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Conference Paper

A comprehensive view of regional economic development in Finland

50th Congress of the European Regional Science Association: "Sustainable Regional Growth and Development in the Creative Knowledge Economy", 19-23 August 2010, Jönköping, Sweden

Provided in Cooperation with:

European Regional Science Association (ERSA)

Suggested Citation: Ahokas, Jussi (2010) : A comprehensive view of regional economic development in Finland, 50th Congress of the European Regional Science Association: "Sustainable Regional Growth and Development in the Creative Knowledge Economy", 19-23 August 2010, Jönköping, Sweden, European Regional Science Association (ERSA), Louvain-la-Neuve

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**50th Anniversary Congress of the European Regional Science Association
19th – 23rd August 2010
Jönköping, Sweden**

**Towards a comprehensive view of regional economic development
in Finland**

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Abstract

Regional economic development has become a widely popular research subject within economics and economic geography. The rise of the ‘new economic geography’ in economics and the recent development in economic geography with (among others) institutional, evolutionary and relational ‘turns’ have introduced a considerable number of new conceptual and theoretical instruments that can be utilised in the analysis of regional development.

The variety of different approaches has certainly produced many positive outcomes for the discipline and the picture of regional economic development has emerged. Yet, at the same time the field of regional economic development studies has become somewhat fragmented. While researchers are working with some special theoretical frameworks and while they are concentrating on some specific issues, the general view of the regional economic development remains fuzzy.

Therefore, the aim of this paper is to illustrate prospects for examining regional economic development in a broader scope. The theoretical basis for the study is derived from institutional economic geography and political economy. It is argued that regional economic development process should be understood as a multi-level dynamic spatial process where different institutional, economic and political development paths interconnect and interact. The enquiring of these paths and their underlying mechanisms in detail deepens and diversifies the understanding of regional economic development process.

The empirical part of the study concentrates on the processes around five key institutions and structures that have contributed to the regional development within the national borders of Finland. Although the research subject is a nation state, an open system approach is employed and relational aspects of regional economic development are recognised. By investigating the driving processes of regional development a comprehensive view of regional economic development in Finland is obtained and the table is set for further research.

KEYWORDS: regional economic development, ontology, institutions, research framework

1 Introduction

The research of regional economic development has advanced considerably during the last decades. The discussion on the discipline and its recent developments has been intense as different theoretical and thematic frameworks have been introduced within the field. For example, the institutional turn in social sciences¹ has contributed heavily to the regional economic development studies (Martin 2000). Also the recent development in the economic geography with relational (see Amin 1998, Boggs & Rantisi 2003) and evolutionary (see Boschma & Lambooy 1999, Boschma & Frenken 2006, Martin & Sunley 2007) turns has brought new insights to the field. In addition, during the last decades the theoretical interest in space has arisen among economists. With this development region has become a recognised research subject also in the mainstream economics which has had positive implications for the research of regional economic development (e.g. Krugman 1991, Fujita & Thiesse 2002). Interestingly, also the globalizing tendencies of the contemporary economic system have produced new perspectives for the research of regional economic development (Scott 1998, Storper 1997).

Without question, the recent development of the discipline and the introduction of novel thematic and theoretical perspectives has been an improvement. The research of regional development has made progress and a more comprehensive view of economic development in regional framework has evolved. However, the simultaneous inputs from various different theoretical approaches have made the field of regional economic development studies more or less fragmented. Although many common interests is to be found from different research frameworks of regional economic development there are also a number of colliding views and commitments. Chief among these are the ontological commitments of different frameworks. Because the ontological stance has a defining role in the research process these differences have led to varied theoretical and methodological choices.

Several propositions have been made over the last years regarding the construction of coherent and comprehensive research framework of regional economic development where recent thematic and theoretical perspectives could be combined in a consistent manner (Cumbers et al. 2003; MacKinnon et al. 2009). In addition, some authors have called for more accurate definitions for the concepts in use and more accurate description of the theoretical agenda of research (see Markusen 1999, Lagendijk 2003). Thus, researchers are pushing for more critical analysis of regional development by demanding thorough investigation on the scientific foundations of the discipline.

The current quest for critical analysis and accurate conceptualisation in regional development studies is a welcome phenomenon. Accordingly, the aim of this paper is to respond to recent calls by proposing a research framework of regional economic development. The validity of the framework is evaluated by applying it in an analysis of regional development in Finland. The main argument concerning the framework is that regional economic development must be understood as an ensemble of multi-level spatial and temporal processes that interconnect and interact with each other. Different economic, political and cultural processes as well as wider institutional processes must be analysed to provide a comprehensive understanding of regional economic development.

¹ In recent times institutional approaches have gained ground in economic sociology (Granowetter 1985) and economics (Hogdson 1998). For a comprehensive view of the institutional turn, see Nielsen (2007).

The basis of the research framework is derived from institutional and evolutionary economic geography but also perspectives of political economy and heterodox economics are utilised in order to constitute a sufficient theoretical foundation. The ontological commitments of the framework lead to an open system approach. The open system approach challenges the common understanding of the concept of region by connecting regional development with wider social processes at different spatial scales, or moreover, in the open space.

The remainder of the paper is organized as follows. In section 2 the research framework of regional economic development is presented with the ontological commitments and theoretical standpoints. In section 3 the research framework is applied in the evaluation of the regional economic development in Finland. Processes around five important institutions and structures behind regional economic development are analysed. The fourth section concludes with a summary of the main findings of this paper. Also issues related to the future research of regional economic development are discussed briefly.

2 The research framework of regional economic development

The call for a comprehensive research framework of regional economic development has arisen mainly in the sphere of institutional economic geography and political economy. Both of these approaches emphasise the importance of wider social processes behind regional economic development. Institutional economic geographers state that economic processes are always institutionally and socially situated. For example, cultural and political processes of society or region interrelate with economic processes and hence socio-political and cultural structures have to be included in the analysis of economic development (Martin 2000). From the political economy perspective the regional economic development cannot be understood without the concept of power. Thus, political struggles and development of regulatory mechanisms must be incorporated to the theoretical framework as research subjects (Cumbers et al. 2003). The common insight for the two approaches is that the research of regional economic development has to take into account also other processes than purely economic ones.

