

3 A policy framework to respond to demographic changes in Korea

This chapter presents relevant policies and practices adopted by selected OECD countries and defines a policy framework with development priorities and measures to tackle socio-economic challenges caused by demographic changes in Korea.

Introduction

Korea now faces a major adjustment as it deals with the twin challenges of demographic decline and adapting to rapid technological change. While the adjustment will affect all parts of the country, the focus of this discussion is on the rural parts of Korea, where people mainly live in small settlements and minor cities. Two policy choices for rural areas are considered here.

The first is to allow a large part of the adjustment to take place in rural regions by adopting policies that reinforce current economic and demographic trends. These include: maintaining the flow of young people from rural to urban places, continuing to allow rural communities to lag behind in adopting technological change, allowing lower quality rural public services to continue in place and generally focusing public policy on fostering urban growth. The result of this policy will be a further reduction in the share of the Korean population living in rural areas and the abandonment of many small settlements when they decline in population and economic function to the point that residents abandon the community. For the nation this will lead to a process of desertification where previously settled areas revert to a natural state.

Alternatively, Korea could choose to try to maintain most of its territory in a settled state by improving economic opportunities and living conditions in rural places; thereby slowing the outflow of rural youth to urban centres and possibly encouraging a flow of people from cities to rural Korea. This second approach preserves the territorial integrity of the country, but will require major adjustments in public policy. Notably, it will require stimulating local economic development to provide attractive career opportunities. Because of the small size of local labour markets in rural areas these efforts will have focus on small and medium size enterprises, and many of these firms will not be competitive in international markets. Further, to ensure that the quality of life in rural areas is comparable to that in cities, there will have to be major improvements in rural public and private services. These investments will be challenged by the rural realities of limited potential for economies of scale and high transportation costs. This means that alternative service delivery mechanisms will have to be developed. Because worker productivity in Korea is currently lower in SMEs and in service-oriented firms it will be important to invest in ways to increase their productivity in order to make rural income competitive with urban income, and to help them offset the broader reduction in the size of the national work force.

Either policy choice also has implications for urban centres. For decades large cities in Korea have benefitted from rural to urban migration as a significant contributor to their labour markets. With demographic decline this inflow of workers will slow, but it will likely slow more if government policy increases opportunities in rural areas as part of a strategy to maintain a populated countryside and decrease congestion in large cities. Even with maintained flows of rural youth in percentage terms, the number of rural in-migrants will decline as the rural population declines. Other factors may also slow rural outmigration as the population ages. To the extent that rural communities retain a more traditional set of social relations, there may be increased pressure on young people to remain near their home in order to help care for elderly relatives. Elderly care is more likely to remain a family responsibility in rural areas because small settlements will be unable to provide public or private elderly housing.

Deciding on a broad approach to how spatial impacts of demographic decline will be addressed is important because it will affect the value of existing efforts to improve rural conditions. For example, the current program to rehabilitate rural housing makes more sense if it is part of a broader strategy to maintain a balanced distribution of the population. But even if this the case, it is unlikely that all rural communities with substandard housing will be viable in the long run. To some extent if communities self-select participation in the program there will be a tendency for the better-organised and more viable places to apply. However, self-selection may not achieve a spatial distribution of surviving communities that meets national needs, so more context may be needed for existing rural programs to make them more coherent with national objectives.

The Korean context

Korea has made rapid economic and social progress over the last fifty years. Much of the progress reflects a sound development strategy that has turned Korea into a global leader in manufacturing. Large Korean firms are dominant in important sectors, such as, batteries, telecommunications, automobiles, ship construction and electronics. Korea's dominant export-oriented manufacturing firms were able to combine a high rate of technological progress with abundant relatively low cost but skilled workers to penetrate world markets. Policies followed by the Korean government supported the growth of these chaebols including financial support and favourable labour and environmental regulations.

A consequence of this growth was an increasing concentration of the population and economic activity in cities. This has led to most regions in Korea being urban in nature, and a decline in the both the number of rural regions and the rural share of the population. However, while rural regions in Korea are few in number, they now produce a higher per capita income than do urban regions (Chapter on Demographic trends in the OECD and Korea). This suggests that there are economic opportunities in rural Korea that can be leveraged for future growth. The rural population in Korea also tends to reside relatively close to a medium size or large city, and there are no remote rural regions. As a result, a large share of the rural population lives in what can be considered a peri-urban environment. This provides the potential to form stronger rural-urban linkages that can be a way to improve the quality of life in both urban and rural locations (OECD, 2021^[1]).

However economic progress has not been uniformly distributed. Three aspects are relevant to the inequality. The first is a significant small firm versus large firm difference in productivity and profitability. The second is the concentration of growth in the manufacturing sector, with services playing a far more limited role. The third is a geographic concentration of prosperity in the largest cities that continue to attract workers from other parts of the country, particularly rural areas. The result is a classic case of unbalanced growth.

During the post-war period Korea experienced a demographic dividend of a rapidly growing labour force that also underwent a major increase in skills (Han and Lee, 2019^[2]). The demographic dividend fuelled the economic transformation by providing a growing number of workers whose skill level improved with each new generation. Many of these workers came to cities from rural regions at a time when rural fertility rates were high, and employment prospects and living conditions in cities were better than in rural communities.

The Korean government is already embarking on a series of policy adjustments to bring about more balanced growth. However, Korea now faces a major new challenge that both makes strengthening and broadening growth more important, and that imposes new constraints on this effort. Korea has already moved from a favourable demographic structure, where new workers were more numerous and better skilled than older retiring workers, to one where the new worker replacement ratio is below one, resulting in a shrinking work force. While workforce skills continue to increase, the rate of improvement from generation to generation is slowing. And, while urban areas are still forecast to grow they will be less able to rely on an incoming flow of workers from rural areas, because persistent outmigration has led to a large decline in the number of women of child-bearing age, and fertility rates of women in rural areas are now comparable to those in cities.

With a less favourable demographic situation a number of common practices and behaviours will need examination to see if they should remain common. Examples are: relatively long working hours, pressure on older workers in large companies to retire at a relatively early age, a pattern of young workers remaining out of the labour force while they search for jobs in large firms or government, a high rate of entrepreneurship by older individuals that can be characterised as being driven by necessity and not opportunity, low service sector productivity and low rates of female employment. These practices and

behaviours tend to reduce labour force participation rates or result in under-employment, which in turn limits productivity.

