Chapter 1

Integration and Territorial Development in Latin America and the Caribbean

*Paolo Giordano, Francesco Lanzafame, and Jörg Meyer-Stamer**

Over the past decade, Latin America and the Caribbean (LAC) has witnessed increasingly intensive regional integration, paralleling the process of globalization (IDB 2003). As indicated by a growing body of literature on economic geography, trade liberalization and regional integration have a notable effect on spatial development, and a compelling case can be made for public policy in this area (Baldwin et al. 2003). Left to the markets, the result is usually polarized and asymmetric development. This is illustrated in the case of Mexico, where booming export-assembly plants along the northern border contrast sharply with stagnation in southern states. Likewise, in Mercosur, the perception of an uneven distribution of the gains from trade integration has prompted lively debate on how to deal with the effects of asymmetries of regional integration. However, regional integration can also offer opportunities for adopting productive development policies to improve competitiveness in an increasingly globalized economy.

Thus, treatment of asymmetries and disparities in the regional integration agreements in force in LAC is emerging as a priority. In the regionalism of the 1960s, such objectives played a prominent role, but the instruments to foster them were intrinsically contradictory and resulted in limited effectiveness. By contrast, the new agreements of the 1990s, which were more effective in promoting regional integration, neglected the asym-

* The authors acknowledge Robert Devlin and Eduardo Rojas for their comments and suggestions.

metry issue (Devlin and Giordano 2004). Today, there is a growing consensus that regional integration can offer an effective strategic platform for formulating national policies aimed at maximizing the participation of local actors in the global economy. The ingredients of such a strategy include expanded market access, clear and predictable trade rules, strong collective regional institutions, special and differentiated treatment for smaller economies, and well-funded financial programs for the transition to free trade (Giordano, Mesquita, and Quevedo 2004).

This chapter explores the connection between regional integration and territorial development. It aims at providing a conceptual framework appropriate to simultaneously assessing the key global and local ingredients of policy instruments that may be suitable to compensate asymmetric economic and social outcomes resulting from increasing exposure to globalization.

Regional Integration: A Framework for Contrasting Local Asymmetries

In this light, one of the most relevant policy questions is how does one link global governance (trade and integration policies) with national governance (territorial policy) to reduce asymmetries and promote an equitable socioeconomic insertion into globalization? Table 1–1 provides a simple analytical way of looking at this issue. Nowadays, most LAC countries can be described as regimes of increasing asymmetries (Type 1), characterized by lack of territorial policies at the national level and lack of compensatory mechanisms at the regional level.

The contributions to this volume consistently support the conclusion that the LAC region should move toward a regime of decreasing asymmetries (Type 4), characterized by the simultaneous implementation of consistent policies at the national and regional levels. Therefore, the question is not *whether* but *how* to achieve the transition. In particular, which policy sequencing is appropriate to ensure the shift from Type 1 to 4? Certain pioneering experiences in the region suggest that governments have moved on the national front, prompting the evolution from Type 1 to 3. The

Table 1–1. Linking Regional Integration and National Policies

National Policy	Regional Integration Policy	
	Increasing asymmetries: Free trade without compensation for disadvantaged regions	*Decreasing asymmetries: Free trade with compensation for disadvantaged regions*
Increasing asymmetries: Macroeconomic stabilization without regional/territorial policy	**Type 1** Washington Consensus	**Type 2** Early EU model (especially in highly centralized countries)
Decreasing asymmetries: Macroeconomic stabilization with explicit regional/ territorial policy	**Type 3** Certain LAC countries (e.g., Bolivia, Brazil, Chile, and Mexico)	**Type 4** Current EU model

Source: Authors' assessment.

missing piece is, therefore, the adoption of an ambitious strategy on the regional front. One can, therefore, muse about the ingredients of such a strategy by highlighting key issues for the governance of LAC regional integration.

Trade and regional integration have emerged as an increasingly important strategic objective for LAC. The demand to intensify the insertion into the global economy has often advanced faster than the institutional capacity to formulate effective strategies, trade policies, and institutions (Devlin and Vodusek 2004). Under these circumstances, it is not surprising that trade-related capacity-building has increasingly gained the attention of governments and donors alike. In order to link territorial development and regional integration, it is therefore crucial to include local actors in the delivery systems of trade-related capacity-building. Hence, it is important to include a local dimension in the needs assessment exercises conducted throughout the region and raise donor awareness of the challenges local communities face in the process of implementing increasingly complex, demanding trade agreements.