Therefore, by following the ideas of institutional economic geography and political economy many important perspectives on society will be included into the research framework of regional economic development. Although the research will still be concentrated on themes like regional economic growth, regional distribution of production, labour and capital, changes in the regional structure of production and technological basis, income, welfare and wealth disparities between regions and on development of regional markets the analysis will now take into consideration the multi-level processes of the social realm. Without this step the analysis of regional development would remain inadequate in explaining the complex interactions of society.

In the research framework proposed in this paper the society is understood as a dynamic and open system consisting of historical and evolutionary processes in space. However, these processes appear only at the actual and empirical levels of social realm. Following the critical realist thinking, the level of real and the mechanisms that produce the empirical and the actual are the principal objects of explanation. This is the main ontological commitment of the framework.

Regional development is seen as an ensemble of processes or development paths that dialectically interact with each other at different spatial scales at different points of time. Development paths and regional processes develop around institutions and other social structures. Institutions and social structures act as carriers of history making regional processes path-dependent (David 1995). However, the importance of history should not be overemphasised. In the society all processes are ultimately open, making it equally important to concentrate on path-creation and path-decay phases of the regional processes (Martin & Sunley 2006). Thus, the evolutionary dynamics of social realm should be attached to the analysis of regional development.

The other important ontological commitment behind the research framework concerns the relationship between individual action and social structures. The statement is that the economic, political and cultural processes are formed in the dialectical interaction of social agency and social structures. The roots of this view lie in the structuration theory of Anthony Giddens (1984). Authors of the critical realist school have constructed alternative theories of social structuration and at same time elaborated Giddens's ideas (e.g. Bhaskar 1979, Archer 1990). Some authors have also tried to combine structuration theory with spatial considerations that can be seen considerably valuable from the perspective on regional development studies (Jessop 2001). By perceiving the spatial dimensions of individual agency and its interactions with spatial institutions² the ontological basis of the regional development research framework strengthens. Thus, the multi-level regional processes build up on the individual agency and regional institutions. Spatially structured individual agency is constrained by the regional institutions that for their part are moulded by the human action.

If human action and institutions cannot be separated from space it becomes necessary to define the concept of space. The argument is that the research framework of regional development should be grounded on the relational understanding of space. That is, space is seen as contained in individuals and institutions and cannot be explained without understanding relationships between them (Harvey 2006). In other words, space is an entity of different social objects reshaping each other in the constant relational interaction. As can be seen, the concept of relational space is consistent with the two ontological commitments presented above.

The relational understanding of space expands perspectives on regional development. Furthermore, with relational understanding of space also redefinition of the concept of region is required. Region can no longer be understood as a closed system and restricted area but as an open system with unlimited interconnections with other regions and spatial scales. Hence, regional processes unite with wider social processes and it is even possible to ask if it is reasonable to talk about regional development in the first place (Massey 1979). In the recent discussions of spatial scale in human geography some interesting ideas concerning the open system approach have been introduced³. For example, Marston et al. (2005) have emphasised a flat spatial ontology that is liberated from hierarchical concepts of scale and other static conceptual categories. Again, the whole concept of region becomes challenged.

² Institution can be understood as a sub-category of social structure. According to Hodgson (2006) 'social structures include all sets of social relations, including the episodic and those without rules, as well as social institutions'. Institutions, on the other hand, are 'systems of established and embedded social rules that structure social interactions'.

³ For more on the scale discussion see Marston (2000) and Brenner (2001).

By committing to the open system ontology a number of entry points that would have been lost with narrower ontological perspective are opened for the research (Marston et al. 2005, p. 427). This is, of course, a positive outcome. However, at the same time, the open system approach of regional development provides a substantial challenge for the research. If the context of research – that is the region – is open-ended and not strictly specified what possibilities does a researcher have to grasp it? For the purpose of research some kinds of boundaries have to be implemented despite the ontological stance. However, the closure of region can never be inclusive and researcher has to understand the relativity and permeability of the assembled boundaries (Mearman 2002, 2006). Accordingly, the conceptualised region is a dynamic and continuously changing spatial entity where different social processes interact.

Cumbers et al. (2003, p. 335) have proposed that ‘research [of regional development] should explore how social relations, operating across different geographical scales, interact in the reproduction of the political and economic landscape through time’. The proposition is valuable and should be championed. Yet, by following the definitions and conceptualisations of space, scale and region presented above the concept of ‘different geographical scales’ is possible to be replaced with the concept ‘open space’. Hence, spatial scales are seen as conceptualisations whose feasibility should be evaluated separately in every occasion and in every study.

If it is possible to distinguish regional processes, sub-processes of wider social processes, the next step for the research is to shed light on the underlying mechanisms of those particular processes. As noted above these real causal mechanisms are the ultimate objects of the social research. Following Lawson (1997) and his critical realist approach in economics this step is conducted identifying demi-regularities, that is, partial event regularities dominating restricted regions of time-space. Thus, demi-regularities indicate the occasional, but less than universal actualizations of mechanisms. The identification of demi-regularities can be facilitated through comparative and counterfactual analysis (Jessop 2005). The critical realist perspective provides interesting methodological and epistemological tools for the research of regional development in open systems that can be utilised in the actual research work.

A comprehensive understanding of regional economic development requires analysis and examination of numerous different processes. Like regional development the research of regional development is a dynamic and dialectical process that will never be completed. Hence, the aim of the research is to produce continuously novel explanations by redefining and questioning previous outcomes and by introducing further dimensions of some previously defined phenomenon (Jessop 2005, p 44). Because the processes behind regional development are changing and different properties of the real are actualised at different points of time new research subjects emerge and earlier results and conclusions of the research will be seen in the new light.

