [SE](#)). Globalization of production in essence means multinational enterprises arranging a configuration of plants across the world that meets their needs to supply exports to a number of trading blocs. The deepening reliance of Scotland on the attraction of such titans means competing for highly mobile investment, with this very competition between regions and states threatening to heighten the propensity of such capital to be mobile. Without a counteracting, long-term sustainable development of indigenous companies, it is recognized that peripheral economies progressively will lose further control over their own destinies: the development of underdevelopment.

In implementing the twin supply-side strategies of inward investment and new firm formation to address regional development and regeneration, RDAs and local authorities collectively arrange for property investments, improving the image of the area in the process. Training, technology transfer, information technology, and telecommunications are also favored areas for investment through local, United Kingdom and European Union interventions. Confirming such joint working, recent research (Danson et al. 1997) has demonstrated the strength of the corporate consensus approach to regional policy in Scotland, with many adopting the Scottish partnership model as the way to organize local and regional development strategies. At the political and bureaucratic levels, then, networking and partnership are accepted as valuable features of economic development strategies.

To what extent has this experience been applied to the implementation of the business birth rate strategy? Addressing this question requires a consideration of the original and subsequent related research into the low rates of new business start-ups in Scotland. As part of the overall study on this subject, SE sponsored research on specific sectors that were considered to contain significant lessons or to have a key role in the economy. Analysis of the clothing and textile industry showed that the popular view of company failures and declining employment was disguising the actual and potential contributions of new firms to the industry in Scotland. However, the role of new firms in the industry was restricted by a lack of innovation and dynamism. Evidence from Italy and Germany, with their strong networking traditions, suggested that the clothing and textile industry had the potential to make a more significant contribution to the economy. This evidence suggests that development through growth in the number of new, small firms rather than expanding the size

of existing companies is the best way forward. In this context, Johnstone and McLachlan (1996) examined the internationalization of SMEs in a region of Scotland - Ayrshire. They examined in particular the development of networking through the establishment of export consortia. They found that recent attempts to improve competitiveness through pooling of capabilities, with the local enterprise agency acting as facilitator, produced mixed results. The reluctance of firms to participate fully in the network was a clear obstacle to realizing economies of scale and scope, with “a low level of trust and the strongly adversarial nature of the [local] sector” (755) a significant factor. Unwillingness to pool resources, concern over allocation of orders within the network, apprehension over cooperation, and a failure to communicate were all cited as reasons for the lack of a full commitment to the project by the member firms. The need for training in networking protocol and processes, the key role of the facilitator, and the benefits of contractual agreements among members were identified as necessary for the local industry to create a successful cluster. Further details of this study are given in [section 5](#).

Looking at high tech and academic spin-offs, the economic consultants PACEC reported minor differences in the factors explaining low levels of NFF in these specific sectors and in the overall economy. PACEC perceived the research base within industry to be inadequate, with few organizations acting efficiently as incubators for spin-outs and new high tech companies. The infra- and super-structure were deemed deficient, with poorly developed and weak specialist resources, social networks and information flows within the high tech community. PACEC highlighted the lack of demand for high tech companies. This lack of demand, PACEC concluded, constrained development of a home base and put firms at a cost disadvantage in export markets. In comparison with other areas, notably Massachusetts, policy support was seen as less extensive. Problems in establishing a high tech firm were compounded by the actual process of formation and growth, with the lack of support and ambition at home stunting development opportunities. All of these problems seemed minor compared with problems facing academic spin-offs, the authors argued. Major restrictions in promoting new firm formation were identified in Scottish higher and further education institutions and in their business, funding and cultural environments. Entrepreneurship was perceived as alien to academic traditions, risky and stigmatizing, so that significant barriers to entry into the marketplace had been erected.

Westhead and Cowling (1995) also looked at high tech business start-ups and questioned the certainty of such conclusions. They believe that the debates on the major factors affecting high-tech firms are still unresolved. In a study from the United States, Muniak (1994) has argued that there are essential conflicts over the promotion of regeneration policies at the urban and at the national level. In the same vein, and as seen here, much of the policy and analysis in the United Kingdom seems to suggest that the needs of local and of national economies may not be coincidental with regard to the encouragement of high tech and academic entrepreneurs. Policies to improve NFF in the country as a whole may lead to different effects across regions, perhaps providing strong virtual and vicious cycles of uneven development.

These various studies on high tech and academic spin-outs and starts suggest that networking, partnership, trust and cooperation were poorly developed or actively discouraged in Scotland. The role of branch plants in diminishing the ability of entrepreneurs to set up their own businesses was noted frequently, as more unexpectedly was the skepticism and obstruction of the business development and academic establishments.

In section 5 we highlighted the problems of developing an embedded cluster in the electronics industry in Scotland. Research by Lipka and Howie (1993) on the North Sea oil industry has demonstrated that Scottish companies tend to be restricted to the peripheral, low value added areas of the sector, such as catering, supplies, labor-only contracts, and maintenance. Unable to integrate forward because of a lack of market strength and too low on the value chain to establish an export oriented sector of any note, such companies realize few opportunities by cooperating in an industrial cluster.

One model to address such problems is corporate venturing. Corporate venturing covers assistance to entrepreneurs or SMEs to exploit new ideas, corporate restructuring through staff creation of new independent businesses, and the development of new profit centers and subsidiaries to exploit new products, processes and markets. It has been suggested (SE 1993) that Scotland is poorly provided with such approaches to regeneration and restructuring, which is unfortunate because, by reducing risk and establishing new ventures with better prospects, these approaches offer an effective, additional element in promoting NFF, especially in the high tech industry.

A perennial problem facing new entrepreneurs in Scotland, and in the United Kingdom more generally, concerns financial support. Considering the extensive research on financial aspects of supporting new firms and networks, the SE (1993) findings proposed an attempt to close the widening equity and financial gap with a move to the provision of risk finance by the public sector and by the private investor, the so-called “business angel.” Some of the sections on finance in *Scotland’s Business Birth Rate* (“Finance - The Big Issue?,” “Informal Investment - A Neglected Source?,” and “Finance - The Ongoing Debate”) suggest that little of this problem has been resolved. The equity gap is contrasted with the availability of money; the question of access is a major and persistent feature in the Scottish business environment, and to a greater extent than elsewhere. Given the significant power and size of the Scottish financial sector, its invention and introduction to the world of investment and unit trusts, and its strong history of (savings) banking, there is an argument that “improvements in the behaviour and performance of both lenders/investors and actual/potential business founders” can and must be encouraged (SE 1993).

Many of the factors influencing enterprise creation and regional economic development raised in the SE inquiry are common to most communities, and arguments surrounding these factors are well rehearsed elsewhere. However, the inquiry’s identification of entrepreneurial potential and cultural issues as significant adds an extra dimension to our understanding of the processes involved in NFF. The SE research directly challenges the business development community in Scotland to address its own behavior and attitudes toward potential entrepreneurs. The SE inquiry used extensive interviews across several countries, and literature reviews, to establish the comparative levels of interest in entrepreneurship, perceptions and experience of entrepreneurship, and social attitudes towards enterprise. According to the research results, the perception of entrepreneurs by the community in Scotland was less positive than it was elsewhere. Recognition of entrepreneurs’ contributions to the economy was not sufficient to undermine the key role the community reserved for government intervention (Figure 6.3). The Scottish perception may be a reaction to Thatcherism, but it is undoubtedly related to Scotland’s economic and social history. It has been argued that persistent unemployment, poverty and deprivation, against a relative economic decline of eighty years duration (Danson 1991), have thrallled Scots to the philosophy of collective intervention to generate jobs. Entrepreneurs were seen in these surveys as being less caring and community oriented than the respondents. As argued here, the strategies of SE, with their denial of the relevance of trust and cooperation, have exaggerated rather than addressed this view (See Figure 6.3: What people think about entrepreneurs).

Although further analysis by SE (1993) showed a lower pool of self-confessed, potential entrepreneurs, there was still a substantial proportion of adults who believed they had the ability and desire to run their own businesses. Statistics suggest that there was no anti-enterprise or dependency culture; rather, with much unexploited potential, there seemed to be a barrier to converting desire into reality.