In its early decades of growth, Korea placed limited emphasis on rural development, with the notable exceptions of the land reform program of the 1950s under President Syngman Rhee, and in the 1970s the Saemul Undong program of President Park Chong-hee that provided support for village modernisation and economic diversification in addition to agricultural support (Looney, 2012^[3]) (Whang, 1980^[4]). More recently, Korea introduced a major multi-year effort to revitalise rural areas and improve living conditions with the Comprehensive Rural Village Development Program (Box 2.10) that operated from 2004 to 2017 (Hwang, Park and Lee, 2018^[5]).

For most of the last fifty years Korea relied upon an unbalanced growth strategy that supported a relatively small number of globally competitive manufacturing firms concentrated in a few cities, particularly Seoul. Most recently Korea has embarked on a balanced growth approach that seeks to reduce the share of the population in Seoul by fostering the development of a number of new cities, and a broadening of the economy. The new strategy, Innovation Cities has the goal of fostering a shift in population and economic activity away from the Seoul metropolitan region to 10 existing regional cities and a new administrative city, Sejong (OECD, 2021^[1]). Spreading population and economic activity to cities distributed across the country will relieve pressure on the Seoul region and lead to an improved geographic balance. And, while the policy is mainly an urban development approach, it should provide spill-over benefits to rural territory near these new growth poles.

However, the policy, as currently conceived does not explicitly identify rural development as a contributor to balanced growth. Certainly, increasing the number of dynamic urban regions and spreading them across more of the national territory provides greater opportunity for rural people to access urban services and employment opportunities, but this is not the same as strengthening rural development. Without more support for rural development it may be possible to create a more balanced urban system, but ongoing population and economic decline in rural areas is likely to continue.

Few regions in Korea are characterised as predominantly rural, 5 out of 17 regions. This may suggest that rural issues are not very important for Korea. However approximately 18% of the Korean population live in a rural environment because all types of region contain both urban and rural territory and populations (Chapter on Demographic trends in the OECD and Korea). Most of these people live in fairly close proximity to a city, with a median travel time of less than half an hour. This makes constructing opportunities for strengthening rural urban linkages a potentially important way to improve rural well-being. Close geographic proximity allows the possibility of rural people accessing services from nearby urban centres and perhaps finding work in these urban places if commuting is possible. Similarly, rural areas can benefit from urban people purchasing local goods, such as farm products, or from urban families travelling to rural areas for leisure activities. While these linkages can develop independently of national government support, they are more likely to lead to a stronger rural economy if they are explicitly encouraged (OECD, 2021^[1]).

As noted in the chapter on Demographic trends in the OECD and Korea the quality of life of rural people in Korea is often inferior to that of urban Koreans. This includes: access to reasonable quality housing, availability of public services, quality of education, access to transportation, and, in some places, environmental quality. If rural regions are to continue to make a positive contribution to national development it will be important to ensure that rural areas are desirable places for workers to live. Assuring Inclusive growth across Korea can be framed in terms of: ensuring work and skills, and opportunities to start and grow businesses (OECD, 2021^[6]). And these are certainly the key factors influencing productivity and production. However, in an environment where the labour force is shrinking and places must compete for workers, it is important to ensure that some places are not disadvantaged because they are currently unable to offer an adequate quality of life.

Korea now must decide how its rural policy will support general development objectives in this new period of demographic decline. It is clear that some rural places will not survive, because the national population is falling and there will be a significant geographic rebalancing of people. However, the number and geographic distribution of surviving rural communities will hinge on policy choices by the government on where investments in increasing productivity and providing public services will occur. Choices that assign a priority to favour factors that encourage the permanence of a significant share of the population across rural regions will reduce desertification and may meet national security objectives, but will require the implementation of a range of policies that focus on improving rural conditions. Conversely, a policy regime that is mainly urban focused will inevitably lead to higher rate of rural decline.

Lessons and suggestions for Korea

Defining a rural strategy for Korea

Korea has undertaken a highly successful national development strategy over the past fifty years that has made it a prosperous country. Historically much of Korea's growth was driven by investments to support export-oriented manufacturing. This was clearly successful, but it has resulted in rapid urbanisation of the population as rural residents migrated to cities for better jobs, and significant rural decline. Korea has become a major manufacturing power and is a global leader in electronics, automobile and ship-building. In the process the economy and Korean society have become highly urbanised with Seoul becoming the dominant city. Currently the Korean government is engaged in efforts to spread economic activity and the population outside Seoul to create more spatially balanced growth and reduce increasing congestion costs in the capital city. Much of this effort involves creating a network of secondary cities. While Korea has a clear urban strategy it currently lacks a parallel rural strategy that could add to the current focus on achieving more balanced growth and increased prosperity for all citizens wherever they live.

OECD countries are affected by demographic change in different ways. Mainly due to ageing, immigration and falling fertility rates, many cities and regions in the OECD are likely to continue to “shrink” in the coming decades, even with some increases in population due to migration (from within or outside the country). There is a need for new thinking and policies to overcome some of the expected challenges ahead (e.g. ensure financing of services that are likely to see increased demand with the growth of the ageing population; balance employment opportunities for the youth and the elderly; innovate the management of urban infrastructure). The silver economy (referring to the elderly workforce) and the white economy (referring to the economic opportunities of healthcare) could be new sources of growth together with opportunities from green economy activities, but there is a need to create an enabling environment by providing appropriate support to local governments and business. At the same time, national and local governments are already working to address the ageing workforce, which is a priority issue, and a number of programmes and initiatives are in place (Martinez-Fernandez et al., 2012^[7]).