During the last two or three decades the sphere of regional development studies has expanded as many novel (or recovered) themes and perspectives on regional development have gained ground. Lately, explanations of regional economic development have been constructed increasingly around the concepts underlining the special characteristics of regions. Concepts like agglomeration, regional innovation systems and learning regions have become very popular (e.g. Fujita & Thiess 2002, Cooke 1992, Maskell et al. 1998). Hence, the research has explained regional economic development through endogenous regional

development paths. For example, development of production structure, technological change and the evolution of knowledge networks among other things have been under thorough investigation in recent years. Obviously, researches of regional development have experienced the region-based approach very powerful which have made it a dominant paradigm with regional development studies (Lovering 1999).

Without denying the many virtues of these approaches some major shortcomings arise, in particular, if the ontological stance presented above is accepted as a basis of the research of regional development. Firstly, region-based approaches of regional development have very often adopted a rather strict version of path dependence which distinguishes them from the evolutionary and open system approaches (Martin & Sunley 2006). For this reason region-based approaches understand regional institutions and social structures as unchangeable entities and constrains of the human action (North 1990). Thus, the dialectical interaction between institutions and individuals is curtailed to some kind of institutional rule setting.

Secondly, region-based approaches have frequently specified firm or even region as an essential actor of regional development. This kind of conceptualisation does not correspond to the view of social realm postulated in this article. Accordingly, a firm is just one possible institutional framework of the human action. Moreover, if region is understood as an independent economic actor many social processes will be concealed in the concept without proper investigation (Martin & Sunley 2006, p. 411-413). Hence, it is necessary to pay attention to other fields of social activity and other institutions that contribute to the processes of regional economic development. Besides firms institutions like nation states, political parties, trade unions and other class and cultural movements are fundamental in explaining the processes of regional economic development.

Thirdly, the dominant approaches have strongly emphasised the endogenous character of regional development. This kind of view is in deep contradiction with the relational understanding of space and open system approach of regional development. Although many regional processes can be handled in research as partial closures and although these processes could appear empirically strongly independent they always are interconnected with wider social processes in the different geographical scales, that is, in the open space.

Despite these contradictions the region-based approaches have provided interesting and important thematic perspectives on regional development. Especially, the regional processes around firm and production have been investigated with rigour within the paradigm. Hence, these thematic perspectives should be integrated with the research framework presented in this article. Although the ontological commitments of different approaches differ considerably the thematic perspectives on regional development can be some what similar. Thus, the literature of regional development studies provides various interesting entry points for the research to be conducted in the presented framework.

Important perspectives on regional economic development can be found also from the theories of uneven regional development (e.g. Massey 1984, Smith 1991) and from the theories of cumulative causation (e.g. Myrdal 1957, Kaldor 1970). These theories are built up on a comprehensive analysis of capitalist economic system and society. The Marxist approach of uneven regional development that became popular among economic geographers during the late 1970s and early 1980s emphasised the political aspects of regional economic development. Especially, the class conflict and the spatial perspectives of capitalist

accumulation process were at the core of the analysis. Theorists of uneven regional development have proclaimed that the research of regional economic development cannot be carried through without paying attention to power relations of capitalist system and the relationship between capital and labour.

The theories of cumulative causation begin with the analysis of capitalist economic system concentrating on the economic factors that lie behind the uneven regional development. By accepting the possibility of disequilibrium and cumulative development paths these economic theories move away from mainstream economics (Kaldor 1972). Historical and evolutionary development paths as well as institutions are important conceptual tools for the theories of cumulative causation⁴.

Regional economic development, power and institutions have been objects of research also with the regulation school of political economy. The recent spatial accounts of the regulation school have investigated regional institutions as executors and intermediates of different modes of regulation (e.g. Jones 1997, Peck & Tickell 2002). The main interest has been in the capitalist accumulation process which has also covered major part of the regulationist research of regional economic development. Thus, the research has tried to shed light on the relationship between wider regulation systems and regional institutions.

Accordingly, approaches of political economy bring broader view of social action and institutions to the research of regional development. The view that economic development is purely economic and that a firm is the ultimate institution or actor of regional development becomes contested. Thus, institutions like nation state will be included to the analysis and at the same time the concept of region will be deepened.

The policies put up by the state affect regional economic development multiple ways. For example, economic policies, regional policies and social policies have considerable effects on the processes of regional development. Hence, the investigation of the changes in the state institution - and hence in the policies - constitutes the core of regional development studies derived from political economy. In addition, also changes in wider social power relations are important from the perspective of regional economic development. The examination of the struggles between different economic and social classes as well as examination of other social antagonisms related for example to race, gender or sexuality will broaden considerably the perspective of regional economic development and they should be included to the research framework of as research subjects and explanatory factors.

So far, most of the presented processes of regional development have been material but also ideological processes matter. Transformation of the ideological structure has many implications on the regional development as it operates through discourses, attitudes and modes of thought. Consequently, ideological processes affect to the individual action and thus shape up the material processes, social structures and institutions. For example, mainstream theories of regional economic development can be understood as ideologies that have effect on human action and through human action further on regional institutions.

⁴ There are many theoretical and thematic similarities with the theories of cumulative causation and region-based approaches although the ontological and methodological commitments differ considerably. For example, the 'new economic geography' owes much to the work of Nicholas Kaldor in 1960s and 1970s (Krugman 1991).

Sometimes mainstream modes of thought and hegemonic ideologies became challenged by alternative ideas and schemes of thought. This kind of situation can be interpreted as ideological struggle following the Gramscian approach of political economy. Particularly, if the existing ideological structure is wittingly put under pressure by some class pursuing for change in material processes the ideological struggle unites with material struggles. However, often individuals are affected unconsciously by the ideological structure and social action is transformed which has significant implications on the social processes. Therefore, all types of ideological processes have to be taken into consideration in the research of regional economic development.

3 Processes around the key institutions of regional economic development in Finland

The presented research framework of regional economic development illustrates well the breadth and multidimensionality of the field. These elements make the empirical research of regional development very challenging as already the description of different processes and interactions between them requires tremendous effort. This is however just a start as the final aim of the research is to shed light on the real causal mechanisms behind the actual and empirical processes. Thus, the accurate framing of the research theme and theoretical and methodological choices are to be done after the descriptive phase of the research process.