Regional collective institutions can play a key role in the consolidation of regional markets, where local economic actors can successfully implement the first steps of their internationalization processes. They may also function as institutional "anchors;" that is, they restrain national policies that create asymmetries (e.g., government subsidies for private business—a long-time, key instrument of territorial development policy—which resulted in wars between territorial units of a country and neighboring countries). Finally, as the European Union (EU) example illustrates, regional collective institutions can pursue top-down approaches to stimulate bottom-up initiatives, promote horizontal learning and exchange between regions, and effectively pool resources to ensure greater efficiency in the delivery of technical and financial assistance. LAC policymakers can learn much from examining this evolution, thereby abbreviating their own learning curves.

In this context, LAC's biggest challenge is how to devise effective and ambitious policy instruments to promote the adjustments required to minimize the social cost of the transition to free trade. Iglesias (2004) clearly identified the key issues:

- macroeconomic stability,
- sectoral adjustments,
- investments in infrastructure and human capital,
- poverty reduction and equity, and
- good governance.

Trade agreements will determine how local economies are coordinated with the world economy in the decades to come. However sound, well financed, and far reaching, policies aimed at facilitating the transition to free trade must be explicitly consistent with territorial development policies. Such a holistic approach, based on a strong connection between regional integration and territorial development, would help the LAC region move from Type 1 regime to Type 4.

To sum up, when creating regional integration schemes, it is useful for national policymakers to delegate powers to supranational bodies, which ultimately must be accountable to elected national governments. However, it is crucial to establish a clear mandate for these bodies to counteract the natural tendency of free markets to create spatially asymmetric development. Moreover, regional policies should be supplemented by consistent, well-funded national policies that ensure a socially equitable and territorially balanced transition to free trade.

Understanding the Problem

The Washington Consensus aimed at creating a level playing field by eliminating market distortions, which create an array of obstacles to national-level growth. Current regional-integration projects aim at removing obstacles to free trade at the regional, interregional, and hemispheric levels. This New Regionalism is part of a multi-polar trade strategy aimed at supporting comprehensive processes of national structural reforms (Devlin and Estevadeordal 2001). In sharp contrast with past goals, these new initiatives aim at promoting growth by creating regionally integrated markets that permit the promotion of efficiency gains through trade and foreign direct investment (FDI) (Devlin and Giordano 2004). They also foster geopolitical objectives among like-minded countries and, more importantly, generate demands for additional regional cooperation to more fully exploit the advantages of a regional market.

To what extent will this approach promote spatially balanced growth in LAC countries? Economic geography has shown that, under free-market conditions, economic development leads to spatially imbalanced growth (Arthur 1994; Fujita, Krugman, and Venables 1999). One can thus expect that national-level stabilization policies, decentralization processes, and regional integration will reinforce the current pattern of asymmetric growth within and among countries. Indeed, it is likely that regional integration has such an effect without accompanying development policies for disadvantaged locations.

Which options will balance this tendency? The traditional approach to regional policy—based on top-down policy, allocation of funds, and, in some cases, territorial privileges—has mostly failed (Hansen, Higgins, and Savoie 1990). It created market distortions that slowed growth and often led to massive misallocation of government funds, thus deepening the problems of public deficits. On the other hand, few regional policies are explicitly embedded in regional-integration cooperation schemes. The most notable case is that of the EU, although recent evaluations have questioned their efficiency (Sapir 2003).

The past decade has witnessed the emergence of a new pattern of territorially-based development policy, which, in LAC countries, like elsewhere in the world, emphasized endogenous potentials and bottom-up processes. As a result LED, cluster development, and similar approaches have mushroomed in many countries. Paradoxically, these issues did not play a prominent role in the regional-integration agendas of the 1990s, even though many new integration agreements stemmed from sectoral and bottom-up approaches adopted in the late 1980s. Indeed, little evidence indicates that bottom-up approaches to territorial development have had a major effect to date. To understand why, it is useful to examine several factors.

Policy framework

Is administrative decentralization giving sufficient incentives and latitude for policy formulation and implementation at the local level? Can local authorities raise their own taxes, and are the incentives development-oriented? Are any regional policy instruments suited to address the externalities that arise from the increasing interdependence of local economic and social systems with regional and global contexts? Or, at a minimum, are incentives sufficient to ensure that local and national policies are consistent with collective regional objectives?

Local authorities will pursue development efforts if they can expect a tangible benefit, such as employment creation, which usually creates legitimacy with the local electorate. Conversely, without local-level elections, local authorities will feel less pressure to act and will point to national governments to take responsibility for reducing unemployment. It is also possible to broaden the local tax base, but local taxes and more local business are needed to generate more local tax revenue.

Regional integration can play an important role in stabilizing the policy environment for national and local policies and signaling policy direction. In the old regionalism, contradictory policy signals may help to explain the region's failure to advance (Devlin and Giordano 2004). In the new regionalism, governments have been more successful in locking in reforms and consistent in signaling sound policymaking through regional commitments. A clear regional commitment to pursue territorial development policies may, therefore, help guarantee the sustainability of national and local policies.

