Assessment of local economic development and its factors to improve welfare in the several regions in Indonesia

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Abstract. This paper has developed a model in assessing local economic development performance by utilizing primary data collected from 3 regions in Indonesia using a participatory approach of 304 respondents in Singkawang, Bau-bau, and Kupang. It is observed that to achieve the local performance model, and divided by two different models. First is the human resource, infrastructure, social capital, and financial capital that positively impact entrepreneurial strategy. While institutions, technology, local government, and central government have no impact on entrepreneurial strategy. Second is entrepreneurial strategy has a positive impact on local economic development (local performance). Findings also revealed that all impact is positive, aligning with the existing literature of local economic development in developing countries.

1. Introduction
The concept of local economic development plays an important role and also as a contributor for the economy cycle especially in emerging countries. The main goal of regional economic development is to build up a local or regional area's economic capacity. This is a crucial matter in developing economic regions in remote areas because when the economic capacity increases its economic future, it will eventually lead to a higher quality of life for the people living in these areas.

This research aims to look deeper into the potential of remote areas in Indonesia through quantitative analysis and to find out the important variables that affect the LED Critical success factors (Local Economic Development) in several areas using a structural equation model. Moreover, with focusing on remote areas, in the most cases, the main problem come up into a system of hard to say economic activities. in almost all the time, that can be categorized as family-based productions depending on the natural circumstances as harvest time of the crops, weather conditions, etc. Furthermore, the researchers want to upscale and upgrade the existing economic activities to a high productivity-based system on these situations.

In addition, the specific objective of this research is not only to answer the needs of a community about this problem, but focus on realizing local partnerships, improving a better investment climate in the local area for future job growth, creating sustainable development activity and reducing poverty. In addition, the most important thing about this research also about future expectation that a city can become economic drivers who will contribute to local and regional growth. to empower the local governments in order to create good governance principles, to enable local governments and stakeholders with analyze and fulfill their own investment needs and to provide local partnerships tools and strong mindset to look forward for the future (www.worldbank.com retrieved on June 2014)

This research involving the participants from the several background such as central and local government, academician, locals, and private stakeholders who are collaborated to work together for...
construct a realistic business plan and converted into concrete action. The sample that used in this research includes 90 local workers in Singkawang, 107 local workers in Baubau and 107 local workers in Kupang. These places are being samples of Local Economic Regional Development (LERD) because of the uniqueness and advantage of the economic activity. Subsequently, Local Economic Regional Development (LERD) research is based on local initiatives, which also include local stakeholders who carry out analyzes and maximize competitive advantages resources in that area. This includes optimizing integrated local ideas and skills to drive regional economic growth and development. Through this LERD program, local people government administration is expected in the future to be able to make plans and action related to the optimization of the regional economy below. Moreover, overall about this research is useful in terms of improving better quality of life in all aspects of the society.

Furthermore, this research are trying to answer the following main issues such as: "What are the factors that influence local economic development in three secluded areas in Indonesia?" With this research question, we intend to investigate the factors that influence local economic development. In view of the above consideration, a novelty of this study is that it adopts a quantitative analysis approach which derived from the qualitative model by conducting survey through self-administered questionnaires to the staff of local government, academician, private sectors, and locals who are induced to work together to improve quality of life, create new opportunities and fight poverty in Bau-Bau, Singkawang and Kupang. This three area has been chosen since Indonesian president chooses this area as piloting area for city development. The results of this quantitative research are used to identify the final model of local economic development in Indonesia, then this model can be generalized not only in the scope of research in Indonesia but can apply to global conditions.

1.1. Local economic and regional development

Local and regional development definition has been broadened into encouraging inclusive government and governance [7]. Local and regional development is defined as a study related to productivity and with the implementation in the East and Southeast Asia region. Furthermore, differences in the quality of development carried out by government agencies greatly affect economic performance in that regions. It means that the relationship between the central-local is one of the important roles for regional and local economic development under the responsibility of sub-national or sub-state governments. [2]. For the central government are able to apply policies in the scope of local communities, it is very important to have the support system of strategic groups within the regional community to negotiate and carry out its policies. Moreover, the result of a regional economic development process or as known as the dependent variable (local performance) – is the extent to which a local region has achieved a specific targeted competitive performance and the concept of sustainable development program through its regional governance. From the previous literature, institution, natural resources, Infrastructure and technology, social capital, financial capital, local government and regional governance are the factors that influence the local performance of local economic development.