Other OECD nations have recognised that it is important to move beyond just trying to reverse demographic decline in rural areas to finding ways to adapt to and manage the decline process. For example, in the Netherlands, population and households are projected to decrease rapidly in the near future. The decrease in the number of youths and the ageing population will also cause a rapid decrease in the size of the potential labour force. In 2010, the Dutch Government identified a strategy called “anticipating regions” for facing population shrinkage. Regions and municipalities had to anticipate the effects of demographic decline and adapt housing policies but also define new policies for the local economy, retail trade, business locations and the labour market. In fact, the experiences in shrinking regions show that there is little use trying to combat demographic decline and that a policy shift from combating shrinkage to managing, shrinkage is more effective, even if it is a difficult process. To do so municipalities need to work together at the regional level to ensure that they do not compete for the same residents and businesses. This also helps preventing unprofitable spatial investments, financial problems

and unoccupied homes and offices. Regional and national government shall support municipalities in their search for new coalitions, in developing financial resources and in exploring the possibilities provided by existing regulations to implement common strategies that focus on anticipating and managing shrinkage. Main takeaways from evaluations of policies to manage shrinkage include: 1) Approach demographic challenges in an integrated way and adopting a long-term perspective. 2) Develop adapted financial instruments to facilitate long-term intergovernmental co-operation. 3) Make sure the right preconditions are in place to realise the opportunities in shrinkage areas and take away any obstacles in regulation that prevent regional-specific efforts and approaches. 4) Sharing experiences, expertise and knowledge between regions. 5) Make sure regions and municipalities have enough resources to maintain the basic social infrastructure to which everyone has a right. Make sure there is some flexibility in funding since this infrastructure might cost more in shrinkage areas than elsewhere (Verwest and Van Dam, 2010^[8]).

Italy's "inner areas", rural areas that are found to be exceptionally remote from urban centres and to face specific infrastructure and service-delivery challenges, cover almost 60% of the national territory, hosting nearly 23% of the national population and encompassing approximately 53% of Italy's municipalities. Inner areas are characterised by: distance from large and medium-sized urban centres; a wealth of natural assets and cultural resources; and a complex settlement pattern shaped by diverse natural phenomena and human settlement processes. In aggregate, these areas are experiencing population ageing and decline, loss of jobs and shrinking public and private service supply. Their decline in many cases has hydro-geological consequences and entails loss of cultural heritage and landscape degradation. A National Strategy for Inner Areas development has recently been developed with a view to promoting the recovery of such areas on the basis of a set of interconnected projects focused on few selected priority fields of intervention and co-ordinated with ordinary sectoral policies (service provision). The strategy seeks to enhance well-being and quality of life in Inner Areas by turning differences into competitive strengths, overcoming differences, interconnecting locations, and strengthening networks. The Strategy pursues two complementary objectives: i) improving Inner Areas populations' capability to have access to essential services (education, health, transport); and ii) promoting Inner Areas' development by capitalising on local assets and stimulating job opportunities. The ultimate goal of the Strategy lies in reinforcing Inner Areas' demographic structure. Five major innovations differentiate the strategy from previous efforts in this field: 1) Though it is a national strategy, it is based on partnership across levels of government and a strongly participatory approach to local development. It neither forces local actors to conceive new development measures themselves nor plans them from the capital. 2) It has two clear aims of accessibility and promoting development, and the central government's approach to these two goals is differentiated. For accessibility, it is a supply-focused policy rationalised by sustaining their quality of life. For promoting development, it is a support-giving function to promote local initiatives in selected domains. 3) The framework to promote development is well-conceived. It is a step-by-step process, enabling the government to minimise the risks of pouring resources into undesirable areas and to maximise the benefits expanding others. One prototype area per region is selected to evaluate the potential success of the Strategy and trigger a positive learning mechanism. All the selected areas come to be part of a project federation to encourage networking, exchange and learning. 4) The process for selecting prototype areas is very transparent. Meetings, datasets, results and reports are published on line. 5) The sustainability of Strategy actions is ensured by a bottom-up approach in which municipalities and regions are directly responsible for Strategy implementation. Municipal associations are utilised in Italy as a platform for collaborative work. (Source: Information provided directly by the Department for Development and Economic Cohesion of the Italian Republic). (OECD, 2016^[9]).

Similarly, Japan has introduced two new strategies that provide a context for developing a range of policies to address demographic decline. The Long-term Vision and the Comprehensive Strategy for Overcoming the Population Decline and Vitalizing Local Economy were both approved by the Cabinet in December 2014. The "Long Term Vision" is Japan's vision to alleviate the rapid population decline and vitalise the regional economy for 2060. The primary perspectives are: 1) Ease the overconcentration in Greater Tokyo Area; 2) Support young generation's hope for work, marriage, and parenthood; 3) Solve the regional

challenges based on the specific characteristics of each region. The “Comprehensive Strategy” is Japan’s basic policy principles and its implementation for the coming five years. The objectives are: 1) “Generate stable employment in regional areas,” 2) “Create a new inflow of people to regional areas,” 3) “Fulfil the hopes of the young generation for marriage, childbirth, and parenthood,” 4) “Create regional areas suited to the times, preserve safe and secure living, and promote co-operation between regions.” The Government and local governments co-operate in pursuing solving issues by: 1) creating “Regional Economy Data Analysis System” to provide local governments with big data to analyse various indicators, including demographics, business activities, and tourism trends in each region; 2) financial support (grant for local governments, local allocation tax, and tax incentives for businesses) for creating the “Regional Comprehensive Strategy” in each region and its implementation; 3) Human support by assigning government officials and the other experts to assist the chiefs of smaller cities, as well as providing local governments with consultant service by government officials. The “Long Term Vision” is revised every five years, and the “Comprehensive Strategy” is revised every year. In December 2020, “Comprehensive Strategy” was amended, which included the measures for avoiding spreading the pandemic, such as promoting Digital Transformation and decarbonisation society, promoting teleworking, creating attractive universities and industries in regions, and increasing the number of people who move or visit regional areas frequently. The “Basic Policy for Overcoming the Population Decline and Vitalizing Local Economy in Japan” contains detailed policies to achieve the principles in the “Comprehensive Strategy (OECD, 2016^[9]).

In recent years, Korean governments have recognised the need to invest in rural areas. Several factors are important.