A closer look at the SE analysis suggested that the very agencies established to promote business start-ups lacked trust and cooperation in the indigenous entrepreneurs under their charge. Interviews with the business development industry and among opinion-formers demonstrated complacency, a less than positive attitude to policies promoting new SMEs. They also revealed that among members of these groups, there was a dependency culture in which it was believed that native Scots entrepreneurs could not be a dynamic part of the regeneration process. A misperception of the characteristics of indigenous people, and therefore of potential entrepreneurs, was not uncommon, with some agencies suggesting higher barriers were required to limit entry by local businesses into the market.

Many of the concepts at the heart of regional economic development strategies, such as the encouragement of inward investment, the avoidance and fear of displacement, and the provision of business advice, suggest that they may in their implementation corrupt the promotion of NFF in ways not identified before. So, while dominant and branch plants have been considered as potential destroyers of entrepreneurship (Fothergill and Gudgin 1982; Storey 1982), the reality may be more complex. There is evidence that RDAs and government departments have been opposing management spin-outs, effectively scuppering the opportunity for technology based developments by sanctioning the closure of R&D laboratories in nationalized industries, and dampening enthusiasm and support for management/worker rescues of branch plant closures (Strathclyde Regional Council 1988; Danson 1991). The rationale for the agencies’ actions is that, with the views of overseas owners and future investors paramount, the position of inward investment agencies cannot be compromised in the international market for mobile capital.

WHAT PEOPLE THINK ABOUT ENTREPRENEURS

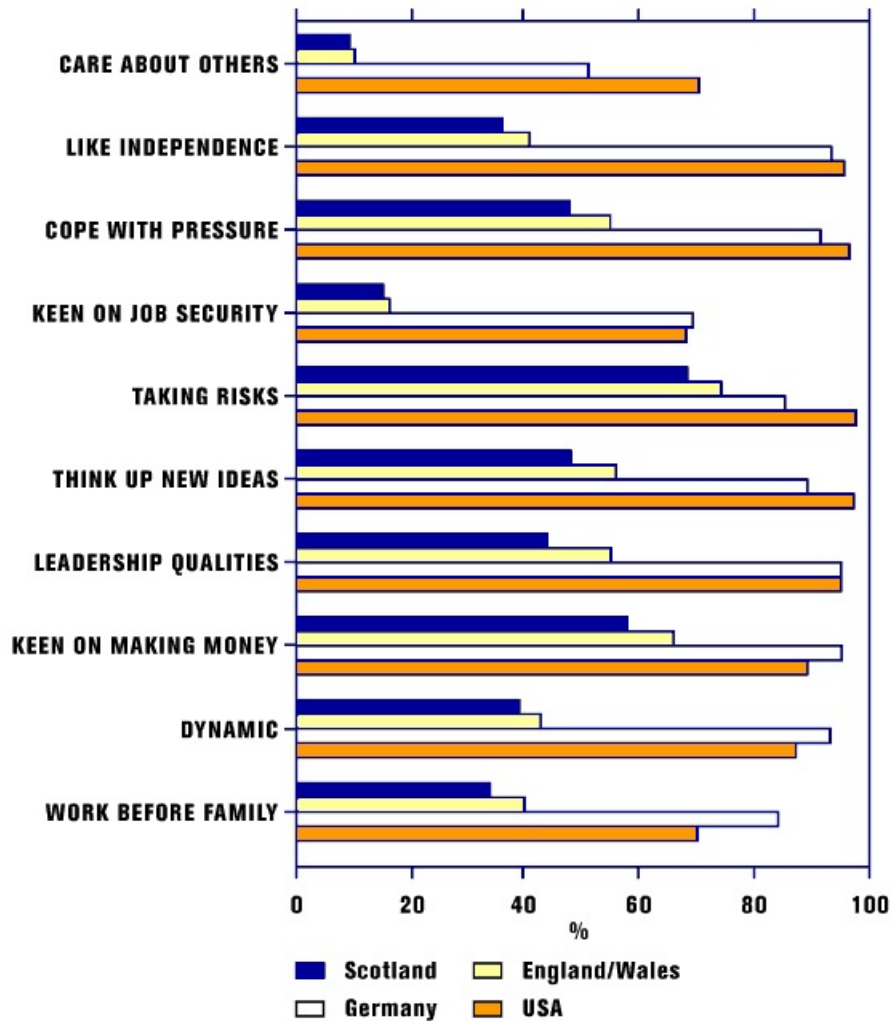


Figure 6.3

The SE analysis concludes that concerns over displacement dominate much thinking, while there is scant recognition given to the longer term processes of innovation, dynamism and efficiency. Protecting the status quo is preferred to encouraging indigenous start-ups (SE 1993, 23). Research such as that done by SE is indicative of a wider, growing interest in the concept and importance of social networks in the entrepreneurial creation process. Recognizing this interest, SE addressed the role of networking directly. Its analysis revealed Scotland as having a more extreme set of rules and social mores in determining support and advice. Those who would have most difficulty establishing a business elsewhere - the young, women and the working class, appear to face higher hurdles in Scotland than in the southeast of England and beyond. Lack of security and of alternative employment in the event of failure, and the effects on family life of creating a new firm are the major concerns of potential entrepreneurs according to the SE report (1993, 24). The report expressed the view that these problems could be overcome in some instances by wider discussions with informed contacts and with existing entrepreneurs. This seems all the more important given the less than positive attitude of business development organizations toward entrepreneurs. Unfortunately, the low level of entrepreneurship identified above becomes self-perpetuating in these circumstances, compounding the earlier barriers to enterprise.

Knowing an entrepreneur is an important rocket for changing someone from a potential to an actual business creator. Those who are most dissuaded from making the transition are least likely to have a set of relevant contacts. In addition to financial support problems, the greater severity of funding problems in Scotland is associated with the lower degree of penetration of the ideology of the property-owning democracy there.

With the United Kingdom's funding bodies showing a preference for mortgages on borrowers' homes to be used as collateral, there is an additional barrier to establishing companies in areas where owner occupation of housing has tended to be low traditionally.

McNicoll (1996) and Whittam and Kirk (1996) have discussed this set of elements in more detail. McNicoll, on behalf of SE, concluded that encouragement of the idea of entrepreneurship would often be sufficient to prevent most potential ventures from failing to reach the starting line, despite the environment of hurdles and obstacles. Struthers et al. (1996) add an interesting discussion of recent developments in Russia, where the restructuring of the last few years has highlighted a number of key issues. Not least among these are the importance of market defining characteristics (indeed prerequisites) of property rights, contract laws, information, and degrees of risk and uncertainty. The influence of organizations and individuals within current and former networks is shown to be significant in the processes of new firm formation and business development. This discussion of the role of information and networks is extended by Devins (1996), when he considers measures taken to overcome market failure to provide business advice and knowledge. The dual need to monitor and evaluate advice programs and services, and to know the companies supported, are seen as essential to the long-term health of the new firm sector.

Curran and Leitch have presented (Figure 6.4) a stylized account of the development of linkages and networks as they affect different-sized companies and organizations in response to external environmental changes. Examples of such changes include the establishment of the single European market and new forms of enterprise regulation. Such changes always affect and are qualified by the system and strength of the local and regional networks within a locality.