1.1.1. Institution. In scientific terms, the term institution is difficult to interpret more deeply because the meaning has various points of view as many social phenomena discuss and are tied to the definition of an institution. [6], many authors consider institutions not only to be constraints on but also enablers of human behavior [6]. The focus point that institutions play a very important role in any society, because they provide the structure of rules and run activities of the organization as a whole. According to North (1990), an institution becomes 'rules of the game', because they set a target and limits regarding the choices of individuals within it. Apart from that, institutions can also determine the opportunities of a society that they have in it.
The definition of an institution and its application in society becomes a major influence because it determines how effective and accurate the implementation of policies in society is. Moreover, it also contribute huge influence on the competitiveness for regional economics. Central-local government relationships also have an important role as a form of responsibility related to the extent to which regional and local economic development (LED) have been applied by the sub-national or sub-state government [8]. Regarding national government, it is hoped that the policies in local communities will be able to apply, but to make it happen, a local strategic group support and synergy from the regional community is needed in terms of negotiation and implementation of policies. Successful negotiations and implementation of these policies depend on the relationship and effectiveness of actions among stakeholders in the business community and several levels of government collaborating with each other.

1.1.2. Natural Resources. [1] Noticed that the distribution of economic power and resources endowments (natural resources) so far is exclusive because they are not available simultaneously in an area. Therefore, nature conservation measures should not only be related to development. [3] Furthermore, it shows that stable economic development cannot be achieved without sacrificing natural resources that will run out and of course become a reference for future generations. [2] has added that sustainability has structural as well as natural limitations, which cannot be eliminated by seeking a compromise. In conclusion, the sustainability of natural resources and development in the economic aspect must be studied further because they are interrelated and have an effect on the future [5].

1.1.3. Infrastructure and Technology. An important aspect related to the arrangement of the LERD program relates to how infrastructure and technology can be made available. Where any availability of local infrastructure is seen as a support and business attraction for a region and also an incentive for companies (Florida, 2002). A "smart" infrastructure is needed in terms of improving business plans for a region, where infrastructure and technology are related with the provision of hard and soft services that can support added value activities, increase collaboration and encourage the main progress, accelerate resources and provide a better quality of life. After that, this role can encourage innovation and better R&D that more going forward in the future, creating a supportive local business climate, also finance and technology field that accelerates business [7]. Furthermore, sustainable economic development for a region can be realized with local resources that have been provided by the government.

1.1.4. Social Capital. The OECD defines social capital as "a system with shared norms, values, and understandings that can facilitate co-operation within or among groups." In other words, social capital means a relationship between individuals and entities that can economically be valuable. It creates a real-world connection between groups or individuals and enables people to collaborate (OECD Insights: Human Capital). Thus we can see social capital from the built network perspective and coordination among all area stakeholders. In the form of LED research, social capital supports increasing returns through leaders, which positively impacts the local business atmosphere.

1.1.5. Financial Capital. The enhancement of LERD can be achieved through financial sources such as entrepreneurial activity and quality. Some of the entrepreneurial activities and qualities such as; (1) informal capital, is a capital from close-relate family, neighbors, and friends [8]; (2) Micro finance institutions, that are institutions with issuing small-scale financial loans aimed to individuals who are on the poverty line, where these loans can be used as initial capital in the process of starting their business; (3) bank loans, which are the main source of capital for entrepreneurs who have plans to increase the scale of their business.
to the next stage and (4) Business angels, individuals who invest a certain amount of money into a business that has a development growth and in the early stages [2].

1.1.6. Local Government and Regional Governance. Local government and regional leaders can govern and make decisions at the local level for local purposes due to Indonesia's decentralization. Decentralization can fulfill the specific need for a region to be identified and provided by the regional or local government [4]. The more resources that a region possesses, furthermore, as a result the better it may perform. An area can still succeed even if they have few or relatively low resource endowments or only a few economic expansion opportunities [1].

