

**Regions, cities and the world:  
well-connected or subprime views?**

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### **Abstract**

Connected regions are the basis of national economies and global trade yet the models used to study them are relatively little appreciated. Regions themselves are internally differentiated, with concentrations in activities and populations to be found in cities and towns and around various natural or other resources. How such things influence connectedness and our views of it are central to this paper.

Regions, cities and the world are all connected in various ways. Connections may be of various types, duration and significance. Connections associated with external trade are taken as a point of focus and development. Consideration of some of the alternative views in use demonstrates not just the partiality of various views but also confusions that can arise when differences go unappreciated. De Bono (1986) finds such things at the basis of our inability to solve many important problems.

It will be seen that views and models have been chosen from a relatively narrow suite of simple idealisations, empirical studies and compelling images. Associated policies and actions have been predisposed by these particular and limited viewpoints. While this may have been acceptable in a relatively stable world it becomes problematic and perhaps dangerous at times of instability or marked uncertainty, such as the present.

A need for much better dialogues has long been evident. It is much more pressing today given the considerable push for very large sums of regional infrastructure investment. Subprime regional development thinking or actions today could be very costly tomorrow.

## 1. Orientation

The connectedness due to trade of regions, cities and the wider world is the focus in this paper. How connectedness is viewed is the first concern. Distinctive viewpoints exist, including the practical (focussed on “action now”), theoretical (focussed on “more general” patterns) and the empirical (focussed on “recorded observations”).

Each viewpoint involves a distinctive mix of approach, concepts and constructs. Observers and active participants are alternately positioned and variously presumed actively involved or not.

- A practical person may seek “to move product”, that is to achieve physical export.
- A more theoretical person may seek “to understand patterns of trade” (and/or payments) including, perhaps, why and under what conditions trade occurs.
- A more empirically inclined person may seek “to analyse the data”, typically so as to establish what have been “the important” sectors.

All three viewpoints are to be found in a region, conference, nation or indeed almost any group gathering. Each viewpoint can contribute meaningful insights. None alone is sufficient for robust understanding.

***An example illustrates:*** a map may show prices at various places for a product, say a kilogram of beef or a litre of milk at some time. Such is the empirical pattern, one which spells out some “noted difference”. Given such price differences, a theorist might expect arbitrage-driven trade. Product is assumed able to be moved from place to place so as to take advantage of price differences. The more practical person might point to transport, industry or refrigeration difficulties as “causing” differences, and of the need to address these “real problems”.

Each sees different things as significant and each may see various opportunities, needs and risks. Problems are compounded if each uses distinctive and dis-connected representations or inadequate dialogues. This was well-demonstrated by a presenter to an academic seminar who mapped beef prices in several cities of Russia in the mid 1990s and then asked for audience suggestions. Somewhat predictably, responses missed what turned out to be a major point: that organised crime had established “informal customs booths” around the city with the highest prices. None had suggested the need to remedy criminal behaviours, despite this being a focus of the seminar.

Distinctive viewpoints involve particular views of regions, cities and the world. Underlying thinking may be put somewhat over-simply as a more:

- practical view, interactions occur in some structured space and time.
- theoretical view, stylised transactions cross voids.
- empirical view, partial records are compiled and analysed.

Ideally each of these views should be well matched so as to provide suitable complementary insights. Too often, however, one view is assumed sufficient.

Mismatches between views are common. Theoretical and empirical views may be markedly mismatched not only with each other but with practical realities, for example. The implications of such mismatches may be very significant, as in the current sub-prime fiasco and attendant tragedies. Here not only were empirical records flawed (and too often fraudulently based) but the theoretical view was limited. Gaps were selectively exploited by the opportunist aided by the incompetent. Even the most diligent were misled.

