

## Regional Economic Policy Transition in Local Government of Korea

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### • Introduction

The concept of regional economic growth has a multitude of facts based on the set of features that describe the position in relation to their policy efforts. Recent world trends related to regional economic policy at the local level can be traced to several factors in that its policy progresses from direct involvement and intervention to creating a favorable policy environment thus enabling local firms to promote and develop their initiatives. It is widely recognized that traditional practices are classified as supply-oriented policy and a rising firm's managerial capacity as demand-oriented policy. The local government of Korea is not an exception to this policy after full mobilization of local autonomy in mid-1990's.

Looking at the historical process of regional economic policy in Korea, the Republic of Korea experienced rapid economic growth and transformation since the early 1960s. It went from primary industries to a modern industrial and tertiary sector, resulting in shifts in population and economic activities concentrated to the Seoul metropolitan region. At the same time, a long history of Korean migration towards Seoul in order to pursue opportunities in related to power and wealth might have contributed to a concentration of population. As the nation's capital and largest city, the Seoul metropolitan has the advantage of being the center for the major decision making bodies germane to the public resource allocation, communication and finance, as well as providing a skilled manpower and mass consumer market. During the 1970s and 1980s, Seoul continued to dominate the economy, but momentum of growth spread to areas near the capital and to the south-east provinces.

Central government policies which sought to maximize national development in pursuing efficiency may have been one major cause of increased regional inequalities, and such tendencies toward polarization may have been exacerbated by the concentration of agglomeration effects in a few favored areas, that of Seoul and Pusan. Such concentrations of population and economic activity have become a major concern to policy makers who strive for balanced regional economic development.

To date, the regional economic policies pursued in Korea have been regarded as a component of the national economic development strategy with very limited local participation. This has arisen largely because of the strong sectoral policies of central government, insufficient local financial resources for regional economic policy, the international political situation surrounding the peninsular, and South-North relationship that requires a centralization of power by the government. Recently, the Republic has entered a transitional era of regional economic policy with the emergence of statutory local development power and the mobilization of local resources. The financial crisis in Korea and economic globalization trends are other factors that necessities a demand-oriented policy direction. Recently, local government is gradually approaching policy process with an entrepreneurial state.

## • Objectives and research methods

### A. Objectives

The objectives of this research can be defined as (1) to analyze the major factor difference in regional economic policies by regions, (2) to find out the specific policy means that make its differences, (3) to estimate the impacts of policy environment in relation to its formulation process.

### B. Research methods

To achieve the above research objectives, all local governments were interviewed with prepared questionnaires in order to collect relevant data concerning major variables during April-July, 1999. 67% of respondees returned the questionnaire. the index of policy priority among other choices ranked by local policy makers, Gun as an administration unit, are consisted of 53.1% and cities as Si-unit, 46.9% over 81 reasoned regions as shown in Table 1. The index of policy priority indexes were measured as 2--highly agreeable; 1--agreeable; 0--undecided; -1-- disagreeable; -2--extremely disagreeable. Thus the higher a score on an index, the more policy it has in place to promote regional economic development. Correlation analysis and F-test methods for these index variables were employed to verify its statistical relevance.

<Table 1> Respond Regions

Regions	Number	%
Urban	38	46.9
Rural	43	53.1

## • Theories and related Research

Many scholars paid little attention to the economic development initiatives of local government. The reasons for the lack of scholarly attention may stem from the prevailing fact that economic performance has been considered the product of central government efforts. Recently an increasing number of scholars have noted, however, the development potential of policy choice made by local government themselves. Many scholars showed interested in theoretical(Eisiger 1988; Fosler 1988; Boeckelman 1996) and empirical reports( Jones 1990 ; Elkins 1966; Kossy;1966; Leicht 1994). The general consensus of these scholars is that local business climates manifest either entrepreneurial or similar conditions. Eisinger(1988) insists that the entrepreneurial state attempts to manipulate growth through both tax and regulatory policies and the pursuit of demand policy initiatives in developed countries. Similarly, Fosler(1988) argues that some local governments attempt to stimulate growth by manipulating factors that are related to he costs of capital formation. Brace(1993) also argues that the developmental activities of local governments in USA are likely to have a major effects on local economic growth in his research.