Local governance

To what extent are local actors empowered to create solutions? Does the structure of policy and politics at the local level encourage problem-solving? That local communities can form a consensus, even if national politics tends to be riddled with strife and dominated by zero-sum games, is a romantic notion. In the real world, local communities are often just as divided as the society at large, and conflict over issues is even more likely to be mixed with personal and family conflicts and rivalries.

Indeed, the most effective way to condemn a local-development initiative to failure is to demand the formulation of a full consensus. Innovation and consensus are mutually exclusive. Innovation implies that only a few pioneers are prepared to accept the risks attached to it. Thus, one can either have an innovative territorial development initiative based on a limited alliance of particularly risk-friendly local actors or a consensus-based initiative shared by all relevant players.

Nevertheless, for collective action to have a sustained effect over time, the transparent involvement of State and non-State actors and well-functioning mechanisms of citizen representation and oversight are required for defining the policy priorities that define the framework of the insertion into globalization. Moreover, they are essential for holding elected subnational officials accountable and to ensure local-management transparency. Attainment of these governance objectives, which are essential conditions for democratic oversight, is a necessary condition for good fiscal management and accountability at the subnational level. Strengthening of the central functions related to setting performance standards, performing evaluations, and ensuring transparency of subnational government operations is also required to ensure good governance.

Outreach initiatives and an ordered dialogue that allows local actors to provide inputs into the formulation of trade and integration policies are key to promoting ownership and consistency of regional and territorial development policies. In the EU, for example, involvement of civil society in trade negotiations has proven to be an innovative feature of trade-related policymaking (Giordano 2002). Such initiatives probably responded to growing demonstrations of local groups, which increasingly organized events and actions related to globalization and trade integration. Participation in trade policymaking is only incipient in LAC, particularly at the local level. However, certain countries have witnessed a growing movement that will probably consolidate in the future (Ostry 2002). In any case, participation in an ordered, meaningful dialogue is often complex and involves technical issues. Thus, it presupposes the diffusion of sufficient trade-related capacity at the local level.

Local effects of globalization

To what extent is the local economy embedded in the global one? Is it connected to global corporate networks or value chains? What types of restrictions does this create for local policymaking? What is the specific policy space for local authorities? What should local policymaking's objectives and instruments be? Although globalization is pressuring localities to upgrade, it is by no means encouraging local initiatives. In the business sector, companies must develop a global perspective, which often erodes their local involvement. Moreover, the evolving global view of companies and the persistent local view of other organizations and politics create a mismatch, which makes public-private initiatives difficult.

Territorial economic policy aims to enhance local competitiveness and attract new investments of various sizes in order to exploit more fully locational comparative advantages and generate robust growth in local employment and income. Three basic factors must be considered:

- use of endogenous abilities and assets (e.g., local natural resources and productive and entrepreneurial skills),

- generation of external economies within the territory, and
- reduction of business-transaction costs.

The sources of public funding for LED must be consistent with sound fiscal discipline. In fact, local governments should support the growth of dynamic, competitive, and self-sustained enterprises that become tax contributors rather than consumers of fiscal resources.

Subnational governments play a key role in complementing national policies to create competitive conditions to promote LED. They can reduce regulatory barriers to private investment and create a favorable environment. They can improve the capacity of territories to compete with others for new direct investment through:

- providing good-quality local infrastructure,
- implementing policies and regulations that promote firm efficiency (ranging from labor training to natural-resource regulations, including the operation of real-estate markets),
- promoting functioning markets for business-development services in the local economy (e.g., accounting, maintenance, informatics, and advertisement), and
- promoting cooperation among enterprises to create economies of scale in providing certain goods and services.

If sufficiently connected with local subnational realities, regional integration can be a powerful policy tool. It can function as a dynamic catalytic interface that buffers local actors' exposure to global contexts. Competition with similar neighbors may be a useful training ground for preparing firms and institutions to face world-class competition. It can also provide a framework that helps to eliminate incentives for welfare-reducing fiscal wars among local districts that compete over foreign investment. As the EU case illustrates, development of trade and business contacts at the regional level may promote functional and institutional cooperation across a wide range of areas (Devlin and Estevadeordal 2004).

Box: Glocal Development: Opportunities and Challenges [1]

Recent years have witnessed much discussion about globalization; at the same time, localities have taken on an increasing relevance. The interrelationship between global flows and localities takes three forms: 1) exclusive predominance of global flows through localities, which frequently breaks down local structures, bending them to its interests and strategies; 2) defensive, self-centered localism—countries and regions that attempt to escape global flows by sealing themselves within their boundaries (they believed they could go it alone amid globalization's transformation of the entire planet); and 3) the glocal approach, whereby global and local actors meet, negotiate, and exchange ideas (dialogue also occurs between local actors, who aim to increase their combined negotiating strength).