Nonetheless, the next part of this article adheres to the descriptive operation and the actual analysis of the real is left to the forthcoming work. The purpose of the following endeavour is to bring forth some important processes around the prominent institutions and structures behind the regional economic development in Finland⁵. By analysing these processes research field of regional economic development becomes concrete and essential research themes for the future work become visible. The time period for the analysis is the last sixty five years, that is, the time after the Second World War. The length of the time span and the complexity of the regional economic development guarantee that the following query will be incomplete in many ways. Nevertheless, the investigation tries to describe processes and their interactions around five pivotal institutions and structures that contribute to the regional economic development. These institutions and structures – structure of production, economic regime, nation state, firm and ideological structure – are derived from the theories presented in the previous chapter.

Structure of production

One of the central structures of regional economic development is the structure of production. The processes around this structure explain a substantial part of the regional economic development in Finland during the last decades. The structure of production illustrates relationships between different industries and sectors and portrays their economic importance in society.

The production structure of Finland is part and parcel of the western structure of production (Veblen 1923, p. 65). Consequently, the changes occurred in the production structure of Finland are not endogenous for the region restricted by the national borders. The foremost

⁵ National borders of Finland provide boundaries and the spatial closure for this research. However, boundaries are understood permeable and dynamic which makes it possible to explore wider social processes with the closure.

dynamics behind the development of the production structure are the dynamics of the western mode of production where the demand for ever growing profits merge with the productive opportunities arising from the technological progress and from the continuously expanding markets that can absorb the novel products (Kaldor 1957, Pasinetti 1993). However, the regional institutional framework and regional social and economic processes have generated various peculiar characteristics for the production structure of Finland.

The basic trend in western world has moved production away from primary production, mostly from agriculture, towards manufacturing and from manufacturing towards services. Structural changes have occurred different times at different areas. Thus, the historical development of production structure has been spatially uneven and regional processes have contributed to the development of the structure unequally. For example in Great Britain, the heartland of the industrial revolution, it was assumed already in the 1960s that the production structure had developed to the mature stage. To the stage where all the excess labour force from the agriculture was absorbed to the high productivity industrial sector (e.g. Kaldor 1966). At that time the integration of the Finnish country people with manufacturing and service sector was just in the very beginning.

The structural change of production has massive effects on the regional economic development. The location structure of primary production is decentralized as the resources of agriculture and forestry, that is farmland and forests, have distributed widely. Thus, the location structure of production tends to be more even in the regions where the share of primary production in the structure of production is substantial. In manufacturing industries the same amount of production is fabricated at much smaller geographical area. Also the production of service sector tends to be spatially more or less centralised as the adequate demand for the profitable service activity is impossible to achieve from sparsely populated areas.

The industrialisation process in Finland has been very slow compared with the other western countries. The share of manufacturing industries in the production structure measured with the nominal value added has never been over 35 per cent as in traditional industrial countries the share has been near 50 per cent (Hjerppe 1987). Moreover, before the Second World War the share of manufacturing industries was under 25 per cent of the total value added. Hence, it can be stated that Finland could not be called industrial country until after the war⁶.

The growth of manufacturing industries was rapid in the 1950s and 1960s. At the same time the share of primary production decreased with considerable pace. All of the released labour force did not move to the manufacturing sector because the growth of the service sector was also substantially fast. Thus, in Finland the movement of labour force from manufacturing to services was partially substituted with a movement from primary production directly to service sector that had started to grow rapidly in all industrial countries (Hjerppe 1987, p. 76).

The development of Finnish manufacturing and service sectors from the beginning of 1950s manifests the cohesion of the regional production structure with the higher level structure of

⁶ Despite the nascent growth of manufacturing industries the importance of the agriculture was understood crucial for the national economy still in 1940s. The evacuated Karelian people were resettled to the countryside and they were given a patch of land to be cultivated.

production. The celebrated catching up mechanism worked at the full force bringing the production structure of Finland closer to the western standards. In manufacturing industries the technological progress of the western production system was put to use with large scale productive investments. New investments combined with relatively low labour costs provided competitiveness for Finnish products also in the international markets. The access to the Soviet markets was an important advantage for Finnish manufacturing industries. Altogether, the structural change of production proceeded at a gallop affecting also to the regional economic development.

The spatial division of production started to change along side with the change of the production structure. As the role of primary production declined the migration from the rural areas accelerated. The decade from mid-1960s to mid-1970s became the decade of the 'Great migration' in Finland. The post-war generation had to search job opportunities from other sectors of production and found them from the urban areas and industrial districts both in Finland and Sweden. The centralising tendencies in the spatial division of production became obvious but also some decelerating processes were activated and actualised.

Although the industrialisation moved production away from rural areas the emerging industrial districts were many and they were located rather evenly around Finland. One reason for the decentralised location pattern was the resource dependence of the pivotal industries like forest, pulp and paper industries. For historical reasons the eastern Finland was filled with sawmills and paper plants and many industrial districts developed around these factories. Another consequential reason was the activity of state from 1950s on. The early regional policy conducted by the Finnish government was aimed at decentralizing the manufacturing industries and dispersing them to the areas where economic development was considered sluggish⁷. This first phase of regional policies took place in the 1950s and 1960s when big state-owned companies were established and production plants were located in disadvantaged regions (Tervo 2005).

These processes had explicit effects on the regional economic development which continued fairly harmonious in different parts of the country. For example, the research of Pekkala (1999) has shown that the regional disparities measured with per capita regional GDP diminished in 1960s and 1970s when in 1980s regional divergence occurred and in early 1990s differences in per capita regional GDP remained unchanged⁸. It can be stated that the convergence of the economic indicator in 1960s and 1970s was mainly due to evenly situated production but also due to the migration which contributed positively to the indicator at the net loss regions.