In related these new trends of local government efforts toward their own survival development, regional economic policies in this research are classified into two broad categories adopted by Eisinger' definition: supply-oriented and demand-oriented policy. Each classified regional economic policy also consists of several sub-categories and has been associated with dynamic regional changes.

## •. Present situations

Traditionally, regional economic policy in Korea has not been able to use high cost policy tools specially directed at fostering local economic development but rather contribute to the negative consequences of economic growth in the metropolitan areas. It can be interpreted as a by-product of the national economic policy in its attempt to encourage industrial decentralization from the metropolitan area in order to prevent migration to the target areas. Current regional economic policy in Korea, dealing with regional balanced development goals, is very much at a 'starting point' in terms of scope, resource, policy structure and impact (Hong, 1997). The following is an account of some of the most pressing problems:

1. Korean regional economy has a high spatial imbalance particularly concentrated in the Seoul metropolitan region in terms of gross regional domestic product, population and social infrastructure, as well as an accumulated agglomeration. The regional imbalance diversification annually grows wider than the Gini index of regional income; it increased by 23% during 1985-1993 but rocketed to 32.2% during 1994-2000 (KIET, 2001). The recent economic crisis in Korea make it clear that the high value-added and high technology industries tend to move to relatively competitive regions. One option is to compete with other regions that have an economy specializing in high-value products; this requires a high degree of competitiveness.

2. Local industries in Korea mostly consist of branch offices of firms located in metropolitan regions. These local branches primarily produce spare-parts or the production chain for their mother firms located in large cities. Local government efforts to devise effective policy measures geared toward local employment and regional income generation are hampered. Furthermore, local industries in Korea are characterized by low labor productivity traditional management structures and old production methods. Regional economic policy in Korea has been traditionally concerned with the government is role of policy provisions including tax deductions, loans, industrial site development in order to promote local industrial development and generate income. These are not easy goals to achieve its objectives in view of the present conventional policy tools for regional economic development.

3. The high degree of major economic activity concentration in the metropolitan regions results in serious socio-economic congestion without countervailing policy measures. In particular, the concentration of high technology firms, higher educational and research institutes are another factors seriously affecting increasing regional disparity. At the same time, the implementation of industrialization under the growth pole development strategy has resulted in a concentration of industries in large cities primarily Seoul and Pusan and in recently developed cities. This industrial concentration, in turn, has brought about a relative backwardness in the industrialization of smaller and remote cities, leading to unbalanced regional development. Industrial location policy as a part of regional economic development should be refocused on encouraging greater connections regional economic situation should be addressed by local governments.

4. In recent decades, the policy execution has focused on a top-down approach usually beginning with national development goals which may not be compatible with regional developmental priorities. It limits the abilities of local authorities in the design and implementation of economic development policy. Since the recipients of regional economic development programs are not clearly targeted,

the focus needs to be on small firms which support the local economy. Local authorities tend to have excessive rate burdens and bureaucracy when dealing with this sector.

## • Major Findings

Local government may affect regional economic development strategies, especially in less developed regions having a lack of resources. For example, policy makers in city areas are more likely to be influenced by the level of regional competition rather than in rural communities. In this respect, the regional economic policies by the local governments are classified into two broad categories : supply-oriented and demand-oriented policy, which many policy makers easily follow its implementation. Each classified regional economic policy also consists of several sub-categories and has been associated with dynamic regional changes. Of course, differences among regions(urban and rural) can be expected to affect economic development strategies.

### 1. Supply oriented policy

There are three categories of supply-oriented policy measures used to promote local economic development responding from the local government officials are shown in Table 2. These three supply-oriented policies are tax reductions, loans/ financing and administrative-service improvement categories. The index number identifies their efforts to promote the regional economic development between two forms of local government by comparing the index. The index number in Table 2 having more than 1.00 indicates that all regions employ four sub-categories of policy tools within the supply- oriented policy sector; particularly a higher adoption in the field of tax matters including reductions dealing with property register taxes, local property taxes, property acquisition taxes and tax releases equally as a financial policy tools respectively.