The glocal approach is characterized by the convergence of local and global actors in areas of reciprocal advantage and common interest in an attempt to build common projects. Such a convergence is never natural—it is always sought and negotiated amid difficulties and tensions; however, two conditions make it possible:

1. The local fabric, represented and constructed by local actors, must be sufficiently dense and complex to express its arguments and negotiate its interests. National authorities, local communities, locally-based institutions, associations of firms and professionals, universities and research and educational institutions, public or private service agencies, and chambers of commerce—all must have the capacity and will to network and negotiate. Since the 1980s, locally-based glocal actors have begun to emerge throughout the world. This has occurred in the so-called region-states with only a few million inhabitants (Singapore, Ireland, Finland) and in regions, city-regions, and industrial districts whose economies have been particularly dynamic in introducing innovation to their production sectors and linking to the neuralgic points of world markets; cases include Bavaria and Hamburg (Germany), Scotland (Great Britain), industrial districts of Lombardy, northeast Italy, Bangalore (India), Trinidad and Tobago (Caribbean region), and Orlando and Las Vegas (United States). These local systems have shown great dynamism and flexibility in their capacity to create a network of horizontal links within and among local systems and vertical, glocal links connected to the global dimension.
2. Global actors must build a culture of complexity and a vision of their interests beyond the immediate situation. They must realize that the development and well-being of localities, in the medium and long term, are the conditions permitting their business development and profitability. In the aftermath of World War II, the United States realized this crucial lesson when it launched the Marshall Plan to reconstruct Europe.[2] Applied to the glocal approach, the Marshall Plan offers two important lessons: 1) the importance of the interdependence of well-being and development between continents and countries and 2) continental integration, both economic and political, as a driving force for development.

[1] This box draws on Bressi (2003)

[2] The Marshall Plan was an act of great political intelligence, which enjoyed extraordinary success, partly thanks to the start-up (through the Organization for Economic Cooperation, promoted by the U.S. government) of early forms of economic and political collaboration among European countries; these were the germ of the subsequent integration process that culminated in the European Union.

Seeking a Solution

Bottom-up processes in countries affected by liberalized trade cannot be relied on to cope with the potentially negative outcomes of this process. At the same time, in LAC countries, active participation in international trade flows requires accelerating innovation, including technology transfer and development of new production sectors and learning processes. To this end, strategies must be devised to promote new firms and activities, restructure uncompetitive sectors, and support small- and medium-sized enterprises (SMEs) to strengthen ties between exports and productive sectors and thus participate competitively in new trade flows.

Notably, nowadays most analysts avoid such labels as "industrial policy." In fact, the 1990s witnessed the ending of industrial policy as defined over the previous three decades (i.e., a central government activity that aims to create entirely new industrial sectors). Dominance of the Washington Consensus was not the sole factor that led to the demise of industrial policy. Too many industrial policy initiatives simply failed; they often created serious problems, such as the financial drain frequently observed in State enterprises created with industrial policy instruments. The general consensus is that central governments are no longer positioned to plan multifaceted industrialization processes since the economy has become too complex and continues to change at a rate that far exceeds the planning capacities of government bodies.

The demise of industrial policy is one reason why LED; cluster initiatives; and other decentralized, territory-based development approaches became popular in the 1990s. The question is whether these approaches can fill the void created by the disappearance of the "development State" of earlier decades. Despite some policymakers' positive opinion, concern over this issue is growing in LAC. For example, competition with China—where public policies have played a critical role in promoting industrialization—is prompting a promising new debate that is rethinking the role of the State and competitiveness policies (IDB 2004).

Today's overriding issue, however, is not whether to conduct territorial development policies, but how to conduct them effectively and efficiently. From an operational standpoint, a well-designed structure of intergovernmental relationships should provide subnational governments incentives for allocating resources efficiently to most socially profitable uses. Subnational governments must 1) assume clearly defined responsibilities; 2) have sufficient resources with which to discharge their assigned functions; and 3) face budget constraints and take full responsibility for the trade-offs involved in collecting, allocating, and managing a limited resource pool.

Examples from international experience

Taken alone, bottom-up approaches to territorial development are unlikely to compensate for the centripetal effects that free trade has on spatial development. Experiences from other countries and regions demonstrate that bottom-up approaches must be complemented by top-down approaches and that local approaches must be explicitly linked to regional initiatives.