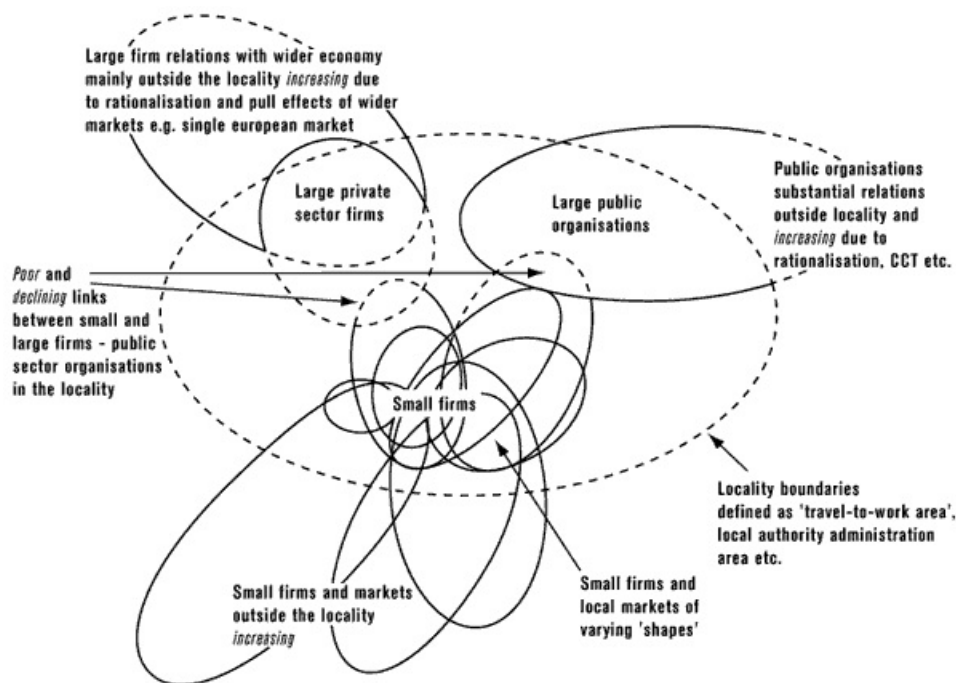


Figure 6.4

Harrison and Leitch (1996), in considering Northern Ireland's experience, argue for the establishment of entrepreneurial teams to progress business ideas and opportunities, positively assembling a collection of talent and expertise, rather than an approach that passively supports the market. The consensus, here as earlier, is for intervention to overcome market failure in labor, capital, land, and knowledge sectors, but to address the establishment of trust and cooperation directly.

In summary, the business birth rate strategy in Scotland has tended to be passive with regard to the promotion of trust and cooperation. Networking is identified as important but is to be encouraged at the level of the individual entrepreneur on an atomistic basis. This approach to networking contrasts sharply with the extensive and successful model of regeneration established between the regional economic development

agencies and organizations themselves, and with the industrial clusters of traditional sectors that created the nineteenth century Scottish economy.

6.5 Conclusion

In this paper we have argued that the economic development of the Scottish economy suggests that there is scope for the establishment of networking arrangements once again. To ensure the success of potential networks, SE needs to move from contractual trust to goodwill trust within the networking arrangements. To achieve this it is necessary to develop a group approach to firm organization. This requires the involvement of all potential firms in the decision-making process to make sure that the needs of the firms are being catered to within the networks. This collective approach is required because the services being delivered within the network of firms will consist of elements of public goods such as information. We have noted that within networking arrangements punishment strategies exist, but rather than prohibiting trust, these strategies can enhance it, acting as a safeguard mechanism. With an economy dominated by branch plants, however, it is unclear how multinational enterprises can be encouraged to adopt more cooperative strategies, and so to become more embedded into the Scottish economy.

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7 Regional Development and Multilevel Governance

7.1 Introduction

The addressing of regional problems throughout the developed world through regional industrial policy and regional planning has fluctuated according to relative economic performance, political support and ideology, and policy priorities. Regional intervention has undergone various metamorphoses, such as the growing use of RDAs. It has also reflected other influences, including European Union funding on that continent and the perceived benefits of relying on inward investment rather than indigenous growth.

As has been argued here, no singular approach or theory can lead to a full understanding of all the forces and pressures on decision-makers to adopt a particular approach to regional economic development. Some (e.g. Wannop 1995) have noted, therefore, that an analysis and an understanding of regional intervention and regional planning has to take account of wider political analyses. This signifies a new appreciation of the form, nature and potential of mechanisms and instruments of regional intervention. Thus, "since regional issues are recurrent, regional planning and governance are essential acts in continually managing an imperfect system of governance" (Wannop 1995, xxi).

The environments of such federal states as the United States and Germany suggest a different set of relationships between different levels of government than more centralized countries such as France and Italy. The political context of regional policy and regional planning in the United Kingdom, for instance, has been that of a unitary state. Within this context, the partial devolution of responsibility for administration or implementation was performed according to geographical area (Scotland, Wales and Northern Ireland) and function (including training and development agencies). In the last two years of this millennium, however, political changes are accelerating the slow devolution of administrative powers. Thus, alternative constitutional arrangements are being put into place that will transform the context within which regional governance and intervention takes place. Debates over such arrangements are not new: Kindle (1997) highlights the role federalism has played in constitutional debates in the United Kingdom at different times.

This section addresses the issues of regional constitutional change, regional autonomy, and regional planning and policy. It calls upon the revealed experiences of a number of states with a variety of constitutional forms in evidence. The discussions in this section are concerned specifically with the appropriateness of regional intervention under alternative regional forms of governance. In the United Kingdom, in particular, the introduction of a Scottish Parliament, a Welsh assembly and English regional assemblies poses challenges and opportunities for regional policy and planning. The United Kingdom's political agenda appears to favor a regionalization of governance and posits a recognition of a regional problem in terms of relative economic, social and environmental indicators. This is ironic because at the same time, the new constitutional arrangements require careful consideration of the appropriateness of existing regional instruments. Horsman and Marshall (1995, ix) address the need they see for economic changes on a larger scale; "The traditional nation state, the fruit of centuries of political, social and economic evolution, is under threat. Changes in the structure of the international economy, technological advance, and the end of the Cold War will force - indeed are already forcing - a realignment of the relations among states, citizens and the international economy."

A further irony can be seen in the apparent contradictory growth of regionalism or nationalism at the same time as the growth of the supra-national powers of the European Union. This is happening through closer scrutiny and regulation of the national policies of the member states of the European Union, and through increased intervention in the regional and national restructuring programs in these areas.

Undoubtedly some of the strongest forces acting on the communities, regions and nations throughout the developed world arise in the globalization of production and markets. The Group of Lisbon (1995) articulated some of the pressures brought about by these processes of global competition that are redefining the central role played by the nation state and national capitalism. The Group points to the increasing complexity of world events, the power of globalization, the fragility of the ecosystem, the threats to global political

democracy, scientific and technological change and “the paucity of social justice and of cultural dialogue and tolerance” (Group of Lisbon 1995, 141).

This quote also serves to illustrate the international dimension to the research agenda of this piece, and the need for the academic, policymaker and practitioner communities wherever they are located to refer to experiences outside of their areas to enlighten debate. Similarly, what is clear from much of the literature is that, although many authors may draw on fiscal federalism and networking theories to explain or understand the likely consequences of changing patterns of regional governance, they demonstrate the paucity of many economic approaches to the analysis of the links between varying levels of regional autonomy and economic development. This confirms the need for a wider reading of the literature than a simple single discipline approach, and especially a better appreciation of the significance of shifts in behavior and attitudes arising from changes in regional governance forms.

There are three organizing themes to this section: the first concerns the forms of federalism and networking that are appropriate to regional economic and constitutional autonomy. The second sets out the evolving ideas associated with regional governance, institutions and development. The third theme concerns the fiscal and monetary regimes appropriate to regional autonomy and regional economic development.

7.2 Federalism and networking

Roberts (1997)²⁸ provides a comprehensive overview of changing regional constitutional forms and the appropriateness of arrangements for regional planning and regional economic development in the United Kingdom. He refers to the extensive European research on such forms of governance, documenting new and emerging challenges to traditional regional planning practice and changes to the institutional context within which regional planning operates. In highlighting the dynamics of regional planning, Roberts makes reference to three crosscutting themes which he argues will dominate debates about appropriate regional problems, policies, instruments and institutions in the next few years. These themes are territoriality, sustainability and spatial competence. In particular, he suggests that regional planning in the future will have to address the delicate relationship between economic progress and environmental quality within a sustainable framework. These themes will need addressing, he argues, whatever the constitutional agenda of the United Kingdom. Furthermore, he points to the need to be able to devise and to implement strategy as the bedrock of regional planning.

The discussions pursued by Roberts are useful in highlighting the differences in the relative competence of regional and local authorities across the European Union and beyond. Following Wiehler and Stumm (1995)²⁹ four groups of subnational government can be classified:

- Regions with wide-ranging powers (e.g. the German Länder)
- Regions with advanced powers (e.g. the Spanish autonomous communities)
- Regions with limited powers (e.g. Dutch provinces)
- Regions with no powers (e.g. the Greek nomoi, Portuguese planning regions, Irish counties, English counties, and Northern Ireland)

Recent developments are obviously changing this list, with Northern Ireland in particular moving up the ladder of autonomy. Nevertheless, the variety within the European Union is clear, and it stands in contrast with the position and indeed the stability of the central-local government relationships in such nations as the United States.