This Table also reveals that city governments tend to positively have less need of or pressure to use a wide-range program to adopt as policy tools. However, less resourceful rural regions did not employ all regional economic policies particularly in the broad domain of property tax exemptions and local tax releases because of their local financial reduction. These local tax exemptions are not relatively minor compared to other policy tools. The central government prefers the local tax reduction policy as a financial tool. Local tax policies do not, however, work well in reducing production costs for local firms in designated areas. The efficiency of these policies may yield sufficient policy objectives compared to other policy options.

The category of loan/ financial policy shows also same propensity for local governments that the most popular policies are financial aids, followed by direct and indirect loan programs, fund-raising and bank interest release concessions for locally based firms to stimulate their economic activity. At the same time, the index numbers also indicate that most local governments prefer administrative policies that improve administration services, deregulate administrative permission, minimize paper work, reduced inspections, revitalize committees and provide technical guidance to local layers. The administrative service improvement policy requires no local finance so that every local government has recently this policy. However, these administrative policies did not

seriously root take specific programs for improving management practices and increasing profit. It will take time to make the policy actually viable in the field. The deregulation approach seeks to reduce the role of government in enhancing the autonomy of the private marketing.

There are no differences between urban and rural municipalities when it comes to employ supply-oriented regional economic policy tools. We can draw the conclusion that this arises because Korea has a relative shortage of local policy resources available and only short periods of local autonomy. Statistics show that only 50 percent of the local governments in Korea have sufficient local funding for maintenance expenditures procured by local financing. This explains that almost all the local governments have similar government funding available for implementation.

Policy Tools		Urban Gov.	Rural Gov.	
Tax reductions	Register Tax Exceptions.	1.11	1.09	1.10
	Local Property Tax Exemptions.	1.12	1.02	1.07
	Property Aquisition Tax Exceptions.	1.08	0.99	1.00
	Tax Releases	0.93	0.78	0.84
Financing	Financial Aid	1.12	1.18	1.20
	Indirect Loans	1.15	1.01	1.08
	Direct Loans	1.11	0.95	1.03
	Fund-raising	0.98	0.78	0.87
	Interest Release	0.83	0.68	0.75
Administration	Adm. Service Improvement	1.11	1.09	1.10
	Deregulate of Permission	1.02	1.11	1.06
	Minimizing Paper Work	1.05	1.05	1.05
	Reduce Inspections	0.97	0.90	0.93
	Revitalizing Committees	0.95	0.89	0.91
	Technical Guidance	1.02	0.78	0.89

< Table 2 > Supply Oriented Policy Tool Index

$$F=14.53 > F_{14,2} = 6.51$$

The local governments of Korea have implemented most of their regional economic policies by a matching grant system with the exception of small/ local projects. This means that the local governments due to the lack of local project funds are placed in a passive position when dealing their own regional development policy. At the same time, it can be interpreted that the local policy-makers understand how difficult it is to get funding from the central government and that implementation takes time. One way to solve this issue is to pre-allocate funds from the national tax to local projects.

## 2. Demand oriented policy

The demand-oriented policy for regional economic development generally requires more resources, effort and expertise. It is more difficult to implement than conventional supply-oriented policy. There are three broad categories of demand-oriented regional policies that are based on marketing, manpower supply and infrastructure. All regions generally adopt most policy tools with the exception of exploring overseas marketing, financial aid for

training and research which usually is the responsibility of the central government. There are several reasons to expect that urban/rural governments will adopt different policies regarding regional economic development. Rural officials are likely to be more active in promoting economic development, whereas the urban are more dependent upon service industry development due relatively to their main interest areas of transportation, housing and welfare programs, Urban governments have a higher index score in most policy domains than rural governments. This explains the tendency that city governments have relatively higher access to project funding in problematic areas.