Pekkala and Kangasharju (2004) found out that the per capita GDP divergence occurred also during 1990-2000. The depression of Finnish economy in the beginning of 1990s hit extremely hard on the poorer regions that had already in the 1980s begun to suffer from the changing conditions for example in state policies. During the depression productive investments plunged and never recovered to the level prior to depression. The share of

⁷ The ideological background of the policy can be found in a famous pamphlet "Does our country have the patience to become prosperous?" published in 1952 and written by the prime minister and later long time president Urho Kekkonen. In the booklet Kekkonen advocated broad regional policies to foster the development of northern Finland.

⁸ The data consisted of NUTS3 regions. The problem concerning the economic scale arises as the movement of production and people from rural areas to urban areas within the region is not captured in the measurement.

manufacturing industries diminished in the structure of production which had major implications especially on the smaller and remote industrial districts. In 2000's the productive capacity of the manufacturing industry has continued to shrink as globally oriented firms for example in forest and electrical industries have invested more and more in the Asia and South America instead of Finland.

These circumstances have strengthened the role of service sector in the structure of production. Both private and public services have grown constantly over the last four decades. As stated above services are more strongly tied to the final demand than are primary production and manufacturing. Thus, especially private services tend to be established into the populated urban areas where the demand is adequate. Of course there are service sectors like tourism and telecommunications where the demand could be gathered from broader geographical areas. In any case, after the depression of early 1990s the private service sector seemed to become the most divergent sector in the Finnish economy boosting the regional differences of per capita GDP (Pekkala & Kangasharju 2004, p. 265).

Public services on the other hand are more evenly located because the universal welfare services are guaranteed to every individual regardless of the residence. In many peripheral areas public services and public sector have become very important also as employers. For example in one of the poorest regions – in Kainuu region – public sector was employing over half of the total employed people in 2007.

Economic regime and the state

The change of production structure has been a crucial factor behind the regional economic development in Finland. The technological progress and dynamics of the western mode of production have shaped the structure of production at the aggregate level and regional institutions and processes around them have moulded the structure at a regional level. As the examination above addressed the changes in the structure of production are dependent on the changes of many other structures and institutions. One of the most important changes has been the transformation of the economic regime. A culmination point for the transformation of the economic regime was the collapse of the Bretton Woods system in the beginning of the 1970s.

The Bretton Woods system was established after the Second World War with an intention to stabilise the world economy and to ensure favourable conditions for the growth of real economy. The Keynesian full employment was set as a primary economic target in almost all western countries⁹. The most important outcomes of the system were the regulation of capital movements with capital controls and consolidation of the currency system with fixed exchange rates. Regulative practices arose from the common understanding that speculative capital movements and deregulation of the economy was the primary reason behind the economic turbulence of 1930s (Helleiner 1994). The constructed regulative system enabled governments to manage demand and to control economy systematically with monetary and fiscal policies. Thus, the role of the state as an economic actor strengthened considerably.

The new economic regime was optional for the Finnish economy and for the emergent

⁹ The concept of full employment in Keynes's theory (1936) must be distinguished from the NAIRU full employment appearing in mainstream economics today. For Keynes full employment stood for situation where no individual was involuntarily unemployed. The NAIRU full employment is the level of unemployment that does not accelerate the inflation rate of the economy.

industrialisation process of 1950s. Although at the later day the financial conditions of the Bretton Woods era have been alleged to be very tight the regulation of financial markets did not pre-empt the positive development of the Finnish economy. For example, after the war the investment rate increased to the historical high and stayed there for the following four decades (Hjerpe & Vartia 2002). The economic growth was rapid and the unemployment rate remained low. From the historical perspective it seems that the time of Bretton Woods was favorable to the real economy as the promoters of the system had declared in 1940s (Marglin 1990).

As stated above, the economic regime had major effects on the regional structure of production and regional economic development. At the time of Bretton Woods the government and the central bank had huge role in financing investments. For example, firms needed a green light from the central bank to receive foreign loans (Pihkala 1986). The domestic loans were the main resource for investments. The role of the government was also active concerning the allocation of the financial resources and investment support was a popular policy instrument in 1960s and 1970s. As government was in control of the financial resources also spatial aspects could be taken into consideration when allocating investment grants and loans. Through state-owned companies the government could directly determine the location of production and new investment. As the even development of regions was ideologically supported there were few limitations for the decentralising process and hence the regional economic differences diminished in 1960s and 1970s.

The Bretton Woods system broke down in the beginning of 1970s. By the end of the decade all major currencies were floating as new currency regime was established. At the same time the dismantling of capital controls accelerated and the regulation of financial markets was reduced piece by piece. The wave of reforms went ashore in Finland in the beginning of the 1980s and national capital controls were reversed one at a time. The notable action was obtained in 1986 when firms were allowed to apply long term foreign loans without permission of the central bank and the interest rate controls of domestic bank lending were demolished (Kiander 2001). Hence, the possibilities of government to control the allocation of investments and the location of production were diminished substantially.

The impact of the transformation of economic regime started to show truly after the depression of 1990s although some aspects of the change had showed up already by the end of the previous decade. Increasing share of the effective demand consisted of exports and the share of gross investment decreased markedly in the Finnish economy. The industrial production started to disappear from peripheral areas as the international capital movements flowed towards more attractive areas with lower labour costs and location closer to the final markets. Some authors have called this process 'the new international division of labour' (Fröbel, Heinrichs & Kreye 1980; Scott 1996). The example of Finland addresses that it is equally reasonable to understand the process as the new international division of productive capital.

As mentioned before the economic regime constructed after the Second World War emphasised the role of state as an economic actor. The control over financial resources and the spatial allocation of productive capital were not only devices for the government to influence regional economic development. The foremost process defining the regional economic development in Finland and other Nordic countries was the rise and development of the welfare state. In Finland the welfare state process gained strength in 1960s and early

1970s as variety of novel social and welfare policies were introduced.