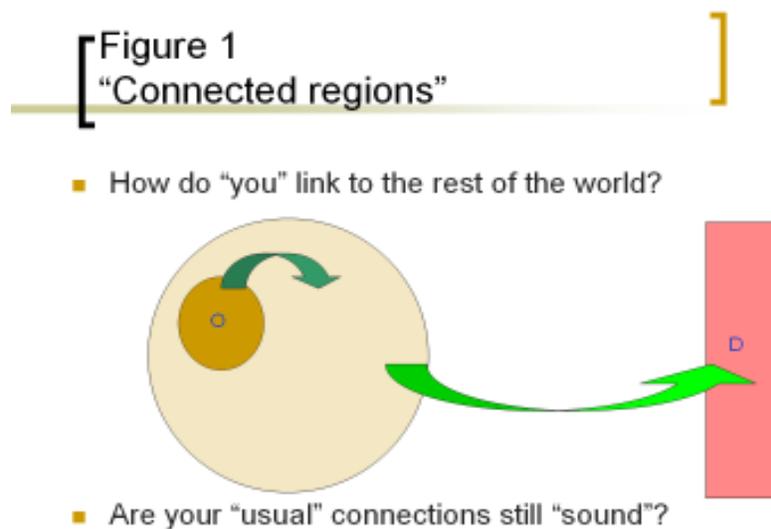
Subprime finance is not the concern of this paper but it raises nicely the issue of whether we have subprime regional thinking in Australia. My working premise is that theoretical, empirical and practical views are often not well matched. Further, alternative theoretical views are used without recognition of the significant differences between them. International trade theory provides some examples. In such disjointed circumstances policy will rely more upon the power of interests than the power of relevant ideas.

How might cities, regions and the world be better viewed for purposes of regional development? Answering such a broad question is beyond the scope of a paper such as this but some directions can be discussed so as to help advance constructive dialogues.

## 2. Approaches: positioning city, region and world

*How do and might we view “a region” or “regions, cities and the world”?*  
 Answers to this central question can be developed in a number of ways. Each “answer” will involve a particular approach which will incorporate selected views and viewpoints.

Consider the schema outline in Figure 1. Links via “a flow” are shown by using arrows from an origin O within a small circle to a destination D in a distant rectangle. Between lie a large circle which encompasses the small circle and some “unallocated” space. Two interpretative questions are also posed.



Interpreting the first **question of how you link** requires “your allocation” to at least one of: the small or large circle; the rectangle; the small or large arrow; or an unallocated space. Placements within each of these extended objects (such as at an arrow tip or tail) changes both proximity to other objects and any imputations such proximity might have: “at the tip” might have an inference of linking to the next stage or cutting through, for example.

Many such inferences may be implicit as may be the value ascribed to some placement. Consider phrases such as being “at the cutting edge” or “top” of an organisation, or “getting there” (as when some “one” figuratively moves “along the arrow” towards the tip). Colloquially in Australia being “in the regions” often seems to imply being “away from the action” or places of importance. Habit and popular use, often via a conventional wisdom, reinforce easy acceptance of such popular assumptions.

Assigning “where you fit” introduces not just placement but also associated inferences of what you do or may be able to do. Richardson (1978) contrasts the “neoclassical view of interregional competition as a struggle among equals” (p 150) with the core-periphery view within which spatial distribution of power tends to be unequal. “The core regions are defined in terms of control over their own destinies while the peripheral regions are dependent upon and controlled by the core.” (p 151)

The competitive market position at the heart of the neoclassical view is based upon an absence of structure, both internally and externally to a party, and upon the hegemony of the market.<sup>1</sup> “Price takers” and any like parties are essentially peripheral. At the core are “market conditions somehow set”.

The setting of market conditions has been considered in many ways including:

- through some “proper” appreciation of difference with trade resulting, as in the comparative advantage of Ricardo;
- through some “proper” appreciation of some entity state, such as in the widely influential marginal (cost, revenue, utility, benefit etc) position;
- via some automatic mechanism, as in formal models that assume a tendency towards equilibrium such as with supply and demand curves;
- via some disruptive mechanism, as in models that assume a tendency towards disequilibrium or far from equilibrium situations;
- by simultaneous decisions of many fully informed parties, as in the Walrasian general equilibrium;
- by sequential decisions of some active parties, as in many innovation, transition and development models;
- through the exploitive actions of countries as in colonialism;
- through the exploitive actions of companies, as in dominated supply chains; and
- through the exploitive actions of consumers, as in unsustainable demand arguments.

Choices made about the setting of market conditions matter. Each may be influential in any situation with attempts to establish a dominant view common.

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<sup>1</sup> In the polar opposite of monopoly it is the hegemony of one firm that matters.