The lack of spatial competence, the imposition of top-down policies and other reasons blamed for the failure of regional planning by Roberts (1997)³⁰ have gradually been addressed *within the European context* by a move back toward enhanced regional autonomy and responsibility. The significance of the European dimension

²⁸Sustainability and spatial competence: an examination of the evolution, ephemeral nature, and possible future development of regional planning in Britain’ in *Regional Governance and Economic Development*, M Danson (ed.) , European Research in Regional Science 7, Pion: London.

²⁹The powers of regional and local authorities and their role in the European Union.’ *European Planning Studies* 3, 227-250.

³⁰Roberts *op cit*

cannot be neglected here. The European regional structural funds, and their preferred delivery mechanism of the partnership model, have been critical not only in establishing regional networks of agencies and authorities, but also in creating the conditions and environment for quasi-regional governance structures. These have undoubtedly been instrumental in convincing the administrations of some national governments that greater devolution has benefits.

These points are echoed by Armstrong (1997)³¹ who, in the context of the proposed English regional assemblies, draws out the characteristics of multijurisdictional planning frameworks in which the principal issue is the optimal assignment of functions. While confirming the theoretical case for regional level institutional intervention for the purposes of regional planning and development, Armstrong stresses the need for flexibility to allow for the different interests involved at the subregional level. The subregional level has remained a relatively isolated area for debate, although attention is now being paid to the role of local government within new forms of regional constitutional governance (Sinclair 1997).

Cappellin (1997) has examined the nature of federalism and the network approach to national regional policy in the volume that contains Roberts's and Armstrong's works³². He views these as a means of facilitating the cooperation and/or competition between different national and regional institutions. He stresses a new approach to regional development policy and planning within a federal arrangement based on public-private partnership (rather than on public authority). The aim of the partnership approach is to create flexible mechanisms of governance of those public-private relationships in order to establish a strategic agenda for change. This can be achieved through the establishing of networks that stress the transactions between institutions and partners rather than the older prescriptive or centralized "top down" system.

These studies show that there are connections between the different areas of governance and methods of analysis. The micro-, meso- and macro-levels obviously interact in ways that make it difficult to separate the varying forces and forms of influence.

Haynes, Maas, Stough and Riggle (1997)³³, in contrast to the pictures painted of these fairly centralized countries, have analyzed the experience of regionalism within the federal systems of government in Germany, Canada and the United States. In particular, they consider the obstacles to establishing and maintaining regional coherence in policy and planning. These include sectoral bias and the emphasis of the role of institutions and policies in regional representation and empowerment. Their discussion of regional development within a federal system offers some important insights into planning intervention at a regional level in a unitary state. The principal lesson it offers is that it is important to acknowledge that policymakers are dealing with regional jurisdictions in a constant process of dynamic realignment. The authors reach the conclusion that a federal system does not automatically imply that the regional dimension is recognized or that appropriate arrangements flow out of federal institutions.

Returning to the theme of networks, Eser (1997) examines the lessons that city networks have provided Germany. In Germany, city networks represent a form of strategic planning within a federal system. Eser views these as a form of regional planning mechanism that can secure a strategic perspective on meeting the needs of economic development in localities where economic spillovers exist. He stresses, however, the extent to which normative issues can be integrated into the networking approach to regional planning and development.

7.3 Governance, Institutions and Development

As described elsewhere in these learning materials, the arrangements for regional governance are changing within the United Kingdom especially radically. The changes have provided a rich source of material for political scientists in recent times, and a proving ground for a limited number of economists to try to understand the implications of such changes for the economic development of particular areas. Nowhere are

³¹'Regional-level jurisdictions and economic regeneration initiatives' in *Regional Governance and Economic Development*, M Danson (ed.), European Research in Regional Science 7, Pion: London.

³²'Federalism and the network paradigm: guidelines for a new approach in national regional policy' *Regional Governance and Economic Development*, M Danson (ed.) , European Research in Regional Science 7, Pion: London.

³³'Regional governance and economic development: lessons from federal states' in *Regional Governance and Economic Development*, M Danson (ed.) , European Research in Regional Science 7, Pion: London.

these proposed evolutions going to have an impact more strongly than in Scotland. Scotland now has its own democratically elected Parliament for the first time in its history, which is remarkable given the span of its history.

In work joining a growing library of publications on the devolved Scottish Parliament, Newlands (1997) has considered its economic powers and potential³⁴. The Parliament will represent a new form of regional government in the United Kingdom, and Newlands draws on economic theory to explore the potential impacts of such a body and its related powers. Drawing from the American literature in particular, Newlands focuses on the fundamental macroeconomic objectives of government: stabilization, distribution, allocation and growth functions. Newlands argues that the focus of debate and appraisal is most appropriately directed at the processes of sustaining growth and development. This allows him to demonstrate that such a body as the Scottish Parliament may benefit those beyond its own boundaries and the national economy. Significantly, and appropriately, he stresses the uncertainties associated with establishing this new form of regional government and the care that will have to be exercised in its execution and implementation. Newlands argues that in many areas and communities, the development or devolution of specific new regional powers can lead to “backlash” effects and other reactions that may undermine any universally favorable developments. Such analyses as Newlands’s, based on successful and stable models elsewhere, can be applied to prevent unfavorable effects of devolution. Newlands’s line of argument links explicitly the key issues of taxation, expenditure and economic growth to a subnational layer of governance, and to the [Scottish Parliament](#) in particular.

A particular area of debate in any country concerns the direct financial costs of operating a local or regional government. Bryan and Hill (1997) have discussed³⁵ the costs and benefits of a Welsh Assembly, again by referring to the United States’s federal literature³⁶ as enlightening for the regional scientist. They concentrate on an investigation of the synergies made possible between government agencies and departments and other organizations within an area once devolution of power is introduced. However, although they see the potential for specific improvements, enhancements and innovations in linkages between economic agents and players within Wales after the establishment of a Welsh Assembly, they view the importance of subjective views as being as powerful as economic logic in the final public analysis.

Hill and Morgan (1997) also consider the interactions between inward investment, supplier networks and regional growth within a regional governance framework. They examine the trends in foreign direct investment and its impact on regional economic development in Wales. In analyzing the characteristics of growth potential through inward investment and the importance of networking and facilitating vertical and horizontal links between firms, they highlight the anticipated advantages of embedding existing foreign direct investments into the regional economy over the attraction of new projects.

Continuing on this theme of the key lubrication qualities perceived to flow from regional governance incentives, Raines and Wishlade (1997)³⁷ discuss cross European perspectives on the use and control of financial incentives in foreign investment promotion. They consider the propriety of using incentives for foreign direct investment in regional economic development and the extent to which European Union and national regulations can modify such arrangements. Their discussion provides an important insight into how external environmental changes around regional institutions impose potential limitations on regional planning and policy strategies. The key role played by the “civil service” of the European Union - the European Commission - is stressed by Raines and Wishlade as well as other commentators; however, they recognize the limited competencies and effective powers of the Commission. Its reliance on member states to police many of the regulations and its requirement to pay heed to political considerations restrict its autonomy in reality. Raines and Wishlade’s work helps confirm to the regional scientist the need to apply a range of expertise and disciplines to evaluations of the relationships between multilevels of governance.

³⁴See both his chapter ‘The economic powers and potential of a devolved Scottish parliament: lessons from economic theory and European experience’ in *Regional Governance and Economic Development*, M Danson (ed.) , European Research in Regional Science 7, Pion: London, and his jointly edited book with John McCarthy.

³⁵‘The costs and benefits of an Assembly for Wales’ in *Regional Governance and Economic Development*, M Danson (ed.) , European Research in Regional Science 7, Pion: London

³⁶They cite the work of P Peterson in particular *The Price of Federalism*, The Brookings Institute, Washington DC, 1995.