The welfare state and the economic regime relying on the Bretton Woods system and capital controls cannot be separated from each other. It has been stated that the regulative economic regime was a *sine qua non* for the welfare state (Helleiner 1995, Ryner 2002). Accordingly, the public social and health care programmes required public service production and large-scale income distribution. Thus, expansive fiscal policies became the prerequisite for the welfare state and the existed economic regime made expansive fiscal policies possible.

Public social and health services and the system of income distribution reduced income and welfare differences between individuals but also between regions. Hence, the welfare state became an inseparable part of regional policies in Finland and the processes of welfare state contributed heavily on the regional economic development (Eskelinen 2001, Tervo 2000). The redistribution of economic resources and the public service production have also diminished demand inequalities and thus provided better conditions for economic growth in disadvantaged regions. Moreover, because many distributive measures like unemployment allowances react automatically to the business cycle the welfare system acts as an automatic stabiliser smoothing the growth of regional differences if, for example, a recession treats regions differently (McKay 1994). These stabilisers activate without political decision making which makes them effective social mechanisms against income and welfare inequalities.

Although the national distribution system was cut down during and after the depression of 1990s is the welfare system still highly important when it comes to reducing regional income and welfare disparities (Törmä et al. 1995; Ahokas 2008). It seems that the transformation of the economic regime has had so far only minor effects on the regional redistribution system. In fact, when many other policy instruments have become history the significance of the 'great regional policy' has increased.

Also the development of the actual regional policy has followed the transformation of the economic regime. In addition, the changes in regional policy relate to the change of state institution. (Moisio 2007). As have been mentioned before the roots of the Finnish regional policy lie in the industrial policies of 1950s. The industrial policies got different forms in the 1970s but remained in the regional policy mix till 1980s. In the 1970s the traditional policies united with broader policies related to the construction of the welfare state (Vartiainen 1998). One of the most important and far reaching accomplishments was the establishment of the regional university network (Eskelinen 2001). The positive outcomes of the regional universities materialised in the mid-1995s when clusters of information technology industry rose around university locations, especially those with technical education and research.

As the economic power of the nation state diminished during 1980s the regional policy started to shift towards programme and project based practices. This development occurred at European level and the European integration process had noteworthy implications on the regional policies and regional economic development in Finland (Vartiainen 1998). The former regional policy employed by the nation state has been replaced with policies ran by local or regional authorities.

During the last three decades a twist has occurred in the objectives of regional policy. At the time of the Bretton Woods system and the post-war economic regime the rationale was that regional economic development and desirable institutional change within regions are highly

dependent on the productive investments (Myrdal 1957). Hence, the state ought to take care of the regional allocation of the financial resources and other distributional measures to ensure the even regional distribution of investments which was seen as a key element of the balanced spatial division of production. After the transformation of the regime the rationale has been that the regional policies should aim at developing regional institutional conditions and capacities to attract mobile capital flows and investments to regions (MacKinnon & Phelps 2001).

The revolution of economic regime has undoubtedly altered the power relations around regional economic development. The shift has become evident by examining Finnish regional policy under different economic regimes. Today the mobile capital is taken as given and the role of nation state is seen as inferior in relation to regional economic development. Although the regional and local authorities are today responsible for regional policy they have not inherited the power the nation state had at the time of the post-war economic regime. Keeping in mind the final aim of today's regional policy the track record of Finnish regional policies have been some what poor. During the depression of the early 1990s the rate of investment dropped over 10 percentage points and the recovery from the bottom has been extremely slow. At the same time net foreign direct investments have increased considerably (Sauramo 2008). Thus, in Finland the challenges for the contemporary regional policy are substantial.

Firm

An essential institution contributing to the regional economic development is firm. In the recent studies of regional development the role of firms has been highlighted and firms have been understood as fundamental regional actors. Accordingly, the economic development paths building up around large firms and clusters of firms have been under vigorous investigation¹⁰. As firms are producers, employers and investors the observations of their importance concerning the regional economic development cannot be rejected.

But also firm as an institution - like economic regime and the state institution - is continuously changing which must be taken into consideration in the research of regional economic development. For example the firms of 1970s are totally different from the firms of today. Also the relations of firms with other social institutions and actors have changed a lot during the last decades.

An interesting approach to the transformation of the firm institution can be derived from Veblen (1923) who presented two main motives for the operation of firm. The industrial or productive motive is grounded on the ambition to create welfare for the society by innovating new products and services. Hence, the production as such is the objective and the purpose of the firm. The business motive, on the other hand, is founded on the desire for pecuniary profits. When business motive becomes dominant the actual production converts to the role of servant and to an instrument for successful business activity.

The business motive can be seen as a governing motive in the 'latter-day firm'. However, at different times the industrial motive has gained ground from the business motive. At the time of the Bretton Woods system with heavily restricted capital movements and regulated financial markets the speculative activity was reduced and the emphasis of the firms moved

¹⁰ For comprehensive analysis of the recent studies see Cumbers et al. (2003) and Martin & Sunley (2004).

towards productive activity. Without liquid capital markets also the investors and the capital owners participated to real investment projects and hence the growth of production was rapid and the investment rate stayed at high levels.

After the breakdown of the Bretton Woods system and the continued expansion of the global financial markets the business motive have gained back the lost ground. As financial markets have offered ever growing profit opportunities has the capital moved away from the real economy and firms have had difficulties finding investors and financial resources for their productive investments (Dumenil & Levy 2004). This development has come forward especially in the regions with high costs of production including Finland.

One important aspect behind the formation of the firm institution is the size of the firm. The bigger the firm the more dominant is the business motive. Under the current economic regime many large Finnish firms have become global enterprises operating and producing different places and geographical areas all over the world. The recent development has increased the differences between small and large firms and thus produced divergence to the progress of the firm institution.

From the perspective of regional economic development the form of the firm institution and the motives behind firm activity are highly important issues because also the location of the firm is dependent on them. The strong industrial motive drives firms to make location decision on the grounds of the real economic factors. Correspondingly, the more powerful is the business motive the lesser extent real economic factors have effect in the firm's decision-making.