According to [8], the decentralized decision-making process in local government is very important, especially for building close relationships between institutions such as government organizations and local businesses. This concept can enhance entrepreneurial ideas and support better innovation for the region. The interactions in it include role of institutions, availability of resources (natural resources, infrastructure, and technology provided by the government, capital and financial aspects), and entrepreneurship which can increase the strong capacity and capability of one region and shape performance especially in local economic scope [2]. but in general, improved performance from that action can only be realized through strong leadership and effective institutions plan that can act as a support for entrepreneurial activity in the region. After that in such conditions, an region can able to mobilize and utilize the wealth of available resources and determine specialization in that location and, at the same time, improve economic performance [7].

![Figure 1. Research Framework.](image)

2. Method
To build the model, primary data was collected through a questionnaire survey approach. The questionnaire was multiple options organized with a Likert scale [8]. A formal questionnaire consists of 7 sections (including first section that contains general and demographic information of the respondents) and 126 questions were developed. Section 2 includes the opinion about natural resources [2]. Section 3 reflects the issue relevant to infrastructure and technology [3]. Section 4 details social capital questions [5]. Section 5 highlights the information about financial capital [4]. Section 6 describes local government and regional governance questions [2]. Section 7 details on the opinion about local performance [1]. Collected response were summarized using data reduction method. All items were tested for reliability and validity first before reduced to the structural variables for hypotheses testing.
2.1. Path Analysis
In order to test the hypotheses, several models are proposed using the path analysis method. The first model is the initial mediation model, without the GES moderation. The purpose of this model is to test all mediation hypotheses, between the nine exogenous variables and the endogenous variables, LCOPER and LGOPER. The second model is the final mediation model, without the GES moderation, and with all non-significant exogenous variables taken out of the model. The purpose of this model is to propose a best fit model that explained the data, without interference of nonsignificant variables. This model is considered more parsimonious while still maintaining explanatory power of the model.

The third model is the initial multigroup model, using multisample path analysis to incorporate GES as moderating variable. The first sample is the unmoderated data, while the second sample is the moderated data generated by multiplying the exogenous variables with the moderating variable, GES. The purpose of the third model is to provide baseline for moderation testing by including all hypotheses, while still assuming no differences between moderated and unmoderated data. The fourth model is the secondary multigroup model, using multisample and assume differences in path coefficients between moderated and unmoderated samples. Moderation hypothesis testing is done by comparing differences between the third and the fourth model. The fifth model is the final moderation model, with all non-significant moderated exogenous variables excluded from the model. Similar to the second model, this model summarized the key variables to Local Economic Resource Development, while incorporating the moderation effect of Government Entrepreneurship Strategy.

3. Results and discussion
The first preliminary analysis conducted is descriptive analysis to obtain a general understanding of the data collected in the survey. Means is used as measure of central tendency, while standard deviation is used as measure of variability. Skewness and Kurtosis is used as measure of normality, in which data with normal distribution must have skewness and kurtosis of between -2.00 and +2.00. Among the nine exogenous variable, Local Government received the highest score from the respondent while Infrastructure received the lowest score of evaluation. On the variability of the data, Financial Capital have the highest variability while Social Capital have the lowest variability. On the normality of the data, since all variable have skewness and kurtosis within the acceptable limit, all variables in the study shows normal data distribution. Full descriptive result is shown in Table 1.