- The first is a recognition that unbalanced growth policies have left rural people worse off than their urban pers. When it was important to induce rural to urban migration flows this may have been considered acceptable. But now there is less need for more people in the large urban centres, and many rural people now lack the skills demanded by urban employers as they transition to more advanced production methods.
- Second, Korea has reached a point where the returns from further investments in strengthening large export focused manufacturing firms in urban areas are starting to decline. Consequently, future economic growth will require contributions from other parts of the economy and from other parts of the country, including rural areas.
- Third, demographic decline has started to impact the labour force with retirements exceeding new entrants. In this environment it is crucial to increase labour force participation rates and to ensure that workers are not “underemployed”. In rural areas there are lower labour force participation rates, especially by females and the productivity rates of rural firms are considerably lower than those in urban places.

The OECD has shown that rural areas can make effective contributions to national economic objectives but they need particular types of support that are tailored to their situation and capabilities, which differ considerably from large urban regions (OECD, 2016^[10]). In particular, economic growth and sustainability in rural areas hinges on the development of tradable sectors that sell their production, whether goods or services, outside the local economy. In the past rural areas tended to specialise in the production of natural resources, including agriculture, fishing, forestry and mining. First stage processing of these resources developed and this introduced manufacturing. Over time, some rural regions have been able to expand beyond first stage processing of resources by expanding the variety of manufactured goods they produce. More recently, many rural areas have become specialised in providing tourist activities that are based on nature of local cultural attributes. In addition, some rural regions have been able to act as retirement destinations for urban residents who relocate to enjoy a quieter lifestyle in a pleasant surrounding. Finally, modern ICT has allowed some services to be able to locate to rural areas, including call centres and various “back-office” functions that do not involve close interaction with customers.

While the service sector, broadly defined, employs more people in rural regions, just as it does in urban regions, most service-sector jobs support the local economy but do not generate any revenue from external sales. Because they lack a large home market, due to a small population, rural areas have to purchase many of the goods and service that are required locally from outside their region. This in turn requires that they sell sufficient locally produced outside the region to pay for their imports. Ultimately, a sustainable rural economy requires a strong core of export-oriented firms that form the base of the economy. On this basis, it will be possible to develop a fabric of firms and local government services that create an improved quality of life. But absent the base, the fabric will dissolve as the externally generated funds needed to support it disappear.

Box 3.1. The OECD Rural well-being framework

The new OECD rural policy framework introduced in the publication *Rural Well-being: Geography of Opportunities* provides a structure for suggesting policy recommendations that address the impacts of demographic decline in rural areas of Korea. The focus on well-being recognises that there is more to rural development than improving income and employment, and that the quality of life in a place or region is increasingly important to residents, employers and workers. Moreover, if local economies are to move beyond relying on their specific natural resource endowment as a source of economic growth, then they have to provide a high quality of life to both new employers and workers if they are to attract them. Because these new development opportunities have multiple location choices, it will be the regions or communities that offers the best package of labour force, infrastructure, environmental and cultural amenities, and public and private services that are most likely to grow. In particular, in an environment of demographic decline when all regions will be competing for a smaller labour supply, a focus on enhancing the local quality of life will offer a competitive advantage in attracting and retaining workers.

The Rural Well-being report identifies demographic decline as one of the main factors affecting rural regions of the OECD. The discussion in the report suggests that populations are projected to decline in all rural regions of OECD countries. This reflects varying combinations of: low fertility rates that reduce the number of child births by each woman; high youth outmigration rates, especially for young women; low inward migration rates, except in some regions with high amenities and good public services; mortality rates that continue to decline. While life expectancies continue to increase in most rural regions, which slows population decline this is contributing to a smaller a share of the population being in the active labour force and higher demands for workers in elderly care.

While virtually all OECD countries are now either experiencing demographic decline, or will soon do so, some, such as Korea, Japan, Germany and Italy, are far more exposed to an aging and shrinking population. This makes it imperative to examine how: a shrinking workforce, a smaller school age population and a larger number of retired individuals affect economic and social policies. Rural Well-being identifies a roadmap for improving the various dimensions of quality of life in rural regions.

In many rural regions the effects of demographic decline have been accompanied by slower economic growth in the time period since the recession of 2008-2009. This is especially the case in more remote regions that are distant from a major urban agglomeration. In general, rural regions have been less able to adapt to new economic conditions that reflect a shift to a service economy, particularly high value-added services, and greater use of digital technologies in all parts of the economy. As a result, productivity in most rural regions has not kept up with increases in urban areas; and some remote rural regions have experienced both declining employment and declining productivity. Broad strategies for improving economic prospects and quality of life include: improving skills, particularly digital skills, better broadband access, strengthening the education system, improving entrepreneurship and innovation

performance. For rural areas investments that accommodate and support higher rates of automation and digitalisation will be crucial.

Source: (OECD, 2020^[11]), Rural well-being: Geography of Opportunity, OECD 2020.

Box 3.2. Rural development policy: the European Union model

The Common Agricultural Policy (CAP) is a system of European Union (EU) subsidies and programmes meant to enable producers of all forms of food to survive and remain competitive on world markets. The key objectives of the CAP are to: increase agricultural productivity; ensure a fair standard of living for agricultural producers; stabilise markets; assure availability of supplies; and ensure reasonable prices to consumers. The Union's rural development policy emerged in a piecemeal way through successive reforms of the CAP. Consequently, there are now two "pillars" through which funding is disbursed. Pillar I, the larger share of the overall budget, provides subsidies to farmers. The second pillar is the Rural Development Regulation. The CAP has evolved in ways that make it more important for broader rural development issues and EU countries can now use the flexibility in the CAP to shift money from direct payments for commodities to other programme areas. Early opportunities for modulation* of direct payments were implemented by the United Kingdom and France at the turn of the 21st century. These were largely for agri-environmental improvements, but they tended to be most valuable in marginal farming areas where additional farm income plays a relatively larger role in the local economy. The expansion of Pillar II makes the CAP an increasingly important factor in rural policy. With the introduction of Pillar II to the CAP in 1999 it began to play a major role in rural development policy within the European Union. As funds are diverted from Pillar I to Pillar II and programmes under Pillar II become more structured and better funded, they play larger roles in conditioning national rural policies. Because Pillar II remains highly oriented to agriculture it promotes a stronger role for farming in rural development. Funding is made available for farm diversification, agri-environmental improvement, farmer training and improving infrastructure that has direct ties to agriculture, such as modernising farm market towns. The broadest aspect of Pillar II is its support for the LEADER programme (Box 3.17), which offers opportunities for introducing locally based rural development approaches that rely on a wide variety of sectors and actors.