Table 3 reveals the tendencies that most local governments have had a traditionally higher priority for investment in infrastructure and manpower programs for which they can get funding from the central government. However, relatively low priorities are the marketing programs which require more effort. The exceptions are advanced area visits, oversea marketing, training programs and research activities which may reflect the degree of improving their ability. This may be the result of traditional social norm in Korea. It is felt that government should not directly work with private firms but also that local government officials are not properly trained in relation to demand policy development and of insufficient local resources.

Policy Tools		Urban Gov.	Rural Gov.	Total
Marketing	Products Exhibition	1.16	1.08	1.12
	Exhibition of Local Firms	1.20	1.02	1.10
	Public Relations	1.06	0.89	0.97
	Visiting Advanced Regions	0.96	0.83	0.89
	Exploration of Overseas Markets	0.95	0.82	0.88
Manpower Supply	Job Employment Capacity	1.19	1.18	1.18
	Financial Aid for Training	1.19	1.00	1.09
	Retraining the Unemployed	1.11	1.06	1.08
	Opening Training Institutes	0.96	0.86	0.91
	Financial Aid for Company Training	0.66	0.62	0.64
Infrastructure Provisions	Transport Facility Improvement	1.36	1.26	1.31
	Provision for Living Infrastructure	1.23	1.06	1.14
	Transport System Improvement	1.15	0.96	1.05
	Environmental Protection	1.12	0.93	1.02
	Industrial Sites Provisions	1.03	0.85	0.93
	Energy and Water Provisions	0.96	0.91	0.93
	Improvement of Information System	0.85	0.82	0.83
	Research/ Information Provisions	0.83	0.62	0.72

< Table 3 > Demanded Oriented Policy Tool Index by Regions

$$F=12.74 > F_{17,2} = 6.11$$

It is an encouraging that local government leaders including major and top decision makers are increasingly interested in developing demand-oriented policy tools such as improvement of administrative services, deregulation of governmental hierarchies

and industrial site provision within the broad category of infrastructure development. At the same time, local government tends to be aware of the importance of public relations for local firms, local product exhibitions and publicity of local firm's activities to possible demanders as well as marketing policy strategies. Local leaders are also beginning to realize the importance of demand-oriented policy tools through improving their managerial skills. There is also a general proposition that relatively less-developed regions, rural areas, are under pressure to use a wide range of policy programs for promoting industrial and infrastructure development in order to show their administrative achievements before the next election. However, the densely populated regions, cities, are more involved in service industries and can afford exhibitions, cultural event programs and living infrastructure provisions because of their available disposal resources.

### 3. Policy Environments

Local economic development projects differ in their policy dimensions and reflect their own diversified socio-economic environments. Three environmental variables are examined with respect to regional economic development initiatives as shown in Table 4. It is an assumption that there is high relationship between policy environmental factors and policy tools. Three policy domains are classified into the categories of political, economic and socio-cultural environment for making regional economic development practically viable, which are important factors in decision-making process at the local level. As shown in Table 4, these three categories have its specific sub-policy measures including financing, tax reductions, man-power and marketing.

Table 4 also shows the relationship among broad policy categories and policy environments promoting regional economic growth. Generally speaking, the socio-cultural policy factor reveals a higher correlation with most categories with the exception of two environmental factors. Particularly, citizen participation and non-government organizations in the category of socio-economic factors shows a relatively high correlation with infrastructure, manpower, public service improvement, marketing and financial policy tools, respectively. This means that citizen participation representing local needs for those policies has recently begun to play an important role in regional policy formulation in Korea. Marketing and

Environment		Loa n	Tax except.	Man- power	Marketi ng	Service improvmt	Technical innovation	Infra- provision
Politics	Central	+	+	+	+		+	+
	Local	+	+	+	+	+	+	+
Econo- mic	Industrial Structure			+			+	

	Local Finance	++	+			+		
Socio-culture	Citizen Participation	+	++	++	+	++		+
	Firm Partn	++	+	++	++	+	+	++
	Government Participation	+		+	++	+		

< Table 4> Relationship Between Policy Environment and Policy Means

+: correlated ++: highly related

manpower programs are recently being developed by local governments. Since economic environmental factor require more local financing and expertise, policy experience variable shows a very low correlation with regional economic policy devices.