| Code | Variables            | Means | Std. Dev. | M ax. | Min | Skew. | Kurt. |
|------|----------------------|-------|-----------|-------|-----|-------|-------|
| INS  | Institution          | 4.19  | 0.7       | 5.7   | 1.44| 0.36  | -     |
| NAT  | Natural Resources    | 4.23  | 0.7       | 5.7   | 1.50| 0.64  | 0     |
| HUM  | Human Resources      | 4.29  | 0.7       | 5.8   | 2.00| 0.46  | 9     |
| INF  | Infrastructure       | 3.22  | 1.1       | 6.0   | 1.00| 0     | 0     |
| TEC  | Technology           | 3.88  | 0.8       | 6.0   | 1.83| 0     | -     |
| LOC  | Local Govt. Support  | 4.53  | 0.6       | 6.0   | 2.14| 0.34  | 4     |
| SOC  | Social Capital       | 4.32  | 0.5       | 5.9   | 2.10| 0.17  | 9     |
| FIN  | Financial Capital    | 3.98  | 1.1       | 6.0   | 1.00| 0.73  | 0.30  |
| CEN  | Central Govt. Support| 4.34  | 0.7       | 6.0   | 1.00| 0.76  | 2     |

Table 1. Result of descriptive statistics.
The second preliminary analysis is correlation test among variables in the model. Basically, the correlation among the nine exogenous variables must not exceed 0.8 to prevent multicollinearity among predictors. On the other hand, correlation between the nine exogenous variable and the endogenous variable is expected to be significant. The result shows that no potential multicollinearity exist among the nine exogenous variable, since all correlation coefficient among the nine are less than 0.80. However, the analysis found that Natural Resources have poor correlations with all remaining variables.

### Table 2. Correlation matrix.

| Variables | INS  | NAT  | HUM  | INF  | TEC  | LOC  | SOS  | FIN  | CEN  | GE S  | LCO PER | LGOP ER |
|-----------|------|------|------|------|------|------|------|------|------|-------|---------|---------|
| INS       | 1.00 |      |      |      |      |      |      |      |      |       |         |         |
| NAT       | 0.22 | 1.00 |      |      |      |      |      |      |      |       |         |         |
| HUM       | 0.52 | 0.21 | 1.00 |      |      |      |      |      |      |       |         |         |
| INF       | 0.53 | 0.09 | 0.51 | 1.00 |      |      |      |      |      |       |         |         |
| TEC       | 0.42 | 0.20 | 0.50 | 0.4  | 1.00 |      |      |      |      |       |         |         |
| LOC       | 0.34 | 0.11 | 0.34 | 0.0  | 0.56 | 1.00 |      |      |      |       |         |         |
| SOC       | 0.51 | 0.17 | 0.38 | 0.6  | 0.50 | 0.43 | 1.00 |      |      |       |         |         |
| FIN       | 0.29 | 0.01 | 0.34 | 0.2  | 0.45 | 0.55 | 0.41 | 1.0  |      |       |         |         |
| CEN       | 0.37 | 0.14 | 0.31 | 0.8  | 0.39 | 0.33 | 0.35 | 1.0  | 0.0  | 1.0   |         |         |
| GES       | 0.55 | 0.20 | 0.52 | 0.6  | 0.58 | 0.45 | 0.54 | 0.2  | 0.4  | 0.4   | 1.0     | 0.0     |
| LCO PER   | 0.45 | 0.09 | 0.44 | 0.3  | 0.48 | 0.33 | 0.43 | 0.2  | 0.8  | 0.5   | 0.66    | 1.00    |
| LGOPER    | 0.29 | 0.05 | 0.34 | 0.6  | 0.34 | 0.31 | 0.31 | 0.2  | 0.3  | 0.5   | 0.66    | 1.00    |

### 3.1. First model

The initial mediation model yield perfect model fit, with chi-square of 0.00 and RMSEA of 0.00. However, multiple path showed t-value below the required 1.96. This means that the hypothesis represented by that particular path is rejected. Only INS, TEC and CEN are significant to both LCO PER and LGOPER, while HUM is significant to LCO PER only and INF is significant to LGOPER only. NAT, LOC, SOS and FIN are not significant to either endogenous variables. Mediation of LCO PER between the significant exogenous variables and LGOPER is proven significant. Alternatively, although the path between INS and TEC to LGOPER is significant, it is negative. Therefore, higher evaluation of institution and technology support reduces respondent evaluation to performance of Local Government. Summary of t-value and standardized loading factor is shown in Table 2 while path diagram of the initial mediation model is shown in Table 3.
Table 3. T-values and SLF of initial mediation model.