³⁷In *Regional Governance and Economic Development*, M Danson (ed.), European Research in Regional Science 7, Pion: London

7.4 Fiscal and Monetary Regimes

Finally, this section considers the nature and appropriateness of different monetary and fiscal regimes for regional autonomy. The financial settlement between different layers of a multigovernance system can create tensions and conflicts that may negate many of the advantages of devolution and regional autonomy. One of the principal needs of late, therefore, in those states which have been decentralizing, as well as within the European Union as whole, has been to try and introduce a more objective and less emotive approach to analyzing the funding and expenditure plans for regional and other subnational governments. Laramie and Mair (1997)³⁸ have applied experiences and theories developed in North America, but especially the arguments developed by Keynes's contemporary, the Polish economist Kalecki³⁹, to examine the macroeconomic effects of regional tax differentials. Laramie and Mair's work was undertaken with special reference to the so-called "tartan tax," which will be associated with the proposed Scottish Parliament. The tartan tax is a local income tax to be applied in Scotland, and its application will mark the first time such a regional tax has been imposed in the United Kingdom. Laramie and Mair consider this in the context of economic growth and make a case which is well founded in theory for a property based source of finance for the Parliament.

As it is providing such an interesting experiment in the United Kingdom, and as it may have far reaching consequences for the continuation of this particular union, there has been a rash of papers and studies on the effects of the "tartan tax." McGregor, Stevens, Swales and Yin (1997)⁴⁰ have provided a more detailed analysis of the financial aspects of a Scottish Parliament and an evaluation of a tartan tax. To undertake this analysis, they utilize their computable general equilibrium model of the Scottish economy, a "flex-price" model, to estimate the likely impacts of devolution in a very open regional economy. Scotland operates within the customs union of the European Union with all its restrictions on anti-competitive behavior, and has a very high propensity to export - in reality it serves as production base for non-European multinational enterprises to enter the European market. Therefore, many of the traditional levers open to an independent state are not available to it. As with other authors discussed above, MacGregor et al. argue that the link between macro policy and regional development is an important theme in composing the arrangements for regional governance and autonomy. They also stress, however, that there is a need for positive intervention in the economy to realize the benefits of devolution, opening up discussion on how potential advantages can be gained through the involvement of the social partners in wage bargaining, investment and public expenditure and budgeting strategies. Within the framework of a balanced budget strategy, they demonstrate how an expansion of the Scottish economy could be achieved, but apparently only with a social contract between labor and the Parliament.

In other contexts, especially federal countries, there are usually better developed methods of dealing with inter-regional financial settlements. Established traditions, practices and systems of constitutional law address the problems of multigovernance structures. Kellerman and Schmidt (1997) have looked at the German case to investigate how such settlements relate to growth and development across the country⁴¹. They offer an insight into the different arrangements for taxation policy and regional development in a federal system. They demonstrate different mechanisms and philosophies for transferring finance and resources from region to region within such a country. Such flows are considered to be the costs or the lubricants necessary to maintain the viability of the federal nation state, and they may promise advantages to all parts of the country. Their analysis suggests that a tax sharing system can lead to a more efficient inter-regional allocation of capital with a possibility of higher national aggregate growth. It also serves as a reminder of the differences between a true federation and that definition of the European Union used by Eurosceptics (or more correctly Europhobes) in Britain to describe the present constitutional governance of the European Union.

Finally, there have been a host of studies on the how idiosyncrasies of particular regions, conurbations and communities can explain the relative good or poor performance of different areas. Doeringer, Terkla and Topakian (1987), for instance, have captured the essence of this genre in their volume entitled *Invisible*

³⁸'Macroeconomic effects of regional tax differentials: a post-Keynesian analysis' in *Regional Governance and Economic Development*, M Danson (ed.) , European Research in Regional Science 7, Pion: London

³⁹'A theory of commodity, income and capital taxation' *Economic Journal* 47, 444-450.

⁴⁰'Some simple macroeconomics of Scottish devolution' in *Regional Governance and Economic Development*, M Danson (ed.) , European Research in Regional Science 7, Pion: London

⁴¹'Regional growth and convergence in a tax-sharing system' in *Regional Governance and Economic Development*, M Danson (ed.), European Research in Regional Science 7, Pion: London

Factors in Local Economic Development (1987)⁴². Porter's study, *The Competitive Advantage of Nations* (1990)⁴³, has been applied at several levels of multigovernance systems. Porter notes the increasing openness of national and regional markets. He demonstrates, though, that in an progressively globalizing world with restrictions imposed by such organizations as customs unions and the World Trade Organization, there are still areas for fruitful discretion in policy terms for local, regional and subnational governments and their partners. Dow (1997)⁴⁴ discusses an example of the use of such discretion when she considers the role of financial sector and monetary policy under a regional government, in this case Scotland. Dow draws parallels with other systems. But adopting a traditional Scottish Political Economy approach, she also draws upon the distinctiveness and historical significance of the country's banking sector to argue that major innovations can be introduced in credit policy to the benefit of both industrial and economic objectives. Perhaps most important in her analysis is the identification of the ability of regional governments to intervene in their economies in imaginative ways that fit their constituencies' needs more neatly than the top-down approaches of the unitary state. Whether the key players in the financial sectors of these communities wish to realize this is, of course, another matter.

⁴²P.B. Doeringer, D.G. Terkla and G.C. Topakian, 1987, New York: OUP.

⁴³1990, London: Macmillan.

⁴⁴'Scottish devolution and the financial sector' in *Regional Governance and Economic Development*, M Danson (ed.) , European Research in Regional Science 7, Pion: London.

8 An Examination of Two Case Studies

8.1 Introduction

In this section we look at two case studies that highlight several of the main points raised in previous sections. The first case study focuses on the industry districts of Emilia Romagna in northeast Italy. These spatially specific production systems have been widely researched and are identified as “the model” of contemporary Marshallian industrial districts. The operation of these districts identifies the productive system beyond a narrow interpretation of the productive system concept, as definitions in section 2 made clear. The governance structure of these districts is regarded as being based on trust and cooperation, so an examination of the districts will help demonstrate a system in which these concepts are significant.

8.2 Third Italy

Of all the regional economies in which industrial districts have been “discovered,” the districts of northcentral Italy are the most widely cited. These districts are commonly known as the “Third Italy” to distinguish them from the established industrial districts of northern Italy and the relatively under-industrialized southern Italy. It is to a review of the literature that describes the establishment of the districts of the Third Italy that we now turn (See Bergman and Feser, “Industrial and Regional Clusters: Concepts and Comparative Applications” in the Regional Science Web Book for further information).

See Figure 8.1: Pattern of light industrialization locals systems: the Third Italy and Figure 8.2: Marshallian industrial districts within the pattern of light industrialisation local systems 1981.

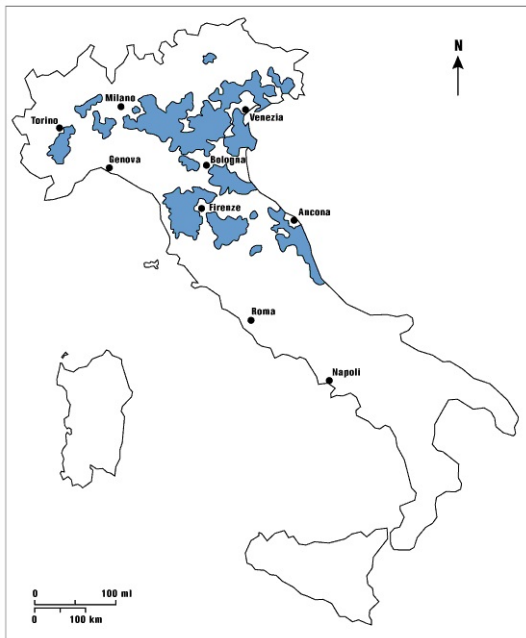


Figure 8.1

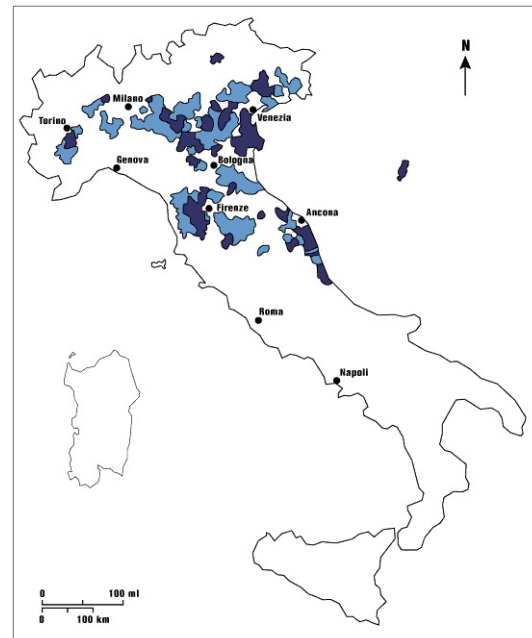


Figure 8.2

Brusco (1982) argues that the historic development of the districts can be found in viewing the specific industrial development within the region. In particular, Brusco identifies two developments that gave rise to the dominance of small medium enterprises (SMEs) in the region. The first was the growth of the traditional artisan sector; the second was deconcentration and the rise of subcontracting. This rise in deconcentration was due to two factors. The first was the rise of a strong trade union movement in the 1960s within the then dominant large firm sector. To counteract the organized labor force the large firms followed a strategy of contracting out to the SME sector. The second factor was the changing nature of consumer demand away from standardized mass consumption goods and toward high value-added, differentiated goods and services. This switch in demand gave rise to different types of techniques of production, such as flexible specialization,

which gave SMEs a competitive edge.