Note: * The term "modulation" is used to describe the transfer of funds from direct subsidy payments under Pillar I of the CAP to rural development expenditure under Pillar II of the CAP. It is a mechanism used to shift financial resources across otherwise separate budget lines.

Source: (OECD, 2011^[12]). (OECD, 2016^[9]).

Tailoring labour force policies to support rural development

Policies may affect the consequences of decline in regions and rural areas in one of three ways.

- The first are supply side policies that try to increase the number of potential workers, either through increasing birth rates or through encouraging in-migration. Inward migration is also a challenge for most nations, and while internal migration within a country can improve population numbers in some regions, it will reduce them in others.
- Second, policies to enhance the utilisation of the current labour force largely by increasing participation rates or slowing the rate of retirement can be introduced. These can be effective, but there are limits to their use since they tend to be less effective each time they are used. It may be

possible to increase the workforce participation rate by a few percentage points, but it becomes much more difficult to subsequently entice those with stronger reasons for not participating. Similarly, the youngest cohort of older workers may be easily encouraged to work longer, but it is more difficult to entice people in their late 60s to continue to work.

- The third, and most effective way to adapt to a shrinking workforce is to enhance worker skills and substitute capital and technology for workers as they become scarce. This has the additional benefit of increasing worker wages because this approach enhances labour productivity, which should increase wages. Improved workforce training is a key part of this but it is clear that skill development has to be tightly coupled to employer needs, which will vary by industry and often by size of firm if they are to be effective. It also suggests that the effects of demographic decline by industry must be examined and effective ways to adjust to this decline must be identified. Only then can appropriate workforce development programs be identified.

Of these policies, very few – increasing fertility rates and increasing immigration, attempt to directly reverse demographic decline. All the rest can be characterised as efforts to mitigate the effects of decline, by altering how labour markets function, how and how governments deliver workforce development programs.

Labour force development is best understood in the context of Active Labour Market Policy (ALMP), which focuses on the supply of labour, the demand for labour and ways to make labour markets function more effectively. On the supply side three policy areas are discussed: retaining a larger share of rural youth, increasing the labour force participation rate of those with low current rates and improving rates on migration to rural areas. Labour demand is mainly discussed in the three subsequent sections covering agriculture, tourism and manufacturing. In addition, the importance of raising the effective supply of labour by improving workforce skills is considered in a rural context.

Supply side policy responses

Policies that significantly expand the number of workers have been difficult to implement in OECD countries. The main driver of national population decline has been a large drop in female fertility rates that took place over several generations. This largely reflects differences in lifestyle choices by families that would be difficult to reverse. For family size to increase major changes in support for women is required. While families can play a role in this process national governments will have to provide far better support for working women than is now available in all but a few OECD countries. This includes: extended paid time off for new mothers and fathers, high quality subsidised day care, access to after school care that is close to places of work and flexibility in working hours to deal with family emergencies. Countries that provide these family friendly policies tend to have significantly higher fertility rates than do countries where these accommodations are not widely available.

While these policies offer only a long-term opportunity to influence fertility rates they can have a significant short-term effect in countries and regions where female labour force participation rates are low. For women to be willing, or able, to take on paid work they must have a way to transfer a significant portion of their household responsibilities for family care to their partner or another provider. In the past this may have been a member of the extended family. However, in modern society it is less common to have relatives living in close proximity, which means that a formal institution, such as a licensed day care facility or a similar entity that provides after school care is required. Cost, quality of care provided and ease of access are all important factors that will influence a woman's willingness to take on formal employment. If countries see higher female participation rates as a way to deal with imminent workforce shortages this may be an additional reason to support programs that also provide long term increases in fertility rates even these may not affect the work force for decades.

Korea has recognised that fertility rates in Seoul and in other high cost, congested, large cities are lower than in the rest of the country. In part this may reflect a self-selection process where individuals less interested in having children concentrate in urban centres or live in cities for the part of their lives when

they do not have children. However, it may also be a response to the high cost of housing, the resulting small living spaces for most households and difficulty in affording care for children without both parents working. Current efforts by the Korean government to provide family friendly environments in secondary cities are an appropriate response to this problem and appear to be successful (Economist, 2020^[13]). To the extent that rural locations offer a contrasting situation to large cities – affordable housing less stress, lower cost of living, perhaps more nearby relatives, efforts to stimulate young households to move to rural communities might have a positive impact on fertility rates. However, it will be important to provide similar forms of support for young mothers. Otherwise, the number of relocations may be small, or relocating families may decide to reduce their degree of participation in the formal labour force to manage the time obligations of childcare.

Box 3.3. The Masuda Report (Japan)

In the midst of Japan's demographic transition, and in light of previous policies' perceived inadequacies, the Japan Policy Council (JPC) in May 2014 published a study entitled "Stop Declining Birth Rates: The Local Revitalisation Strategy", which sought to galvanise debate and policy making on the intersection between ageing and the economy. The report is often referred to as the "Masuda Report," after JPC chairman Hiroya Masuda. The report attracted widespread public attention with its stark warning that 896 local governments – roughly half the total - risked "extinction" by 2040 through further declines in their populations of young women. It argues that the best response to regional decline would be a strategy of building "regional cities attractive to young people," by forging a "new structure of agglomeration" and a "choose and focus" strategy of investment. The report emphasises the need to make these regional cities into the nodes of networks that function to "dam" the flow of younger people into the largest cities. This approach is consistent with some recent government initiatives, particularly those of the Ministry of Internal Affairs and Communications (MIC), which Mr Masuda previously headed. The "autonomous settlement region," which the MIC inaugurated in 2008, is anchored on "core" regional cities of at least 40 000 residents, building on transport, information and communication technologies (ICT) and other networks to link them with surrounding towns and villages and rationalise the region's distribution of health, education, and other services. As of February 2015, there were 85 of these regions. The programme is financed with special incentive measures in the special "Local Allocation Tax" (LAT) (ordinarily used for emergencies). From fiscal year 2014, these incentives were increased to JPY 85 million for the core city and JPY 15 million for each area community (Ministry of Internal Affairs and Communications, 2015). The Masuda Report was presented to the Council on Economic and Fiscal Policy, the Industrial Competitiveness Council and other ranking policy-making organs. Its warnings and recommendations, and subsequent interventions by the JPC, have become important sources of inputs into, and showcases for discussion of, the revitalisation strategy. The report and the follow-up to it have been important in provoking discussion across Japan, as well as in focusing attention on the need to overcome sectoral policy approaches in favour of more integrated strategies for adapting to demographic decline.