United Kingdom. Traditionally a centralized country—the centralization process was reinforced in the Thatcher era of the 1980s—the United Kingdom has started to encourage decentralized approaches in development policy. National authorities in Scotland and Wales are investigating options, and England's Labor government has created nine Regional Development Agencies (RDAs), designed as part of a larger regionalization push (including the creation of regional assemblies). This effort, however, has not made the life of RDAs easier; local authorities tend to perceive them as intruders and competitors, and they tend to become entangled in party politics (Thanki 1999; Fuller, Bennett, and Ramsden 2002).

Germany. Since creation of the Federal Republic in 1949, Germany has evolved its views on territorial development policy, involving a dynamic interplay of bottom-up and top-down approaches. The bottom-up approach rests on the autonomy of local municipalities, many of which have had LED units for decades. Their traditional task was to develop real estate. Since the 1980s, their profile has widened to include such approaches as technology incubators. The 1990s witnessed a further broadening of the scope of activities, often based on the creation of independent LED Agencies, which, in certain cases, became strategic development players, especially in declining regions that had to build a new economic base (Hollbach-Grömig 1996). Since the 1970s, the top-down approach to territorial development has been based on the Joint Task Promotion of Regional Economic Structure, known as the GA (*Gemeinschaftsaufgabe*), which the federal government funds and state governments implement. The GA's effectiveness has been questioned for some time, particularly after re-unification. In certain states, the 1980s and 1990s saw a shift from top-down to combined approaches. For example, in 1989, North Rhine-Westphalia, the largest state government, encouraged the creation of Regional Conferences, whereby local players from neighboring municipalities and counties were to formulate a consensus view on development options and prioritize practical activities (Meyer-Stamer and Maggi 2004).

This activity coincided with a paradigm change in the conceptual discussion on regional policy, which now emphasized endogenous potential. In the mid-1990s, the national government, through the Federal Innovation Ministry, further developed this approach by launching contests to encourage innovative, bottom-up approaches to territorial development. Examples included the BioRegio Initiative to promote high-performance biotechnology clusters and the InnoRegio Initiative (which exclusively addressed the new eastern states) to promote innovative clusters in East Germany. The Federal Ministry for Urban Development pursued a similar approach with its Future Regions initiative. Certain states pursued similar performance-based approaches, which represented a new approach to regional policy that created more balanced incentives. As a result, the perverse incentives of traditional regional policy (e.g., rewarding backward regions' lack of performance), were eliminated, and innovation and bottom-up approaches were encouraged. The rationale was that, in a highly differentiated post-industrial economy, the central government was no longer positioned to coordinate local activities in a centralized, hierarchical way, but had to rely on the effectiveness and creativity of local-actor networks.

South Africa. One of the few countries where local governments have a legal mandate to pursue economic development activities is South Africa. The country's central and provincial governments play a guiding role in developing LED policies and identifying sound practices, while district and local municipalities execute LED interventions. The disappointing outcome of this approach to date involves conceptual and organizational problems (Tomlinson 2003).[3]

Until late 2003, central-government ministries were unable to agree on LED objectives. The Department of Provincial and Local Government, which has coordinated the decentralization effort for several years, tends to define LED as a means of poverty alleviation, looking specifically at population groups with multiple disadvantages (e.g., poor, unskilled, residents in remote areas, women and youth, or persons infected with HIV/AIDS). The Department of Trade and Industry promotes a LED approach that addresses business upgrading and growth, as well as investment promotion. These conflicting policy objectives led to confusion on the ground.

Division between district- and local-level organizational functions is unclear in South Africa. In 2001, territorial reform created relatively large local municipalities, which often united several towns. Typically, four-to-six local municipalities formed one district municipality. The evidence to date indicates that local and district municipalities compete rather than cooperate, even though both are usually in the hands of the African National Congress (ANC), the dominant party. In cases where a different party governs one of the levels, any type of cooperation is more difficult.

European Union. On the regional front, the European Union (EU) has had a long-standing concern with the spatial polarization effects resulting from trade liberalization and regional integration. Therefore, collective policies directed toward disadvantaged localities have been the cornerstone of the regional-integration policy mix, although operational instruments have

[3] Information based on Jörg Meyer-Stamer's extensive interviews and interaction with national, provincial, and local LED players in South Africa.

changed over time. Nowadays, the cohesion policy comprises 35 percent of total expenditure and is translated into financial disbursements via two main instruments: 1) Structural Fund and 2) Cohesion Fund. The conspicuous financial support of the EU, which in poorer recipient countries can represent up to 4 percent of GDP, has played a key role in financing national projects at the local level and promoting convergence across European regions (Griffith Jones 2003).