Within the industrial districts of the Third Italy, however, there were also policy initiatives which encouraged SMEs generally and artisan firms in particular. Artisan firms, or *artigiano*, refers in the Italian context to craftsmen and craftswomen who not only work as skilled workers but also engage in the organization and the running of businesses (Best 1990). The legal position of an artisan firm, according to legislation passed in 1986, states that the owner of the firm must be a working manager and that at least one other member of the firm must be from the same family. Incentives exist to encourage firms to register as artisan firms as opposed to industrial firms.

In analyzing how the artisan firms became established in spatially specific industrial locations, that is, industrial districts, Brusco makes a distinction between two stages of development. The first stage was characterized by public bodies' encouragement of the artisan firms in a manner that lacked an overall policy framework. What this stage witnessed, though, was increased cooperation between the artisan firms and policymakers and enforcers. The second stage saw the establishment of specific agencies such as Real Service Centres, which led to the development of networking between the artisan firms and the policy agents.

This second stage involved a more proactive industrial policy on behalf of policymakers. This policy, for example, led to the establishment of artisan parks on land purchased at favorable prices from the large landowners. This activity involved the local authorities working with the artisan associations, the banking sector and landowners (Brusco 1989).

Alongside proactive policies such as the acquisition of land at favorable prices, the artisan firms themselves formed organizations such as Artisan Associations to promote policies and institutional frameworks that would help them to be successful. The local Artisan Associations are affiliated with the Confederation Nazionale Dell'Artizianato (CNA). The Associations, both nationally and locally, are organized through a democratically elected management committee, the majority of whose members must themselves be artisans. This has led to the artisan firms being able to reap internal and external economies of scale and to develop a degree of cooperation that has been essential for the success of the proactive industrial policy pursued in the region.

In analyzing the activities of the CNA, Best (1990) found that it was the largest of four national confederations of artisan firms. Within the province of Modena, the local CNA branch has 14,000 member firms (representing 39,000 workers), and sixty locations within the province for supplying administrative services to artisan firms, such as accountancy, financial and marketing services. The provision of such services by agencies inspired by the CNA has been likened to small firms having the headquarters of a large firm, enabling the members of the CNA to accrue both internal and external economies of scale. Indeed, it has been argued, "scale economies at the level of the firm are hypothesized to have become less important, altogether, replaced by the achievement of such efficiencies at the level of the district (or network) as a whole" (Harrison 1990, 5). A survey of small firms by the Small Business Research Centre (1992) demonstrated a link between the amount of external advice taken and the rate of growth of small firms. The provision of services provided by CNA-inspired institutions, then, would appear to be fundamental to the growth and development of small firms.

Additionally, the CNA is involved in Loan Guarantee Schemes such as the Financial Consortia operated in Modena. The scheme is based on cooperation between small firms and local and national government and is operated by a board representing member firms and the CNA. The loan guarantee fund consists of moneys from local, regional and national government plus firms' membership fees. Any member firm requiring a loan obtains a report from the local CNA which, if approved by the local CNA and the Financial Consortia, is sent to a bank with a loan guarantee (Best 1990). There is a twofold enforcement mechanism designed to ensure that firms do not abuse the scheme. First, "self-policing" ensures as far as possible that only potentially winning ideas are promoted for finance, and second, firms that default can be barred from applying again. The success of the scheme can be gauged by the low level of bad debts; according to Best (1990) less than 0.2% of borrowers default on their loans. As Brusco comments, "the person who receives a loan from the co-operative will stay up at night thinking of ways of repaying his loan; whereas the person who receives a bank loan will stay up at night thinking of ways of not repaying his loan" (Brusco 1985).

A further initiative was launched in the mid-1970s and 1980s, that of the Real Service Centres, coinciding with a more proactive policy stance from the state agencies. ERVET (Regional Board for Economic Development)

was set up in 1974 by the regional government of Emilia Romagna “to foster economic development and upgrading in Emilia Romagna” (ERVET 1991). In an attempt to achieve this objective ERVET “provides real services either supplied directly by the corporation or through ERVET System’s network” (ERVET 1991). *Real Services* have been defined by Bellini as a set of service activities that “generate structural rather than temporary changes in the organisation of production within a company” (Bellini 1990, 173). Hence, the collective service sector is directly involved in activities related to the circulation of information, training, working out of plans, research activity and the circulation of innovation, each of which focuses on three main areas, sectoral projects, horizontal projects and territorial projects (Cooke and Morgan 1991). Furthermore, ERVET seeks to operate with a public-private mix along with “credit and financial institutions, entrepreneurial associations and Chambers of Commerce” (ERVET 1991), thus developing networking practices. The structure and policy development of ERVET reflects the economic, social and political structure of Emilia Romagna.

It is important to distinguish the role and function of ERVET from the typical regional enterprise agency. ERVET, in particular, does not seek to encourage direct foreign investment or give direct grants; instead, it provides real services for which firms pay a fee. The objective is that service centers such as ERVET provide the kind of services that large firms frequently conduct in-house (such as R&D, promotion of new technology, marketing) to the small firm sector. The advantage to firms that use ERVET is that they gain access to business services at a price below that which they would have to pay if they used the private consultancy sector. ERVET provides structural services that are consistent with its overriding aim of facilitating the long-term economic development of firms and networks within the region. In short, ERVET enhances the survival prospects of artisan firms by allowing small firms to compete on more even terms with large firms.

For example, ERVET promotes new technology activity by playing a coordinating role between small firms in specific industries and interindustry agencies such as ASTER (Agency for Technological Development of Emilia-Romagna). These alliances aim to ensure that the small firm sector has access to the latest computer technology and does not suffer a cost disadvantage. This type of activity tends to be sector specific: for example, CERAL (the Emilia-Romagna Centre for the shoe industry) provides technological information so that firms in the shoe industry remain competitive in the market. At a broader level, the service center provides a vast array of activities such as export promotion, access to European Community R&D programs and projects aimed at environmental issues, such as industrial dereliction and pollution.

Additional service provisions are supplied by other service centers, again operating on two levels, the sector and regional. At the sector level these centers cater to firms within their specific sector; at the regional level they are concerned with issues such as technology transfer and export promotion. The economic rationale can be seen to be arising out of market failure: “First of all, the initial investment required to put together the kind of knowledge necessary to carry out this type of activity is quite high. The market itself is also fairly small ... these kind of activities are specific to certain sub-sectors which include only a limited number of firms ... the centres are not an invasion of the field occupied by private industry, but rather an initiative to combat the insufficiency and incapacity of the market itself” (Brusco 1989, 417). Public financing of the centers has a limited duration (a period of about five years). The idea is that the public authorities should shoulder an important part of the initial investment, and then the centers should become self-financing.

Typical of the sector specific centers is CITER (Centro Informazione Tessile Emilia-Romagna) which operates in the knitwear industry, centered in the province of Modena. CITER was established in 1980 by ERVET and key players in the region, notably an amalgam of artisan associations plus two other industrial associations. The idea of this particular sector specific service center arose out of a training project sponsored by ERVET.