| Variables | LCOPER |  | LGOPER |  |
|-----------|--------|--------|--------|--------|
|           | t-value | SLF   | t-value | SLF   |
| INS       | 1.99    | 0.12  | -2.33   | -0.13  |
| NAT       | -1.33   | -0.06 | -0.39   | -0.02  |
| HUM       | 2.35    | 0.14  | 0.81    | 0.04   |
| INF       | 1.42    | 0.09  | 2.55    | 0.14   |
| TEC       | 2.69    | 0.18  | -2.13   | -0.13  |
| LOC       | 0.09    | 0.01  | 1.49    | 0.08   |
| SOS       | 1.9     | 0.11  | -0.58   | -0.03  |
| FIN       | -0.65   | -0.03 | 1.02    | 0.05   |
| CEN       | 5.45    | 0.28  | 6.16    | 0.3    |
| LCOPER    | n.a.    | n.a.  | 10.20   | 0.53   |

3.2. Second model

The second model is the final mediation model, which yields a chi-square value of 6.11 with a degree-of-freedom of 3.0. Thus the goodness of fit statistics produces a p-value of 0.10648 and RMSEA of 0.059. Thus, the final mediation model can be considered a good fit since both criteria correspond to the minimum requirement of a p-value more significant than 0.05 or RMSEA less than 0.08. This model is also proposed as a best-fit model that better explains the data with a simpler model.

In the final mediation model, there are four exogenous variables with a significant influence on LCOPER. The institution (INS), Human Resources (HUM), Technology Support (TEC), and Central Government Support (CEN) positively influence Local Company Performance. This result is supported by qualitative interview results that highlighted the first three variables as significant determinants for local entrepreneurial strategy (Rokhim et al., 2016). The influence of the exogenous variables on Local Government Performance is mostly mediated by Local Company Performance. Only the CEN show has a significant positive direct and indirect effect on Local Government Performance. INS negatively affects Local Government Performance, lessening its positive indirect effect through Local Company Performance.

Table 4. T-values and SLF of final mediation model.

| Variables | LCOPER |  | LGOPER |  |
|-----------|--------|--------|--------|--------|
|           | t-value | SLF   | t-value | SLF   |
| INS       | 3.16    | 0.17  | -2.33   | -0.12  |
| HUM       | 2.57    | 0.15  | n.a.    | n.a.   |
| INF       | n.a.    | n.a.  | 2.43    | 0.12   |
| TEC       | 4.09    | 0.22  | n.a.    | n.a.   |
| CEN       | 5.59    | 0.28  | 6.16    | 0.29   |
| LCOPER    | n.a.    | n.a.  | 10.54   | 0.52   |

3.3. Third and fourth model

The third model, incorporating GES as a moderating variable but assuming no difference between moderated and unmoderated data, yields a chi-square value of 33.69 with a degree-of-freedom of 21.00. Thus, the goodness of fit statistics produces a p-value of 0.03912 and RMSEA of 0.045. The initial moderation model can be considered a good fit since the RMSEA criteria are still met. Since the p-value of chi-square have a sample size bias toward rejecting the model if the sample size exceeds 100 data, in this case, the p-value requirement can be disregarded. This model is used as a baseline for
determining the moderation hypothesis by comparing the chi-square value and degree-of-freedom with the fourth model.

The fourth model, incorporating GES as a moderating variable but assuming differences between moderated and unmoderated data, yields a chi-square value of 0.31 with a degree-of-freedom of 2.00. Thus the goodness of fit statistics produces a p-value of 0.85830 and RMSEA of 0.000. The secondary moderation model is considered a good fit since both the RMSEA and p-value criterion are met. This model is used as the determinant of the moderation hypothesis by comparing it with the third model. If the difference between the third model (assuming no difference) and the fourth model (assuming differences) is significant, then the third model is rejected, and the moderation hypothesis is accepted. Alternatively, if the difference is not significant, then the fourth model is rejected, and the moderation hypothesis is rejected.