In summary, It is clear the evident that if local government dominantly plays a strong role in regional economic policy, their goals could easily be achieved in short term. The recent development of inducing citizen participation programs in relation to manpower supply, infrastructure and tax reduction is a desirable result of further demand-orient policy development. Economic policy can not achieve any goals without the private sector take part in its implementation. The degree of participation by business elites in promoting regional development may pave the way for success in all regions.

## •. Conclusions

Since the early 1970s, the Korean government has stressed the necessity of inducing spatially dispersed of population and economic activity. To achieve these policy objectives, regional economic policy measures has been employed mainly by the central government which has been heavily reliant on programs involved in construction of industrial sites, infrastructure and the regulation of metropolitan growth activities. Local governments, however, confine their policy activities due to a premature/ incomplete policy environment. There has been increased public awareness that regional economic policies should be designed to give local authorities the capacity to allocate resources in order to maximize their own local development, raising local organizational capacity and ensure a greater equality in the allocation of funding and priorities. There is wide agreement that social justice should be one of the highest goals in Korea.

This study attempts to find out the policy performance and patterns of regional economic policy and to respond to prevailing policy problems focusing efforts on regional economic development in Korea. The following findings are:

Firstly, it is a significant finding that most local governments in Korea tend to adopt supply-oriented policies than the demanded one because of limited local resources and inexperience in its policy formulation/ implementation. It is,



however, encouraging fact that local government leaders are increasingly aware of the importance of demand-oriented regional economic policy including enterprise development, technical assistance, venture capital programs, small business incubators, R&D, tax credits and science parks. This means that the entrepreneurial approach to economic development at the local level is being gradually imbedded after initiating local governance as a result of 1997 financial crisis in Korea.

Secondly, this study indicates the persistence of regional economic policy patterns. The more wealthy, urban and industrial regions are the most innovative in every policy domain promoting regional economic development; this can be interpreted the urban areas have higher access to financial/human resources along with urban government officials who have more experience.

Thirdly, there is a high correlation between policy environment factors and policy tools, particularly with the participation of private sector. The entrepreneurial approach to regional economic development is a crucial element in a firm's capability along with creation of the favorable business climate. Local governments with diverse regional economic policies tend to be associated with high government level and have more financial resources, expertise and a strong local leadership available to them. By contrast, the local governments with weaker regional economic programs are likely to be noted for poorer relationships with low level of policy environmental factor. Therefore, the central government needs to play a coordinated role of resource allocation for less favored regions in order to be diversify/ intensify regional economic development.

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#### ABSTRACT

This study aims at finding out the major policy tool changes in regional economic promotion by regions. The major findings are as follows;

First, most local governments in Korea tend to adopt supply-led policies than the demanded one because of limited local resources and inexperience in its policy formulation/ implementation. Local government leaders, however, are increasingly aware of the importance of demand-led regional economic policy. This means that the entrepreneurial approach to economic development at the local level is being gradually imbedded after initiating local governance as a result of 1997 financial crisis in Korea.

Second, the more wealthy, urban and industrial regions are the most innovative in every policy domain promoting regional economic development; this can be interpreted the urban areas have better access to financial/ human resources along with urban government officials having more experience in policy planning and implementation from their favorable resources.

Third, there is a high correlation between policy environment

factors and regional economic policy tools, particularly with the participation of private sector. The entrepreneurial approach to regional economic development is a crucial element in a firm's capability along with creation of the favorable business climate. Local governments with diverse regional economic policies tend to be associated with high government level and have more financial resources, expertise and a strong local leadership available to them. By contrast, the local governments with weaker regional economic programs are likely to be noted for poorer relationships with low level of policy environmental factor. Therefore, the central government needs to play a coordinated role of resource allocation for less favored regions in order to be diversify/ intensify regional economic development.