However, a recent authoritative evaluation of this regional approach to LED suggests that the cohesion policy should focus on two main areas: 1) implementation with few instruments and 2) financing on a national, rather than local, basis. According to Sapir (2003), on the one hand, a convergence policy should focus on investing in institution-building and human and physical capital, rather than traditional regional-development projects; moreover, national instruments should complement regional projects to foster political acceptability, long-term planning, and avoidance of crowding out national instruments. On the other hand, a restructuring policy that targets displaced workers should be set at the regional level to complement national policies. Such a policy should focus primarily on retraining and relocating the labor force or incentives to set up businesses.

From development fads to balanced territorial-development processes

The international experiences outlined above show that policy networks have emerged as the most adequate response to fragmented governance structures (Messner and Meyer-Stamer 2000). Initially, they were a spontaneous response to the erosion of traditional hierarchical and government-driven governance. Nowadays, higher levels of government intentionally set the stage for the emergence of local and transnational policy networks.

Thus, if local actors can control their tendency to stir up political conflict, what exactly should they do? In this respect, policy guidelines are inconsistent. Currently, cluster development is fashionable. Other specialists would strongly recommend strategic planning. Still others would point at the crucial importance of creating LED agencies.

Some currently fashionable approaches to territorial development appear like a downsized version of traditional industrial policy with an enlightened, brilliantly informed, and strategically capable local government orchestrating the efforts of various players, pulling them out of their short-sightedness and narrow thinking. However, it is well recognized that government failures may induce even more distortions than market failures. Government intervention should therefore be limited to correcting market failures, which impede private actors from taking full advantage of business integration. They should provide national and regional public goods and leave market decisions to private actors.

Other approaches are borrowed from related fields, together with professionals who suddenly find themselves in charge of territorial development. For example, the strategic planning approach originated in urban planning; however, factors relevant to planning roads and buildings may not be applicable to planning a business.

Territorial development approaches must look beyond the current fads. LED is fundamentally a change, risk, asset, and relationship-management activity implemented within a territorial framework. In other words, territorial development is basically about connecting people, not determining exactly what and when they do something. Moreover, one of local government's main tasks is to reduce the administrative burden it places on business and to make the services it provides more efficient.

Synthesizing, it is possible to argue that territorial development takes one of three forms: generic, reflexive, or strategic. Generic territorial development focuses on reducing government-created obstacles for companies, a measure that businesses usually appreciate and that can have a stronger growth effect than other pro-active measures. Reflexive territorial development adds analytical activities to better understand the competitive environment of businesses so they can make better-informed decisions. The EU's current effort to promote regional-foresight exercises is an example. Finally, strategic territorial development engages a variety of partners to agree on a shared vision and distribute responsibility for implementation.

In summary, territorial development must not be primarily about local government grappling with activities that are supposed to "help" business. Successful territorial government involves a partnership between government, private sector, and other players. It involves information-sharing so that businesses know what the government is planning, and vice versa. It may involve joint activities to upgrade locational quality. It may even involve cluster initiatives, but only as the outcome of trust-building between the public and private sectors and not as a starting point. In any event, territorial development should look beyond the local reality and facilitate local actors' connection with international contexts.

Local development and social cohesion

Public policies aimed at stimulating emergence of a vibrant local economy should also be complemented by actions that favor social cohesion (Bouillon, Buvinic, and Jarque 2004; IDB 2004). One key responsibility of local governments is, therefore, the provision of social services, particularly in this new phase of globalization. In fact, increased external competition exposes local communities to structural change, which, in the absence of adequate safety nets, may result in job losses and social exclusion. Local governments should certainly promote economic development to stimulate the creation of new opportunities; however, it is also important to develop viable, efficient, and equitable initiatives to support those who, in the short or medium term, will not benefit from new economic opportunities during the transition to freer trade.

Specific actions for the poorest populations, excluded groups, and low-income geographic areas would promote social cohesion and help assuage resistance to globalization. They would allow for the mutual reinforcement of social and economic policies and would strengthen growth benefits for the poorest populations. In addition, more integrated efforts are needed in poor and excluded territories. Frequently, poverty is concentrated in spatially segregated territorial areas. A spatial focus facilitates diagnosing specific community needs, tailoring services, executing actions, and assessing impacts. Subnational governments can better deliver integrated services with a territorial focus, providing effective responses to the multiple disadvantages of the poor and marginalized.

Social progress depends on the institutional capacity of government and the performance of nongovernmental actors in the social sector. Local governments are the most appropriate entities for providing public services with localized benefits. They can potentially respond better to community preferences and needs, especially people-oriented social services that require good targeting. At the same time, it is important to link economic politics with cultural and social politics (Lanzafame 1996).