A differential chi-square of 33.38 with a degree-of-freedom of 19.00 is obtained by comparing the third and fourth models. Using the chi-square distribution curve, a probability value of 0.022723 is obtained. Since the p-value of the differential chi-square is less than 0.05 then the difference is considered significant within confidence level of 95%. Thus, the moderation hypothesis of GES is accepted. Government Entrepreneurial Strategy is proven to moderate the nine exogenous variables’ influence to both Local Company Performance and Local Government Performance. The result of the moderation test is shown in Table 5.

Table 5. Moderation hypothesis test.

| Statistics          | Third Model | Fourth Model | Difference |
|---------------------|-------------|--------------|------------|
| Chi-Square          | 33.69       | 0.31         | 33.38      |
| Degree of Freedom   | 21.00       | 2.00         | 19.00      |
| p-values            |             |              | 0.021723   |
| Conclusion          |             |              | Significant|

After the moderation hypothesis is proven significant, the next step is to measure the moderation effect. A moderator may strengthen (positive moderation) or weaken (negative moderation) the relationship between variables in the model. This is measured through the change in the standardized loading factor between unmoderated and moderated data. The result shown in Table XX6 shows that GES strengthened some positive relationships, such as TEC and CEN’s influence on LCOPER. GES also strengthened NAT and FIN’s negative influence on LCOPER and the influence of INS and TEC on LGOPER.

Table 6. Moderation Effect

| Variables | LCOPER | LGOPER |
|-----------|--------|--------|
|           | Unmod  | Mod    | Unmod  | Mod    |
| INS       | 0.12   | 0.13   | -0.13  | -0.19  |
| NAT       | -0.06  | -0.11  | -0.02  | -0.10  |
| HUM       | 0.14   | 0.14   | 0.04   | 0.12   |
| 0.53      | 0.48   | 0.07   | 0.14   | 0.14   |
| TEC       | 0.18   | 0.25   | -0.13  | -0.24  |
| LOC       | 0.01   | -0.05  | 0.08   | 0.05   |
| SOS       | 0.11   | 0.06   | -0.03  | -0.06  |
| FIN       | -0.03  | -0.24  | 0.05   | 0.03   |
| CEN       | 0.28   | 0.40   | 0.30   | 0.48   |
3.4. Fifth model
With all non-significant moderated hypotheses excluded from the model, the final moderation model yields a chi-square value of 7.44 with a degree of freedom of 6.00. Thus the goodness of fit statistics produces a p-value of 0.28171 and RMSEA of 0.028. The final moderation model is considered a good fit since both the RMSEA and p-value criterion are met. This model summarized the critical variables to Local Economic Resource Development while incorporating the Government Entrepreneurship Strategy's moderation effect. Although not significant in the unmoderated data, the main difference is that FIN has a significant negative influence on LCOPER in the moderated data. The positive influence of INS, TEC, and CEN to LCOPER is strengthened while INS and TEC's negative influence on LGOPER is also strengthened. The changes in the Standardized Loading Factor in the final moderation is shown in Table 7.

Table 7. Moderation Effect to SLF in the final moderation model.

| Variables | LCOPER | LGOPER |
|-----------|--------|--------|
|           | Unmod  | Mod    | Unmod  | Mod    |
| INS       | 0.13   | 0.17   | -0.13  | -0.19  |
| HUM       | 0.14   | 0.14   | 0.04   | 0.11   |
| INF       | n.a.   | n.a.   | 0.14   | 0.14   |
| TEC       | 0.18   | 0.25   | -0.13  | -0.24  |
| FIN       | -0.03  | -0.24  | n.a.   | n.a.   |
| CEN       | 0.28   | 0.40   | 0.30   | 0.48   |
| LCOPER    | n.a.   | n.a.   | 0.53   | 0.48   |

4. Conclusion
This study aimed to present variables that influence local economic development in several regions in Indonesia. With this in mind, a new model approach was adapted from the already well established local economic development model. The survey results showed the critical variables to Local Economic Resource Development while incorporating the Government Entrepreneurship Strategy's moderation effect. Although not significant in the unmoderated data, the main difference is that financial capital has a significant negative influence on local company performance in the moderated data. The positive influence of institutions, technology, and central government support to local company performance is strengthened. At the same time, the negative influence of institutions and technology on local government performance is also strengthened.

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