While one or more parties may be influential in a market, continuance of a market requires that it be sufficiently mutually acceptable to all involved and affected parties. A central problem in both the subprime crisis and the infrastructure challenge is finding solutions that are sufficiently acceptable to all parties, such as:

- depositors, lenders and borrowers;
- banks and other financial intermediaries;
- governments in their various roles<sup>2</sup>;
- host and affected societies and nations; and
- “market participants” more generally;

Wall Street and Main Street and Your Street, at home and abroad, need to be somehow sufficiently reconciled adequately if the crisis is to properly pass.

In the era of globalisation and multi-national enterprises just passing, the core tended to be in MNE head offices that were located in global financial and managerial hubs. Integration was towards a few centres, the world cities. The primacy of the world city is currently under challenge by “meltdown”: not just individual enterprises but global systems and centres of influence (such as “Wall Street”) are degenerating with some in danger of collapse.

In the recent era of “competitively going for growth”, current consumption and financial positioning moved to the core (Reich 2008). Consumers and financial investors in an individualistic society were made sovereign. Producers, capital formation, common interests, public works and everyday life were peripheral in both mindset and policy. Infrastructure underinvestment was pervasive, for example, as capital was run down to support driven current consumption and immediate financial returns for some in the short run.

Authors such as Rothkopf (2008) see a small group of people at the core, an elite that sets directions, agenda, initiatives and the like. It is not the presence of a core *per se* but rather its capacity and adequacy that warrants attentions. Failure at the core presents peculiarly grave risks. It is the struggle for positioning in the new core that makes the current global dilemma both fascinating and grave.

Comments in this section, including the last three paragraphs, briefly indicate:

- An era in which a particular type of connectedness was favoured;
- A preoccupation with preferentially satisfying some economic (and other) criteria but not others; and
- The importance of an adequate core, one populated by adequate conventions, people and ideas.

In order to address the economic shortcomings arising from this era past, some repopulating of at least our intellectual core seems warranted. Such is the guiding premise of this paper.

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<sup>2</sup> It is worth recalling the multiple roles of governments which various act as citizen representatives, regulators, owners or part owners, major consumers and investors, providers of public goods and public works (or “infrastructure” in more recent times), opinion leaders and custodians of sovereignty.

### 3. Some illustrations using the Schema

A representation such as Figure 1 presumes much. Hidden behind this abstract representation are all manner of assumptions and accommodations. Each era brings its own predispositions as does each participant and observer.

Conventional wisdoms capture common ground. Such wisdoms may be difficult to overturn, often persisting well beyond their useful life (Galbraith 1958). Inadequate understandings, conceptualisations and conventional wisdoms appear to be impeding the development of Australia, its regions and cities.

In addressing issues associated with such overarching bias a key question is: Are there some parts of a schema (such as in Figure 1) which exhibit particular and significant influences *always or under certain conditions*, and how are such influences conveyed?

While schools of thought may generalise about where and how they see such overarching influence, the underlying question is a general one: in any set of connected regions how do various influences play out overall and as impacting on parts?

This broad question will be left for now but preferred answers underlie and colour much private or public policy and other pragmatic thinking. Region, city and world when connected by which ever links can be variously expected to have roles and importance, as can the parts thereof. Interdependencies not only come in many guises but also in various modes of significance (both to itself and to the wider group). How might we check the adequacy of our current predispositions and biases towards the city, region and world trio?

All parts of a schema may have a role to play with each significant in its own ways or at various times or places. Determining which is “most important” appears problematic. It assumes a generality not present in reality. More sensibly we might focus on what are the impacts of deficiencies in any area. How does a failure to satisfy or satisfice “here” impact “elsewhere” or “everywhere”?

It is here that impact analysis can play a central role. However, the state of the art is currently weak due in part to decades of neglect of important issues by researchers, businesses and policy makers. Forging satisfactory new accommodations requires review of connectedness and impacts. From such might emerge better organisational and conventional wisdoms.

In a participative society, particular resolutions and established hierarchy are dependent on sufficient acceptance by and conformance in the group. Being “at the top” requires something useful below, unless it is to be pure vanity. Being “in the society” voluntarily requires sufficient returns for each, as those dealing with problems of alienation and societal cohesion appreciate.