A local approach to social development makes early and coordinated interventions easier. Social policies and programs have focused insufficiently on preventing social ills and key transitions in the life cycle of individuals and families. Strategies capitalizing on powerful synergies that can be tapped by cross-sectoral interventions remain the exception, and programs fall short in combating exclusion. Yet, successes have been documented in all these areas, providing firm grounding for subnational-government actions.

Effective reforms require effective, adaptive, and strategic management—features that have been largely lacking in social-sector organizations. In fact, much can be gained from separating and then re-connecting economic and social development policies.

Past economic and social development approaches were often mixed and confused. Typical examples were support measures for microenterprises that followed social-assistance, rather than competitive, logic. Local governments must pursue LED as a business using a competition-oriented approach, while social development should stimulate the self-help potential of marginalized groups rather than create welfare dependency.

Re-connecting economic and social development policy involves such features as better management of social interventions and projects, clear focus at efficiency and sustainability, and a targeted approach to establish marginalized parts of the population as market suppliers of labor and goods. It is important to invest in promoting human capital accumulation in poor territories and communities, and even more important to align this investment with clearly identified needs and market niches.

Moreover, as previous work with indigenous people demonstrates, projects fail when they do not recognize the cultural characteristics and values of excluded groups. Inclusion must respect diversity and build on cultural identity. Diversity is an asset that enriches the social fabric, and, if properly managed, project outcomes. Health, education, and housing-reform objectives, as well as services provision, must be tailored to incorporate the cultural richness of diverse ethnic and racial communities with a view to increasing these communities' access to and use of quality services.

At the global level, globalization and regional integration require a new set of policies to ensure the promotion of social cohesion. At the local level, cities must rapidly create new tools, implement new policies, and invent mechanisms of social inclusion. Urban rehabilitation, neighborhood upgrading, and integrated urban and rural community development projects take advantage of the synergies of combined interventions, amplifying their effect and reducing the fragmentation and duplication of policies common to many social-assistance programs. International experience (e.g., European Social Fund) demonstrates the benefits of linking social-development goals with a clear business orientation in practical interventions.

Top-down and Bottom-up Approaches: What Are the Lessons?

Six major lessons can be extracted from the conceptual framework and the international experiences outlined above:

- Irrespective of the level of development, central governments should delegate the implementation of certain aspects of the development policy mix to lower levels. They should also ensure the coherence of national strategies with subnational and supranational regional objectives and create policy instruments that are coordinated, effective, and well-financed.
- When discussing intergovernmental relationships among various government tiers, it is necessary to clearly define the aspects related to: 1) expenditure assignment (who does what), 2) revenue assignment (who levies which taxes), 3) vertical imbalance (how is the resulting imbalance between revenue and expenditure of subnational governments to

be resolved), and 4) horizontal imbalance (to what extent should central fiscal institutions attempt to adjust for the differences in needs and capacities between local administrations) (IDB 2004).

- Top-down support for territorial development initiatives should not only address lagging regions but also accelerate good performers' growth by promoting institutional and infrastructure investments that allow all localities to link up in external regional and global contexts.
- Decentralization of territorial development policy easily clashes with administrative structures and political conflict lines. On the one hand, taking responsibility for territorial development can strain the resources and capacities of already overburdened local governments. On the other hand, successful territorial development buys political clout, which politicians are eager to exploit; however, this often impedes the sharing of responsibility with nongovernmental actors.
- A thorough regional integration scheme, characterized by a sufficient level of trade intensity and strong collective institutions, may play a crucial role for the sustainability of territorial-development policies. Trade is a powerful anchor for a broad range of cooperation initiatives, including those at the local level. When regional collective bodies have adequate technical capacity, sufficient institutional independence, and relevant financial power, they can strengthen coherent policy frameworks for territorial initiatives.
- National politicians may find handing over responsibility to regional institutions attractive since it relieves them of having to make unpopular decisions. This delegation of power, in turn, can significantly reduce special interest groups' capture of local politics and foster rational policies directed at long-term development goals.

Based on these lessons, it is questionable whether the most organized approach—clearly defining responsibilities of local government bodies for territorial development—is in reality the most promising one. The international experiences tell a different story: They accept that political conflict and fragmentation exist at the local level, and offer an incentive that may or may not persuade local actors to forget animosities; the objective is to create local and regional policy networks that involve governmental and nongovernmental (including business) actors.

However before attempting to apply such international success stories to the LAC region, one must consider the great structural differences between LAC and other regions, particularly Europe. For example, it is crucial to consider differences in patterns of asymmetries among and within countries; civic culture; level and roots of political conflict; overall governance structure; level of regional interdependence; and, most importantly, availability of funds to finance public policies.

References

Arthur, W. B. 1994. *Increasing Returns and Path Dependence in the Economy*. Ann Arbor: University of Michigan Press.