Source: (OECD, 2016^[9]), OECD Territorial Reviews: Japan 2016.

Policies to retain young people in rural areas

In rural areas of the OECD there is typically a high rate of youth outmigration from rural communities. When fertility rates were high this reflected the pull of better jobs in urban places and a push that came from an insufficient number of jobs for young people in rural regions. Surplus labour in rural regions can lead to wage stagnation and inferior working conditions, since employers believe they can always find replacement workers. This situation, in turn increases both outmigration and lower rates of labour force participation.

Youth outmigration, especially by young females, increases the rate of population decline. Such migration may be rational for the individual, and it is clearly positive for the cities receiving these people; but it is a problem for the rural community and it can be unclear whether it is beneficial for the nation. Korea's effort to encourage a reverse flow of people from cities to rural regions suggests that the social costs of rural depopulation when combined with the costs of urban congestion are too high.

With the number of new entrants into the workforce falling below the number of people leaving, it is important to increase youth participation rates and to ensure that young workers achieve their full potential in terms of productivity. In the past youth outmigration from rural regions achieved these two objectives. Young people left a region where their employment prospects were limited due to a scarcity of jobs, and in urban areas young migrants from rural Korea found work that made better use of their skills, which increased their productivity. This remains true today and will only change if the nature of employment in rural regions changes to make it less advantageous for youth to leave. Whether this happens will depend on the response of rural employers to the increasing shortage of workers.

Productivity in rural areas of Korea lags behind levels in urban areas (OECD, 2018^[14]). In part this reflects differences in the industrial mix, but it also reflects differences in production technology. Rural firms continue to rely on production techniques that are based on low cost labour and high-cost capital. In urban areas large Korean firms are substituting relatively low-cost technology for increasingly costly workers. One consequence of this is a strong incentive for rural youth who already possess a high job skill, or who have the aptitude to acquire high job skills to leave. The resulting "brain drain" from rural regions may be more important than the number of people who leave for rural development. Rural employers face a smaller and less skilled work force as a result. The small number of workers precludes continuing to rely on labour intensive production technology, but the low skill potential of much of the remaining rural youth limits the opportunity to shift to more capital-intensive production techniques that would increase productivity and wages. With no change, a large share of rural firms will eventually fail, either due to an insufficient number of workers, or by falling so far behind in terms of cost and quality that they lose market share.

If Korea is to achieve its objective of more balanced growth while adapting to demographic decline, it will be important to ensure that employment opportunities in rural areas offer comparable standards of living to those in urban areas. This does not mean that wages will have to be equal, or that all careers are available in the two types of geography. It does require that quality of life measured over multiple dimensions be fairly similar, including employment satisfaction. For some rural youth leaving for urban opportunities will still be preferred. Others may choose to stay if a better mix of local skill development and better career prospects is available. Further, if a broader range of employment opportunities in rural areas can be developed the government objective of having residents of urban places relocate to rural communities may be more achievable.

Box 3.4. Regional strategies to retain youth and talents

A study presented at the SEDEC Commission of the European Committee of the Regions in November 2018 has offered insights on how regions could boost their attractiveness to retain or get back young, skilled people. Brain drain is a problem affecting many regions across Europe. There is a high correlation between the socio-economic conditions of a territory and its brain drain/gain dynamic. Structural migration inflows, especially of young highly skilled individuals, usually occur in regions that have a comparative advantage and play a dynamic role in competing for international talents.

Ad-hoc policies or measures implemented locally or regionally to retain, attract, or regain a highly educated workforce can be effective. Recommendations include:

A first recommendation is that local and regional authorities (LRAs) in sending regions to become aware of the brain drain problem. LRAs should also identify the talent they want/need to retain, attract or regain. Establishing a dialogue with the talent in question appears to be essential. This is especially true for young talent.

A second recommendation relates to the need for the co-ordination of players and the synergy of resources to focus on talent-based growth strategies. These circumstances both occur, for example, when a Smart Specialisation Strategy exists. Examples of other valid instruments are physical spaces, virtual spaces, or quadruple/triple helix-based approaches/mechanisms. Co-ordination among relevant players is also intended to improve the local/regional matching of the demand and supply of talent. Similarly, it is intended to strengthen the talent-producing capacity of a region by nurturing its gifted youth.

A third recommendation relates to the opportunity to identify key driving sectors for retaining/attracting talent.

A fourth recommendation is to stimulate the absorption of talent from outside. This could be achieved by attracting international talent and/or regaining such talent that had previously moved away. It may involve the setting-up of specific projects or medium-term strategies as well as branding initiatives or initiatives aimed at rewarding talent.

A fifth recommendation is for LRAs to work on the removal of structural impediments/barriers, which may, for example, be related to infrastructure (e.g. physical and/or technological), services and facilities, the reputation of the locality/region and culture (e.g. gender-biased mentality).

Finally, as brain gain automatically leads to competition for the same resource (i.e. talent), it is suggested that public authorities facing the same challenges should seek co-operative and/or shared solutions.

Source: (Regions, 2018^[15]). European Committee of the Region; Commission for Social Policy, Education, Employment, Research and Culture Addressing brain drain: The local and regional dimension; EU 2018.