In Finland the large firms of the resource based industries are prime examples of the illustrated change. In recent years many production units have been shut down in Finland and other areas with comparatively higher costs of production. Some aspects of this development relate to the circumstances of the real economy. For example, new production plants are usually situated closer to the final markets. However, very often the decision to relocate production arises from the business motive and from the demand to achieve a higher rate of profit. The profit standards set by liquid financial markets are very difficult to meet in the real production which leads every now and then to the shut down of profitable units that just are not profitable enough (Orhangazi 2008). Hence, in recent years many profitable production units have disappeared from Finnish regions making the regional development process yet more unpredictable.

The understanding of different modes of firm institution is necessary in explaining the regional economic development and the role of a firm in this process. When the motives of different firms are apparent the common concepts of regional development studies like agglomeration, learning and innovation become useful tools for research of regional economic development. After all, all of these concepts are primarily associated with the industrial motive and only indirectly with the business motive. For example, in the recent studies of Finnish ICT-industry the perspective has concentrated heavily on the knowledge networks, technological innovations and other production practices and little on the profit structures and business incentives.

Boschma and Sotarauta (2007) have presented the recent development of the Finnish ICT-sector as an evolutionary process with various spatial implications. Although the years of

success of the sector realised not until in the end of 1990s the many development paths leading to the triumph had considerably longer history. The regional university network with high quality scholars especially in the field of technology and engineering provided the needed knowledge-base for the rising industry. The city of Oulu and the surrounding region in the northern Finland is an excellent example of the significance of suitable institutional conditions at the time of technological revolution. Within the last decades the region has transformed from declining region to a prosperous and fast developing region with numerous of successful ICT-firms.

However, the regional development paths of ICT-sector have diverted and the industry has developed differently in different university regions with similar kind of knowledge base (Sotarauta & Srinivas 2006). Accordingly, regional institutional settings are different and they can direct the process of regional economic development to multiple different development paths although the guiding processes are more or less identical.

As is addressed before firms do not operate independent of other social institutions and social actors. One of the most important interactions concerning the regional economic development is that of between firms and the state. Some aspects of this connection have already been highlighted in the previous part of the article. Till 1970s the relationship between the state and firms was almost symbiotic as government took part actively to the economic life providing loans and investment grants for the firms and controlling the financial conditions. Also the monetary and currency policies were aimed at supporting the export sector and firms operating at international markets (Pekkarinen & Vartiainen 1995).

The new economic regime, new regional policies and new economic policies have altered the relationship between the state and firms. From 1990's on increasing part of the government support has been given to firms in the form of research and development expenditure. Also public projects and different kinds of subsidies relating to innovations and learning have become common. Because firms benefiting from today's policies are oftentimes centralised to certain geographical areas have policies become intrinsically centralising compared that to the previous export based economic policy strategy.

There are also other measures that have been conducted in order to obtain appropriate institutional conditions for the large global enterprises. For example, the reduction of corporate taxes has been seen necessary in attracting more inward capital flows to Finland. Government has also decreased ownership and diminished ownership control in firms. This has had an impact to the regional policies as government has been unwilling to intervene, for example to location decisions of public owned companies. Hence, the power of large global enterprises has increased at the expense of the nation state. However, at the same time the power of rentiers, investors and absentee owners over firms has increased telling the already familiar story of the rise of the business motive in the contemporary western economy and society.

Like the relationship between firms and the state also the relationship between firms and the labour movement has been close in the Finnish society. The birth of the so called 'agreement society' and the rising power of the trade unions in 1950s and 1960s lead to a rather peaceful consensus of the state, labour movement and firms (Bergholm 2007). The labour market bargaining with all three participants showed the way towards collective wage agreements strived to ensure the much needed restriction of the wage inflation vital for the export sector

and its compatibility. The modest wage rises were compensated for the labour with social programmes and redistributive measures (Pekkarinen & Vartiainen 1995). Despite the moderate wage rises the wage and welfare policies of 1960s and 1970s changed the functional distribution of income raising the wage share continuously. This development was very important from the perspective of regional economic development as the growth of wages contributed to the domestic demand and thus also the local service sector gained from the growth of the export sector.

Under the contemporary economic regime the power of the labour movement and trade unions have decreased considerably but their strategies and course of action have changed only little. The change in the functional distribution of income in the 1990s shows that the economic power¹¹ of the wage earners has diminished in proportion to the firms and capital owners as the corporate and individual profits have increased substantially faster than wages (Kyyrä 2002). However, moderate or even modest wage rises are seen as necessary by trade unions. The common justification for the 'wage restraint' is that the only possibility to attract mobile capital to Finland is to provide lower production costs compared with the international competitors, that is, other geographical areas.

Trade unions have united with private corporate sector also in the energy policies demanding new nuclear power plants to be constructed in Finland. The same rationale goes here as lower energy costs are seen necessary for the competitiveness of Finnish export industries. Despite the compromises of the labour movement the recent development has been turbulent for the export industries and especially for historically important resource based industries, first and foremost for the forest industry. From the perspective of regional economic development the decline of this sector is crucial as production units of the industry have been located mostly in the Northern and Eastern Finland where economic growth of other sectors has been weak compared with the urban areas of Southern Finland. This development has evoked demands for government action against the large international corporations concerning the location decisions of production but the government has been unwilling to step in even in the cases where it has been a partial owner of the firm (Pikkarainen 2008).

Ideologies and ideological structure

The majority of the processes described above have been material relating to concrete and observable social action. However, material processes and human action interact with the ideological structure and also the implications of immaterial ideologies for the regional economic development are consequential. An ideology is a mode of thought that determines social action. Mostly the influence of ideology to human action and human behavior is unconscious which makes ideologies very powerful social institutions and structures (Gramsci 1979).

From the perspective of regional economic development the most important ideologies rise from the economic theory and theories of regional development. This fact sets a challenge for the research of regional economic development as the theories of the discipline have an effect on the material processes of regional development. In this sense the research of regional development and theories occupied within regional development studies should be specified as research subjects of the discipline.