The activities of CITER involved the development of a product called *Citera*, which is a computer aided workstation for the design of knitwear. Citera was developed in conjunction with ENEA (the Italian Commission for Nuclear and Alternative Energy Sources) and enables fashion designers to gain rapid recall of thousands of images and colors. This enables the knitwear industry within the region to maintain a competitive edge over low-cost imitators by speeding up the turnaround time from design to finished product. What is being achieved for the SMEs in the region is external economies of scale through cooperation. The cost of using this new technology would be out of the reach of the individual firm, but for a small fee firms can utilize these facilities through the service center. The application of new technology to knitwear design and fabrication constitutes a strategy that plays to the strengths of Italian fashion and stands in contrast to

the approach adopted by much of the United Kingdom's textile industry, which relies exclusively on cost cutting. The use of such innovative techniques as Citera has drastically reduced the time taken from design to production of a finished product from months to days, and Citera has helped in the development of the concept of *ready fashion*.

CITER is but one example of the collective service centers developed in Emilia-Romagna. Similar centers have been established in other industries including agricultural machinery, footwear, construction, ceramics, metals and mechanical engineering (ERVET 1990).

See Figure 8.3 Marshallian industrial districts, according to dominant manufacturing industries, 1981.

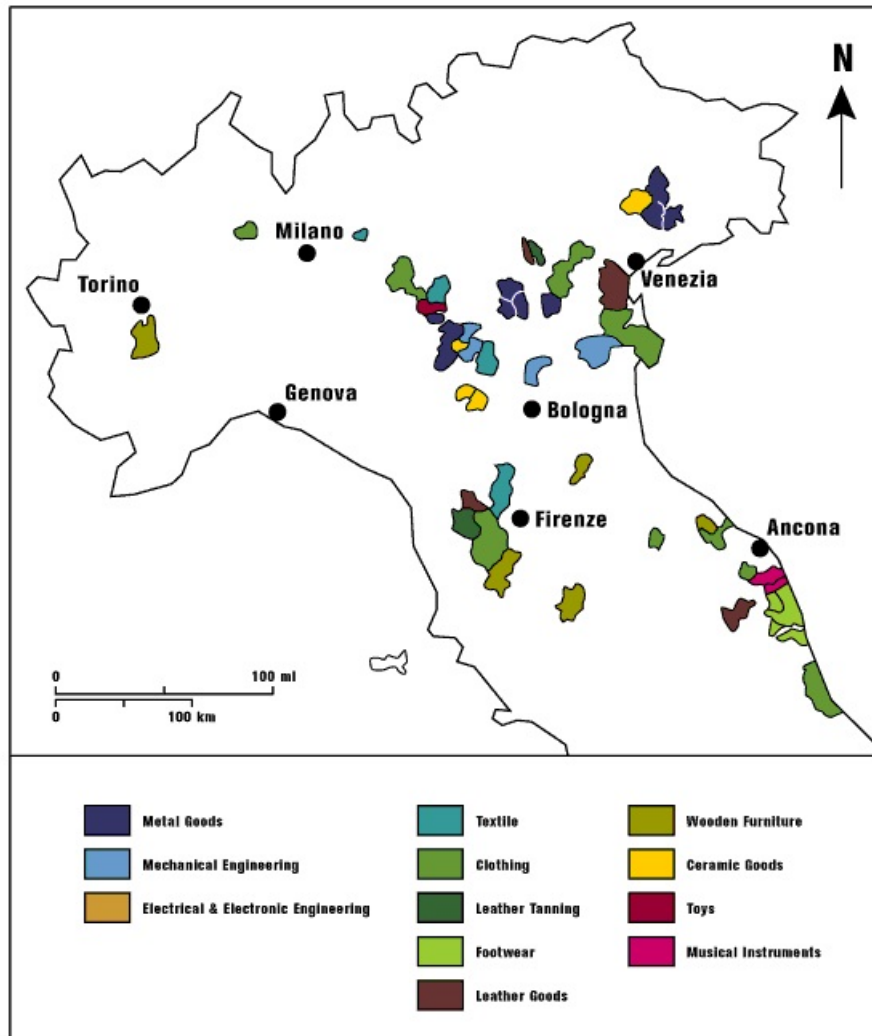


Figure 8.3

The networking relationships developed within Emilia Romagna have led to the development of the phenomena now known as new industrial districts. The thrust of the policy is based on information and *real service* provision rather than grant aided assistance. Whether this concept can be applied to other regions is a debatable point. If industrial renewal is to be attempted through an industrial policy with SMEs playing a key role, the advantages of an **industrial atmosphere** should not be ignored. A networking approach promotes cooperation in the input markets by allowing SMEs to make use of economies of scale and developing the spirit of cooperation. Provision of *real services* has certainly been successful in encouraging growth and has had an important effect in moving districts towards new technology and toward upper segments of the market. But as Brusco (1988, 18) points out, “the problem which troubles many of us in Italy is whether these internal policy measures which are taken at a local level, could be used in the South of Italy to transform

clusters of firms into industrial districts.” Brusco’s view on this question is somewhat pessimistic: “there has been realised in Emilia a harmonious mixture of discordant elements, but one whose complexity makes it difficult to take as a model” (Brusco 1989, 183). While the exact experience of Emilia Romagna cannot be reproduced, understanding where the gains from production within an industrial district actually arise can assist policymakers as they attempt industrial renewal within geographically specific areas. Changing the culture of an economy has been attempted in the case of Scotland, as previous sections have outlined. Further evidence of the desire to change a way in which an establish economy operates is evidenced in “Our Competitive Future: Building the Knowledge-Driven Economy,” the White Paper published in 1998 by the [Department of Trade and Industry](#) in the United Kingdom. It is to a study of this strategy that we now turn.

8.3 Our Competitive Future

The White Paper on competitiveness was published on 16 December 1998 by Peter Mandelson, who was then the trade and industry secretary. The aim of the White Paper is to reverse the long-term decline of the United Kingdom’s economy. Along with the White Paper, the Department of Trade and Industry released a paper that provides the economic analysis for the proposals found in the White Paper. The main focus of the Analytical Report is the importance of knowledge and knowledge creation within modern industrial societies.

The Analytical Report informs us that while “knowledge has always been important, ...four mutually reinforcing processes are increasing its importance for prosperity.” It goes on to identify the processes as “Information and Communications Technology (ICT),” “increased speed of scientific and technological advance,” “global competition,” and “changing demand” (Analytical Report, 3). The report cites the World Bank’s 1998 World Development Report and OECD to reinforce the significance of the role of knowledge and knowledge creation to modern industrial societies. The document is careful to differentiate between codified and tacit knowledge. Codified knowledge is so defined if it can be written down and transferred easily to others, tacit knowledge takes time to acquire and is difficult to transfer. Tacit knowledge has been identified as a source of competitive advantage. Much of the White Paper is devoted to explaining how the roles of institutions, organizations and individuals need to evolve to capture and develop knowledge, particularly of a tacit kind, to create a competitive successful economy. In essence tacit knowledge can be accumulated from within the firm, from its employees, for example, but it may have to be gathered through cooperation with other firms and institutions such as educational and research establishments. This has led to a spatial dimension to the analysis: “In some cases, the need for proximity to other firms or a pool of skilled and complementary labour has led firms to cluster together in specific locations” (Analytical Report 1998, 4).

The organizations required to create and transfer knowledge are not necessarily new, and researchers and practitioners within regional science will be familiar with many of the concepts found in the report. The Analytical Report, underpinning the emphasis on networking and clusters found in the White Paper, highlights findings from endogenous growth theory; namely the importance of intangible assets such as human capital, R&D, brands, contacts and know-how (Analytical Report 1998, 17). However, due to the immobility of factors such as labor and due to the tacit nature of many aspects of knowledge, there is a spatial aspect to the establishment of a knowledge driven economy. It is through cooperation between the key players that firms, regions and ultimately the United Kingdom’s economy is going to be competitive. In terms of science and technology, for example, the Analytical Report explains: “To gain access to technology they (firms) must network with suppliers, customers, competitors and other users of similar technologies. ...Firms are also increasingly developing direct links with the academic science and engineering base” (7). The objective is to then create governance structures similar to those that have been observed throughout this section, namely partnerships, networks, clusters and spatially specific industrial districts.

The report argues that there are two processes at work that are leading to the necessity of greater collaboration. First, while the importance of tacit knowledge has already been identified as the source of a firm’s competitive edge, once it becomes codified it is more difficult to control than other assets of the firm. However, once it does become codified it opens up the possibility for the firm to contract out. Second, due to the high sunk costs of knowledge creation through R&D, it becomes more imperative to seek collaborators. The latter point leads to advantages of both scale and scope (Analytical Report, 20).