These broader considerations have been long discussed in political literatures, as in the notions of representative governments with popularly accepted leadership. They have been less explicitly considered of late in economics, notably in trade and economic development literatures that revolve around perfectible systems of trade or market. Renewed interest in transition, development, cohesion, “fair” trade and the like has yet to impact significantly on the mainstream consensus. In terms of the connectedness of regions, cities and the world there appears to have been little done or thought.

The second question posed in Figure 1 highlights a tendency to assume that the past persists somewhat automatically. Such a habit is useful in dealing with complexity and appears reasonable in dealing with stable situations. It can be counterproductive, however, when the intent is to change the region, city or world or to interpret the effects of some changes in such locales.

In terms of relative scales in the Figure, what might be the effect of making the rectangle half as wide or the distance between O and D greater?

- Movements in the Australian dollar essentially doubled the apparent size of the Australian economy between 2001 and 2008, and halved overseas parties. Movements in recent months have trimmed Australia back thirty percent.
- Rises in energy costs helped markedly raise transport costs during 2007-08. Iron ore to China from Brazil suffered a major cost disadvantage when compared to that from Australia. If oil had reached \$200/ barrel then all the trade liberalisation efforts since the 1970s would have effectively been undone.

Currency movements have varied the relative sizes of markets and the returns from exports. Rising energy costs lengthen the economic distance between O and D. While such movements can be expected the high volatility and uncertainties of recent times adds a new dimension to interregional risks. Issues of scale and changes in relative positions need attention at such times.

City, region and world can be taken as three distinct entities. Which position might each adopt in the schema of Figure1, and what of “empty space”? A simple example of an overseas owned coal mine (Table 1) illustrates.

**Table 1: Specifying and linking a multi-regional trade: an illustration**

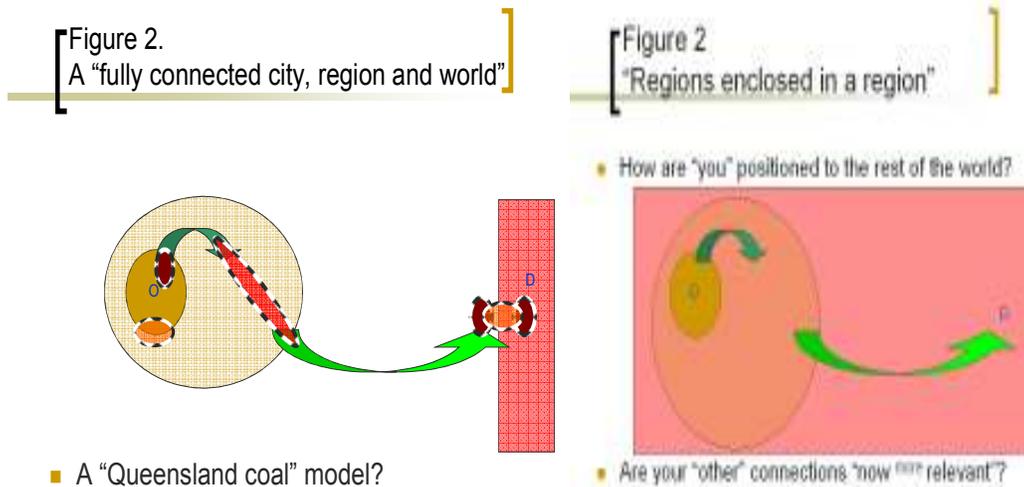
	<b>O small circle</b>	<b>large circle</b>	<b>D rectangle</b>	<b>Space - between the arrows</b>	<b>Space – covered by the arrows</b>
Base Set	Exploitable resource in some locale	Host country (not, potentially or actually peripheral?)	Core enterprise in hub city	“Local” conditions and issues	A reliable transport or other link
Line(s) of influence	<b><i>How and where might links be established and distributed - and with what influences?</i></b>				
An instance	Mine site and surrounds	Hinterland region to coast	Overseas “market”	Overland transport link (eg rail)	Ocean link (eg bulk carrier)

Unspecified in Table 1 are the lines of influence assumed. In a full enclave situation the rectangle might link directly to both small circle and spaces while bypassing the large circle. The small circle (“mine”) effectively “sits outside” its host region. Any impacts in the host country would then be incidental rather than planned or negotiated. Linking the large circle to the spaces indicates influences different to those originating in the rectangle. Mutual accommodations will need to be sought between the two heads of influence.