Increasing the participation rate of underutilised workers

In all cases the main task is to identify policies that will encourage individuals who are currently out of the labour force to engage in employment. In some cases this may be a simple function of wages, which should increase as the number of workers declines. However, in many instances an important impediment is not directly related to wage levels. Women may have low participation rates because they have major household care responsibilities for children or elderly relatives. Providing high quality care at low cost and in close proximity to the home or place of work could increase female participation rates. Elderly may not

participate because they no longer wish to, or are unable to work full time. By creating part-time jobs or facilitating the sharing of a single job among several individuals it may be possible to increase their participation rates. The disabled may not participate because they need specific work adaptations that employers have previously been unwilling to provide. With accommodation's they could be more likely to engage in work.

Box 3.5. Expanding opportunities for older workers

Make use of us: 45 + Employees in your enterprise (Poland)

The aim of this project implemented in Pomorskie region in Poland, was to identify opportunities to develop the human resources policies of SMEs (mainly through the development of the management concept) to more fully exploit the potential of workers 45+. Quantitative and qualitative research constituted an integral part of the project and was aimed at monitoring the situation in the labour market in the Pomorskie, with particular emphasis on issues related to the employment of workers aged 45+. The studies were conducted among SME entrepreneurs and 500 enterprises were questioned. Managers responsible for human resources policy in the investigated entities were the respondents of the survey. The respondents evaluated the group of elder workers quite positively, pointing to loyalty of these workers, respect for work, flexibility, diligence and experience. On the other hand, they evaluated as low: the ability to adapt to change; the desire to undertake further education, and openness to innovation. The result of the positive evaluation of the 45+ workers, as well as declarations regarding implementation of age- management- oriented policies draws a quite optimistic picture of 45+ workers' employment perspective in the SME sector. As a result of the project's realisation, two publications were issued: a guide for SME employers entitled "How to be successful at employing workers 45+" and a book titled "45+ employees in an enterprise".

Perspective 50 plus: regional employment pacts for older long-term unemployed persons (Germany)

The Federal Programme was launched in 2005 as part of the overall Initiative 50 plus, which aimed to improve employment opportunities for the elderly. The programme re-activated more than 580 000 long-term unemployed persons above the age of 50 between 2005 and 2011 and re-integrated 160 000 of these into the regular labour market. The programme targeted specifically the regional level integrating regional employment pacts with a budget for the re-integration of older long-term unemployed persons into the labour market. The programme had a special focus on gender mainstreaming acknowledging that unemployed women above the age of 50 face particular challenges in finding jobs and includes special projects specifically targeting women with migrant backgrounds. The lessons learnt from the programme can be classified along two categories: how institutional arrangements can be configured to deliver effective active labour market policies (governance aspects) and new ways of working with long-term unemployed (methods and approaches)

Source: Polskie Towarzystwo Ekonomiczne w Gdansk, 2012; (Martinez-Fernandez et al., 2012^[7]).

In remote and sparse rural areas, transport to work is more difficult than in urban places. Even where public transit exists, it is generally infrequent and does not cover many routes. This means that people tend to rely on local jobs that are in close proximity to their residence or require an automobile. In the first case the likelihood of a good match between employer and worker can be low, which can decrease participation rates. In the second case the cost of owning and operating a car may be too high given the person's skills and prevailing wages, leading to withdrawal from the labour force. No standardised solution exists to resolve the transport issue, but many rural places are exploring innovative ways to provide relatively low-cost transport options in a rural context (see for example Italy's Inner Areas Strategy and Box 3.6)

Box 3.6. Adapt public transport for rural areas: “Big data” and public transport provision

“Big data” holds much promise for improving the planning and management of transport activity by radically increasing the amount or near-real-time availability of mobility related data. Transport authorities will need to ensure an adequate level of data literacy for handling new streams of data and novel data types.

Traffic operations, transport planning and safety are areas where authorities must critically evaluate where and how new, or newly available data and data-related insights, can improve policy. “Big data” can help governments, businesses and individuals to make more informed decisions. Better data can help transport authorities to understand commuters’ behaviour, provide targeted information and identify policy interventions. In fact, the biggest gains from using big data may come from changing user behaviour.

From the government perspective, there is need for better data to support decision making, at least for the following purposes:

- understanding better the demand (needs by different user groups)
- better planning services to match user needs and
- making the market case for privately operated services (profitability).

Source: OECD/ITF (2015), International Experiences on Public Transport Provision in Rural Areas, OECD, Paris, available at: http://www.internationaltransportforum.org/Pub/pdf/15CSPA_RuralAreas.pdf.

Increasing migration to rural areas

Demographic decline at the national level is typically accompanied by high rates of decline in some regions and increases in population in other regions. Regions that tended to lose population, or which had slow rates of growth prior to the onset of demographic decline, typically continue to experience significant population drops. Korea’s projections show that decline in rural areas will continue and accelerate in some cases due to significant outflows of young people, especially young females. In general, it can be assumed that regions with low rates of employment and low earned incomes will be unattractive to migrants. Further, rural regions across the OECD have been relatively unattractive places for international migrants unless they are required to go there as a condition of entry to the country. Even then many individuals leave for an urban setting as soon as they can, especially if the urban place has a significant number of their fellow citizens (Box 3.7).

If a rural region cannot retain a large share of its youth, it is unlikely to be an attractive place for others. The single large exception to this rule is in agriculture, where in many countries foreign migrants, either permanent or temporary, now constitute a large part of the farm labour force. This largely reflects the prevailing low wages and harsh working conditions on farms that discourage local people from farm work. The use of restricted entry visas that limit foreign workers to farm labour provide farms with necessary labour. While farm employment is unattractive to most rural citizens it can be desirable for people from poor countries. Programs to admit farm workers tend to exist in countries where the majority of production takes place on large farms and a large number of seasonal workers are required for harvest and field operations. However, most farms in Korea are small enough to be able to rely on family labour and often cannot fully utilise all their available labour on a regular basis, which makes bringing in large numbers of seasonal farm workers improbable.

Korea has introduced policies to encourage people in urban areas to consider relocation to a rural community. The success of this program will hinge on both the community being attractive as a place to

live and there being an opportunity to earn an adequate income. Rural places often have desirable amenities and it is relatively easy to provide acceptable housing. However, it can be harder to provide the full set of public and private services that urban people are used to. Even more difficult is providing adequate employment, especially for a young family. If both parents work, which must become common given the shrinking labour force, then high quality affordable childcare will be required. Further, in many rural areas there are few or no opportunities for many urban careers and it can be difficult for an individual to identify a community where their skills are marketable. Box 3.8 provides examples of investments that have been made in a number of rural regions in OECD countries that can increase attractiveness. Box 3.9 describes an island community in Japan that successfully underwent a revitalisation process and is now attracting new residents.