¹¹ The concept of economic power of the wage-earners is obtained from Kalecki (1971). See for more Asimakopulos (1975) and Setterfield (2007).

Besides the theories of regional development the theories of economics have contributed considerably to the regional economic development as paradigm shifts in economics have transformed the mode of economic thought in society. For example, the Bretton Woods system would have never been established in realised form without the economic theory of John Maynard Keynes (1933, 1936). Moreover, Keynes' influence on the establishment was also concrete as he worked as a negotiator of Britain in Bretton Woods in 1944. This way the change of economic thought in society shaped substantially the material development of western society in following decades.

Korpinen (1981) has presented an interesting cycle theory on paradigm shifts in economics and their connections with material economic development. At the time of rapid growth the inflation accelerates causing problems for the economy. This is the time when so called monetarist theories become general trying to work the way out from the inflation cycle. After the monetarist view becomes hegemonic and economic policies are altered in order to curb inflation economic growth stagnates and deflationary tendencies strengthen. Hence, the economy is confronted with new kinds of problems and new economic thinking is needed to answer these problems. Again the Keynesian economic theory becomes dominant changing also the direction of economic policies (Patomäki 2005).

The processes described by Korpinen can be held as an explanation for the transformation of the economic thought in the end of 1960's and in the beginning of 1970s which lead finally to the breakdown of the Bretton Woods system. After the long period of rapid economic growth and inflationary tendencies the monetarist view and especially the economic theory developed by Milton Friedman begun to gain ground offering solutions for the existing problems of the economy (Friedman 1968).

As has been presented earlier the processes originating from the transformation of economic regime which was encouraged by the transformation of the economic thought has altered the regional economic development in Finland substantially, especially after the 1980s. The change in regional policy and regional development strategies has reinforced the transformation. The evolution of regional development theories has contributed heavily to this change.

In the 1950s and 1960s regional development strategies of Finland and other European countries were profoundly influenced by the theories of uneven regional development that assumed regionally polarized growth patterns to be the inevitable outcome of the economic development process (Kiljunen 1979). For example the theoretical work of Perroux (1950), Myrdal (1957) and Hirschman (1958) constituted a powerful ideology that convinced policymakers of the need for regional policy in the battle against uneven regional development. These theories were closely connected to the Keynesian economic thought underlining the importance of the state's control over the economy.

Though, the cycles illustrated by Korpinen are to be found also in the mode of thinking concerning regional economic development. In line with the transformation of economic thought also the dominating regional theories changed during 1980s. The turn brought back many theoretical constructions from earlier times (Martin & Sunley 1996). For example, the concept of agglomeration appeared first time in the regional science and location theory already in early 20th century. (e.g. Weber 1909/1929). The equilibrium or multi-equilibrium

models of regional economic development have become very popular and also the 'thought of regional development' and thus regional policies have adjusted towards region based and market based approaches. Accordingly, this is the natural course of action when equilibrium approaches gain ground in the field of regional economic development (Kiljunen 1979).

Also regional policies in Finland have been influenced by the rise of this 'new regionalism' (Lovering 1999). According to Lovering the rise of 'new regionalism' stands for a development of 'a new cognitive and normative framework' that draws attention 'to some issues and policy objectives and away from others'. On the grounds of this definition 'new regionalism' can be understood as a prime example of hegemonic ideology determining the possible theoretical frameworks for the research of regional economic development and the possible strategies for regional policy. Of course, there is always a great risk to exclude relevant or even fundamental theoretical approaches that just do not fit in the current ideological framework. Hence, the critical approach that recognizes regional theories as ideologies and seeks to expose their interactions with other social processes is vital for the understanding of the regional economic development.

The dialectical interaction of ideological and material processes of regional development can be examined with the help of the praiseworthy analysis of Moisio and Vasanen (2008) on the spatial aspects of the transformation of state institution. According to the authors changes in the material processes of regional development are frequently derived from the specific ideologies of regionalism. Hence, a vision of a certain regional pattern precedes its development in the material reality.

Recently, the concept of metropolis has been introduced in the Finnish regional policy vocabulary. Policymakers have started to call for 'policies for metropolis' and see the centralised regional pattern as an inevitable result of the ongoing processes. Although the regional development process has most certainly been centralising during the last two decades it is fairly safe to declare that Finland is still lacking of a true metropolis at least in European standards. However, if the *senso commune* of regional development supposes the metropolis the chance of having one in the future is altogether greater.

4 Conclusions

The research of regional economic development is a dynamic and ongoing process. The purpose of this article was to contribute to this process by setting up a research framework of regional economic development that could be occupied in the future work. The idea behind the construction of the framework was that before theoretical and thematic considerations are possible the ontological basis for the research should be appropriately defined.

The ontological commitments presented in the paper relate closely to the critical realist understanding of social realm. The social structures, institutions and social action interact with each other generating social processes. Social processes are understood to be evolutionary materialising in the open space. Thus, a flat spatial ontology with aspects of relational understanding of space completes the ontological picture behind the constructed research framework.

The actual research process should start with the analysis of the actualised processes around

institutions and structures that are relevant for regional economic development. Theoretical framing is needed already at this point of the research to specify these social objects. After describing main processes around key institutions and the interactions between them further theoretical and methodological commitments should be proposed in order to shed light on the real causal mechanisms that are the final objects of the research.

As regional economic development is a dynamic and evolutionary process that will never be completed, as well is the research process. Hence, the aim of the research is to generate continuously novel explanations by redefining and questioning the prevailing perspectives. Researchers should persistently make efforts to expand the vision of the research field by introducing in their studies further dimensions of some previously defined phenomenon.

The processes around the five elementary institutions and structures of regional economic development were analysed to capture basic understanding of regional development in Finland. The analysis showed that although processes around them are universal (strictly speaking demi-universal) spatial and regional differences exist and hence the concepts of regional institution and regional structure become relevant. Already the simple investigation confirmed that a deeper examination of these institutions and structures provides a path towards a comprehensive view of regional economic development.

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