But are such schema directly applicable? Considerations of Bougainville copper (or how to lose both a mine and your investment because of neglect of local impacts) point to some of the problems with a full enclave approach. Considerations of Australian bulk transport arrangements (where privately owned railways operate in the Western mineral provinces, a public railway operates in Queensland and various mixes operate in the South East States) indicate not just that there are several alternatives but that each can operate “reasonably successfully”.

Configurations matter, as do the details of how links are made. There are many configurations nested in any trade, be it local or international. Experience around the world demonstrates that there are also many configurations that can be successful.

The key to success seems to be more in an inclusive appreciation of the possibilities rather than some definitive blueprint or template. More directly, people can make things work in many ways but they need to share a sufficient common picture. Potential uses of the changes such as those shown in Figure 2 are left for discussion. “Filling in the gaps” is the focus on the left while “an encompassing world” is presented on the right. Each is distinctive.



Actions will be differently cast in each example. Which parts might will, and should those interested in regional development be focussing on, for example? Similarly, towards which parts may investment funds be preferentially put, and what influence does the location (where?) of an investor have? Distinctive groups may develop common grounds via such schema.

#### 4. Trade itself.

A central theme provides coherence in any approach to an object, issue or problem. Constructive dialogues involve developments around some implicitly or explicitly accepted theme. Without an accepted theme dialogues become fragmented and confused. Without an appropriate theme, dialogues become convoluted, prone to loss of relevance and potentially misleading.

Consider the theme of “trade”. In international trade, products are exchanged by parties and between nations. Which are the parties used in a particularly preferred approach?

- Practically, firms and their factors “do most of the work”. Though governments set the scene, inter-enterprise functional and financial linkages are often taken as central.
- Theoretically, the parties may be nations, sectors, regions, factors of production and only sometimes firms. These link “somehow”.
- Empirically, aggregate statistics are compiled for trading sectors in some nation or region. Enterprises run their own distinctive accounts which are little reconciled to the aggregate.

In any viewpoint some primarily practical, theoretical or empirical basis will be developed in a particular way.

Trade is typically taken to be mutually advantageous. This assumption may be elevated to a position of received truth as commonly appears in business and policy discussions. A positive sum situation is virtually automatically presumed, along with the position that growth and trade go together. This is despite theoretical and empirical arguments that such things need not be so.

Alternative models of positive sum associations can be developed, with comparative advantage being one of the oldest. Theoretically, distributional issues will need attention as do those of interdependence under uncertainty. Empirically, we find limited support in the literature for any single or simple models. Practically, there are all manner of concerns to be dealt with effectively if ideas are to guide actions “appropriately”.

Consider three of the models used in discussing trade:

- **Comparative advantage** (Ricardo 1821), that mutual gain is possible by specialisation and trade;
- **Competitive advantage** (Porter 1990), that group gain is possible by complementary actions, strategies and positions; and
- **Absolute advantage** (after Smith 1986 [1776]), that particular gain is possible by locating with lowest cost operation.

These three views of advantage are markedly distinctive and different. For example, while comparative advantage involves two actively trading regions, competitive and absolute advantage essentially focus on one. However, the three are often used interchangeably, with little apparent recognition of difference or of the significance of differences. Even differences in developments themselves go unrecognised. Some schematics can be used to illustrate the developments of these key ideas in trade.

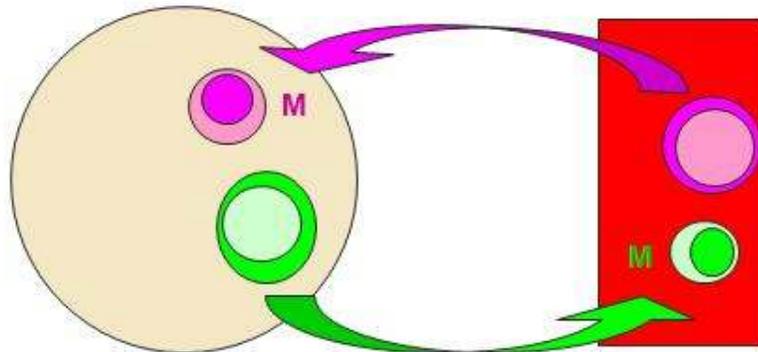
Comparative advantage can be considered in terms of the single factor model, as originally favoured by Ricardo, or a two factor model. A full development can be found in works such as Feenstra and Taylor (2008) or Krugman and Obstfeld (2009). The schema in Figures 3 and 4 show:

- differences in base positions, as to what is in the model and what is not;
- how these things are connected between two regions or nations (in both Figures), as well as within (Figure 4 only, left region shown); and
- the expected consequences of trade, as illustrated by the growing or shrinking circles representing changes in production or factor returns.