Utilizing the established literature on clustering such as Porter (1988a and 1988b) and with reference to

both Smith (1776) and Marshall (1890), the Analytical Report highlights the benefits in terms of economies of scope “drawing upon companies with complementary skills to bid for large pieces of work which each of the individual firms would have been unable to complete” (22). Similarly, clustering can result in savings for individual firms by bulk purchases and joint marketing strategies. Further reference is made to external economies which accrue to firms organized in a spatially specific cluster such as the establishment of specialist support services. The utilization of knowledge, particularly tacit knowledge, is further enhanced with the repeated interaction of firms that are close to each other.

The implications of the Analytical Report could have particular consequences for regional policy. Of the seventy-five policy commitments in the report, the following are of specific interest to regional scientists:

- Funding for up to 10 proposals from industrial sectors to improve supply chains following a successful program developed by the Society of Motor Manufacturers and Traders
- Refocusing regional selective assistance grants on skills, providing £39 million for a skills survey and £10 million for spending on competitiveness by RDAs
- Ministerial and regional encouragement for business clusters and networks, including a review of the planning system

Clusters that are perceived to be of national significance will receive help coordinating across government and with business. As a first step, a team led by Lord Sainsbury will promote industrial clusters in biotechnology. The planning system will be examined jointly with the Department of the Environment, Transport and the Regions (DETR) to make sure that it encourages enterprise and promotes the needs of industrial clusters.

To further encourage innovation, technology access and partnership between industry in the United Kingdom and science and technology, further proposals in the White Paper include the following:

- Doubling Department of Trade and Industry funding for “technology champions” to support the transfer of technology and knowledge between the science and engineering base and businesses
- Creating a network of partnerships to bring researchers together with businesses both large and small to share ideas and commercialize research
- Awards to support high quality research partnerships between business and universities in technology priority areas
- Measures to promote the commercialization of university research, including a new “Reach-Out” fund to encourage universities to work more effectively with business; and a £25 million Science Enterprise Challenge to create up to eight enterprise centers at universities in the United Kingdom
- A look at the working practices of public sector research establishments to ensure that they make the most of the commercial potential of their research

This case study is important because it relates much of the theory that lies behind the vast literature on governance structures to an attempt to implement policy. Within the United Kingdom, the White Paper and the Analytical Report are also better understood in the political context of the *New Labour* government and the so-called *third way*. In the White Paper’s foreword Tony Blair explains that “Old-fashioned state intervention did not and cannot work. But neither does naive reliance on markets” (1).

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Section 3

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Glossary Terms

Clusters	A grouping together of firms and institutions which can have vertical and horizontal linkages. The geographical concentration of clusters is not as important as it is with industrial districts, but clusters are more concentrated than networks. Their emphasis is on the development of cooperation among firms, with the objective of achieving synergy
Constructive Cooperation	The phrase “constructive cooperation” was first used by Marshall in his description of industrial districts. The implication is that economies beyond those expressed in internal or external economies can be gained from cooperation between firms in the same industrial district. Within Marshall this cooperation exists “without any apparent drift to use it as a means of maintaining prices.”
DTI	The UK government department responsible for trade and industrial matters.
DETR	The UK government department responsible for the environment, transport and roads in England. Responsibility for these matters has now been devolved to the Parliament in Scotland and the Assemblies in Wales and Northern Ireland.
Evolutionary economics	These are observed to have grown out of the institutionalist school. There is an underlying vision of dynamics which is evolutionary, in the biological sense, in character. The evolutionary concept is a counter-position to that of static equilibria. The question of incorporating evolutionary dynamics into economics was raised at the beginning of institutionalism by Veblen and even earlier by Marshall.
Governance	Governance refers to the patterns and distribution of the institutionalized capacity to take and influence decisions with regard to a particular locality. Regional governance and regional institutions came to the fore in the 1980s in economics and geography literature, with attention given to dimensions of the long-term future and development of particular regions and localities. Such dimensions include the institutional capacity and thickness in an area, the invisible factors in regional development, networking, and industrial districts.
Industrial Districts	Typically the Third Italy is dominated by production occurring in industrial districts. The districts are geographically defined productive systems, characterized by a large number of firms that are involved at various stages, and in various ways, in the production of a homogeneous product. A significant feature of industrial districts is that a very high proportion of firms within them are small. A characteristic of the industrial district is that it should be conceived as a social and economic whole. In industrial districts, social institutions are as important as economic.

Institutional economics

In institutional economics, final equilibria outcomes are said to be dependent on the beliefs of agents and on the nature of institutions. Institutional economics defines institutions as any shared rule or sets of rules which guide individual behavior by supplementing the conventional utility maximizing calculation. Institutional economics reached its high point in the interwar period in the United States when it became the principal school of economic thought. New institutionalism, associated with the transaction costs school, is a latter day development of many ideas of the original institutional approach founded on a neoclassical view of economic behavior.

Industrial atmosphere

Another term coined by Marshall to discuss knowledge transfer within an industrial district. Marshall claimed that ideas, skills and innovation get passed as though they exist “in the air.”

Learning Communities

Industrialized economies are placing an increasing amount of importance on their knowledge base in order to maintain their competitive edge. The development and maintenance of an economy’s knowledge base requires learning. In a learning economy the rate of knowledge turnover is high, learning and forgetting are intense, the diffusion of knowledge is fast and a substantial part of total knowledge stock is changed every year. Learning processes have been institutionalized and feed-back loops for knowledge accumulation have been built in, so that the economy as a whole is learning by interacting in relation to both production and consumption.

Macro-level

In the context of this text, the macro-level concerns the relationship between regionally-based initiatives and the emerging system of governance at the national, federal or European level.

Meso-level

The meso-level concerns the role of development agencies and economic actors in the political make-up of their region, and involves the operation of individual agencies or networks of development bodies within the region.

Micro-level

Micro-level relationships involve the links between individual development bodies, firms and other actors and their respective environments.

Networks

Networks are the essential means of linking one group of agents to others whom they affect. They are the intricate links based on trust and reciprocal patterns of communication and exchange between producers and clients that are necessary to ensure an economic capability and responsiveness (Grabher, 1993) in support of business development.

Partnerships	Beyond simple networks, partnerships require the commitment of the agents to work fully together to address problems and opportunities. This means they must accept long term structures that work toward sustained commitment to change and the achievement of quality. They must also accept an active commitment to changing the internal operations of each agent and helping other agents to change to achieve an improved system overall. Hence networking alone is largely passive, whereas partnerships require active participation (Mackintosh 1992).
QUANGOs	Semi- or quasi- autonomous (non-)government agencies. Members of the governing bodies tend to be appointed from a variety of sources with the remit of overseeing devolved government spending in many aspects of public life, health, economic development, and public-private partnerships.
Regional development agencies	An RDA is a semi-autonomous regionally based body operating at arms length vis-à-vis its sponsoring political authority. It is a multifunctional and integrated agency, the level of which may be determined by the range of policy instruments it uses. It supports mainly indigenous firms by means of 'soft' policy instruments.
SMEs	Small and medium enterprises, usually defined in terms of number of employees. Small enterprises are recognized as having fewer than 10, 20, 50, 200 or 500 workers; medium as having more than 10, 20, etc. up to 500. Different agencies and authorities adopt different thresholds according to the period and the policy questions and instruments under consideration. Occasionally turnover is used to define the size of enterprise.
Structural Funds	The European Union funds assigned to address the structural problems of the regions and industries of the EU. They are allocated to areas according to a number of agreed objectives, defined in terms of unemployment, backwardness, declining industries, sparsity of population, and similar factors.
Taylorist	The US creed of scientific management, the application of work study and a greater subdivision of labor as a means of achieving increased efficiency (after F.W.Taylor).
Third Italy	A term coined to differentiate production in north central and north-eastern Italy which is of a different orientation than the developed North and underdeveloped South.
Trust and Cooperation	A crucial aspect of production within the industrial districts of the Third Italy is attributed to the degree of trust and cooperation which exists between the key players in the district. Economic gains can be achieved by the promotion of trust and cooperation between these key players, the firms, the financial institutions, the labor organizations, and the local authorities.