Baldwin, R. R. Forslid, P. Martin, G. Ottaviano, and F. Robert-Nicoud. 2003. *Economic Geography for Public Policy*. Princeton, NJ: Princeton University Press.

Bouillon, C., M. Buvinic, and C. Jarque. 2004. "Building Social Cohesion in Latin America and the Caribbean." Inter-American Development Bank, Washington, D.C.

Bressi, G. 2003. *The Impact of Globalization: Opportunities and Challenges for Glocal Development in Europe, in Latin America and the Caribbean*. University of Turin, Italy.

Devlin R., and A. Estevadeordal. 2001. *What's New in the New Regionalism in the Americas*. INTAL-ITD Working Paper No. 6. Buenos Aires: IDB-INTAL.

______. 2004. "Trade and Cooperation: A Regional Public Goods Approach." In *Regional Public Goods: From Theory to Practice*, eds. A. Estevadeordal, B. Frantz, and T. R. Nguyen. Washington, D.C.: Inter-American Development Bank and Asian Development Bank.

Devlin R., and P. Giordano. 2004. "The Old and New Regionalism: Benefits, Costs and Implications for the Free Trade Area of the Americas." In *Integrating the Americas: FTAA and Beyond*, eds. A. Estevadeordal, D. Rodrik, A. Taylor, and A. Velasco. Boston: Harvard University Press.

Devlin R., and Z. Vodusek. 2004. "Trade-related Capacity Building: An Overview in the Context of Latin American Trade Policy and the Mercosur-EU Association Agreement." Inter-American Development Bank, Washington, D.C.

Fujita, M. P. Krugman, and A. J. Venables. 1999. *The Spatial Economy: Cities, Regions, and International Trade*. Cambridge: The MIT Press.

Fuller, C., R. J. Bennett, and M. Ramsden. 2002. "The Economic Development Role of English RDAs: The Need for Greater Discretionary Power." *Regional Studies* 36(4): 421–28.

Giordano, P. ed. 2002. An Integrated Approach for the European Union—Mercosur Association. Paris: Chaire Mercosur de Sciences Po.

Giordano P., M. Mesquita, and F. Quevedo. 2004. *El tratamiento de las asimetrías en los acuerdos de integración regional*. INTAL-ITD Occasional Paper No. 26. Buenos Aires: IDB-INTAL.

Griffith Jones, S. 2003. "Financial Mechanism for Accession: The European Experience and Lessons for the WHFTA." Inter-American Development Bank, Washington D.C.

Hansen, N., B. Higgins, and D. Savoie. 1990. *Regional Policy in a Changing World*. New York: Plenum Press.

Hollbach-Grömig, B. 1996. *Kommunale Wirtschaftsförderung in den 90er Jahren: Ergebnisse einer Umfrage*. Berlin: Deutsches Institut für Urbanistik.

IDB. 2003. "IPES Beyond Borders: The New Regionalism in Latin America." Inter-American Development Bank, Washington, D.C.

______ . 2004. "The Emergence of China: Opportunities and Challenges for Latin America and the Caribbean." Inter-American Development Bank, Washington, D.C.

IDB. 2004. "Toward Sustainable and Equitable Development - Sector Strategies for Latin America and the Caribbean". Inter-American Development Bank, Washington, D.C.

Iglesias, E. 2004. Integración de las Américas y el desarrollo económico y social: más allá de los tratados de libre comercio. Paper presented at the conference The Future of the Americas, January, Monterrey, Mexico.

Lanzafame, F. 1996. *La descentralización territorial en América Latina*. ECLAC, LC/R.1681, Santiago de Chile.

Messner, D. and J. Meyer-Stamer. 2000. Governance and Networks: Tools To Study the Dynamics of Clusters and Global Value Chains. INEF, Duisburg. Mimeographed.

Meyer-Stamer, J. and C. Maggi. 2004. "Grundrisse der Mesopolitik in NRW." In *Die Strukturkrise der Strukturpolitik: Tendenzen der Mesopolitik in Nordrhein-Westfalen*, eds. Jörg Meyer-Stamer, Claudio Maggi, and Michael Giese, 16–44. Wiesbaden: VS-Verlag.

Ostry, S. ed. 2002. *Trade Policy-making Process: Level One of the Two Level Game*. INTAL-ITD-STA Occasional Paper No. 13. Buenos Aires: IDB-INTAL.

Sapir, A. 2003. *An Agenda for a Growing Europe: Making the EU Economics System Deliver*. Brussels: European Commission.

Thanki, R. 1999. "New Labour and the English Regional Development Agencies: Devolution as Evolution." *Regional Studies* 33(1): 73–89.

Tomlinson, R. 2003. "The Local Economic Development Mirage in South Africa." *Geoforum* 34: 113–22.