### Figure 3: Comparative advantage 1

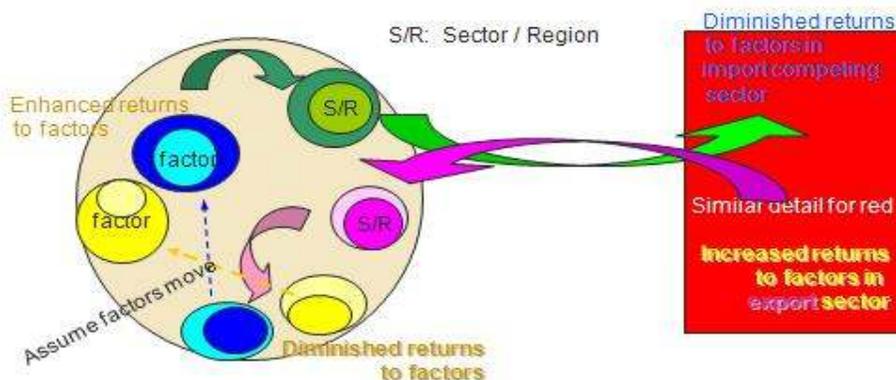
- **Allocable surplus if two regions specialise and trade**

Local production goes from light to dark, with M imports consequent



### Figure 4: Comparative advantage 2

- With multiple factors of production, gains to factors used in exports but less to factors in import competing sectors.

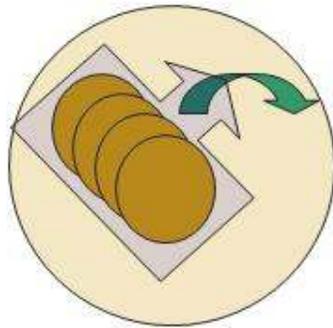


Of particular note is that while the first development of comparative advantage highlights the creation of a surplus through trade (additional production to that which would occur if each produced for its market alone), the second also highlights the different returns resulting to factors depending on whether they are in export sectors (which gain) or import competing sectors (which lose).

Representations of the alternative viewpoints of competitive advantage and absolute advantage are shown in Figures 5 and 6. The individualistic preoccupation of Porter's competitive advantage is clear as is the essential asymmetry of absolute advantage (whereby all tradeable production would be attracted to the low cost nation or region).

## Figure 5: Competitive advantage

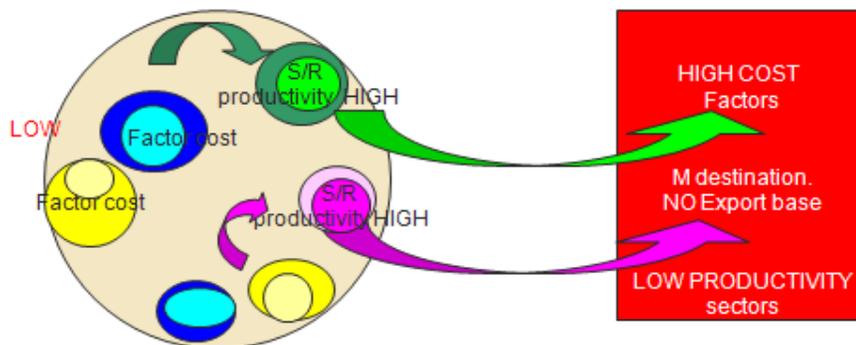
- Making your regional cluster work...



A single region focus.  
Double diamond models  
have gained surprisingly  
little traction.

## Figure 6: Absolute advantage

- With multiple factors of production in multiple locations, where are costs lowest?



Stark differences are evident in all four Figures. Porter (1990) did assert, after all, that he was developing a new trade paradigm in competitive advantage, not some refinement of the pre-existing. Yet each viewpoint has some relevance to trade. Each would have its champions, as can be briefly illustrated (using the numbering of corresponding Figures):

3. *naïve trade is good* view, since a surplus must be good in a state of scarcity (and we are all winners overall). Such is the theme of Comparative Advantage 1;
4. *trade is mixed* as differentiated effects on returns to factors exist (and whether winners should compensate losers is a moot point). Such is the theme of Comparative Advantage 2;
5. *trade is there for the taking* providing you organise, work in complementary ways to compete strategically (and winners are those who work at it). Such is the theme of Competitive Advantage; and
6. *trade is from the lowest cost producers* since, as any firm driven by cost accounting will relate, minimising costs is a business priority. Such is the theme of Absolute Advantage.

Again illustratively, it seems that in Australia these views are preferentially held by different groups including:

3. the Australian government generally, particularly in international trade discussions and spiels;
4. those interested in trade impacts, such as some unions and industry groups (notably those in negatively impacted areas) along with fair trade proponents;
5. state governments and regional development bodies (wherein every region has its cluster and diamonds are to abound) ; and
6. firms, MNEs and large business lobby groups (which favour facilities at “competitively” low cost or low tax sites and supply in chains built across these).

Different parties and advocacy groups can be expected to gravitate to the view and model that best advances key interests. They would also seek to structure dialogues from their own viewpoints.

Jones (1997) finds Australia “trapped by an outdated concept of ‘comparative advantage’ and [a nation that] has barely responded to Porter’s concept of ‘competitive advantage’.” Despite some efforts, particularly in the regions and some States, the charge holds true a decade later it seems.

## **5. Re-Positioning Cities, Regions and the World**

*“The modern theory of international trade began with the demonstration by David Ricardo, writing in 1817, that trade is mutually beneficial to countries. ... Yet almost surely the British economy of 1817 was better described by a model of several factors of production than by the one-factor model Ricardo presented.”* (Krugman and Obstfeld 2009, “Income Distribution and the Beginnings of Trade Theory” Box on p 76)

Why did Ricardo make such a choice of model and couch his viewpoint in a relatively abstract and theoretical fashion?

*“Almost surely the answer is political. While Ricardo was in reality to some extent representing the interest of a single group, he emphasised the gains to the nation as a whole. This was a clever and thoroughly modern strategy, one that pioneered the use of economic theory as a political instrument”. (ibid)*

Ricardo was effectively arguing in favour of a particular income distribution in advancing his theory of trade. Using a single factor essentially assumed away any internal income distribution issues. Ricardo’s central idea is clearly an important one, and a mainspring of much economic and political talk. However, income distribution is also an important idea, one highly relevant to cities and regions in today’s world.

When we view the connectedness of cities, regions and the world we are focussing not just on economic but also on political issues and adopting some position about such things. Any “preferred” view and viewpoint introduces biases and omissions that deserve to be appreciated.

Much discussion fails to recognise this adequately, if at all. The fundamental differences between the Commonwealth and State governments on trade and development, illustrated by their preferences for simple comparative and competitive advantage arguments, need to be more fully appreciated as does the importance of melding appropriate complementarity between legitimately held viewpoints. Krugman (1996) found similarities in the USA

Constructive dialogue is better centred about the adequacy of ideas than the occupancy of a position. A wider definition of legitimacy appears needed if dialogues are to be well built.

The current habit in Australian national dialogues of “one view covers all” is a needless and enfeebling one. It was acutely present in the 2020 Summit in early 2008 when the imperative quickly became the development of a final declaration rather than the advancement and due consideration of a range of important ideas and issues.

How a new government, one with considerable potential, could allow itself to become so blind-sighted and quickly committed to the agenda of the past is fascinating. It is again acutely present in the rush to implement infrastructure spending.

The current era will see considerable repositioning of cities and regions in a post-sub-prime world. That is, tomorrow will be different in some ways and unless we take the time and effort to try and appreciate such things sufficiently we risk being needlessly profligate with our resources and impoverished by our actions.

Such things are rarely easy to advance. Crisis can provide an opportunity for change but rushed solutions are not likely to succeed, unless through good luck or fortunate inspiration. Australia's dialogues about its cities and regions and their places in the world need to be built upon a much more secure base.

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