Box 3.7. Migration as a driver of regional development

Many regions in the OECD face significant demographic change and a declining supply of labour as their populations age. To alleviate these challenges and reap the benefits of migration for regional development, the integration of migrants is crucial, making it one of the most relevant and pressing policy challenges in OECD countries. While migration and the size of migrant communities differ across countries, regional differences within countries also tend to be significant. Despite the scale and relevance of migration, a lack of detailed subnational data on migrants is often an impediment. Furthermore, limited evidence on how migration affects regional development remains a significant challenge for effective policy design. In OECD countries, the migrant population share has increased in recent years, reaching 12% in 2019. However, the extent of migration has a strong geographic nature, with the share of migrants varying widely across regions in the same country. Overall, migrants are significantly more concentrated in specific types of regions than the native-born population, with more than half of the foreign-born population (53%) living in large metropolitan regions, compared to only 40% of natives. Migration has also increased faster in specific OECD regions such as capitals or regions with more dynamic labour markets.

While migration generates valuable benefits for regional economic development, those benefits are not shared equally across space and different people. Regions with more highly educated migration record larger increases in international trade. More developed regions appear to benefit the most from migration with respect to innovation. In contrast, economically lagging regions experience higher adjustment costs in the labour market as a result of migration, which is particularly pronounced among low-skilled native-born workers. Targeted policies could help spread migration's benefits. To ensure that all regions and groups profit from migration, policies should aim to mitigate the potentially adverse labour market effects on vulnerable groups such as non-university educated workers and economically lagging regions.

Source: OECD (CFE) workshop on Migration and regional development, September 2021.

Box 3.8. Improving the local quality of life to attract and retain people

Providing a higher quality of life can both help attract and retain people in a rural place. Improving quality can involve a wide range of actions, including, improving housing, providing better access to services, expanding the range of cultural experiences, improving the quality of the environment, and improving connectivity to other places. In France, the national government has invested in constructing Maisons de service au public (Public services houses) and Maisons de santé (Health services houses) in rural regions. These facilities allow the colocation of a number of public services or health services in low-density or isolated territories while sharing costs and employees as far as possible among communities to improve efficiency. Users benefit from reduced transport costs and the ability to schedule multiple meetings in one visit. It has also been easier to attract doctors and other professionals to these locations because there are greater opportunities to interact with peers. (Information provided by the Commissariat Général à l'Égalité des Territoires, France) (OECD, 2016^[9]).

Another option is to invest in expanding cultural opportunities in a rural place. In the city of Heerlen investments in culture, creative communication and in engaging with communities proved to be successful in creating a positive and creative people's climate which has been central in the city's urban strategies. Two projects were particularly effective: a community-based open web platform, the Zachte G Network for Creative Economy, where creative individuals displayed their talent and work and connect cultural and creative entrepreneurship and Design for Emptiness Challenge, a project gathering entrepreneurs, artists and developers to build concepts for empty buildings in the town centre. The case of Heerlen challenges the common sense that shrinking areas are places without ideas, creativity and innovation and shows that investing in people's climate is as important as investing in the local and regional economy (Martinez-Fernandez et al., 2012^[7]).

Korea and a number of other OECD members are embarking in housing renewal projects to remove decrepit or abandoned homes and modernise other housing in rural places to both improve the overall attractiveness of the community and to provide a better housing opportunity for residents. Since rural homes are typically cheaper to buy than urban homes these improvements in quality may be a means for attracting new residents.

Source: (OECD, 2016^[9]) and (Martinez-Fernandez et al., 2012^[7])

Box 3.9. Regional revitalisation: the Ama-cho model (Japan)

The small island municipality of Ama-cho in Shimane Prefecture offers an excellent illustration of how local revitalisation can occur in a rural setting. Ama-cho saw its population fall by more than 70%, from almost 7000 in 1950 to not much more than 2000 a half-century later. It has since begun to grow again, attracting an influx of new residents from elsewhere, and the local economy has picked up considerably. Ama-cho's experience is instructive in a number of ways, and the lessons it holds are relevant to remote rural communities that are struggling for survival elsewhere in Japan and, indeed, around the OECD. The town had been struggling with decline for decades before it hit upon a mix of policies that enabled it to change trajectory. The change in Ama-cho's fortunes has been the product of a multi-faceted strategy that included measures to put public finances in order; innovation in public service provision (especially education); innovation and entrepreneurship that combines technologies from elsewhere (the best known is the cell-alive system for freezing seafood products in a way that retains quality better than other technologies) with local assets (especially Ama's rock oysters); and a mix of public and private initiatives, as well as public-private collaboration. Ama-cho's turnaround was engineered locally; it was not the result of large-scale intervention or funding from outside. Finally, Ama-cho has not turned in on itself but has rather reached out to the world, working to export its products and attract visitors and newcomers. Social capital and trust within the community have been critical ingredients in Ama-cho's success, and these can be easier to foster in small communities where residents know one another. In contrast to other places however, Ama-cho has worked deliberately to foster a strong sense of community that is still open and outward-looking, welcoming visitors and newcomers and encouraging people to try new things – even when there is a real risk of failure. The island tries to provide young people with opportunities to “learn by doing”; opportunities that a big city could not give them. Small rural places are often thought to be very conservative and resistant to change, and sometimes they are, but a growing number of Japan's rural communities are showing how they can embrace much more open and entrepreneurial attitudes to change.

Source: (OECD, 2016^[9])

Broadening rural policy to respond to demographic decline

Revitalising local rural economies is required, both to slow current high rates of youth migration and to attract urban people to rural areas. Investments in public infrastructure and improvements in government services can make rural areas more attractive places to live, but without a strong local labour market, mainly based on private firms, communities can only survive if they receive ongoing transfer payments. Sustainable rural places must have an economic capacity that allows them to be competitive exporters of goods and services (OECD, 2016^[16]).

While rural policy can be described as any policy that affects the people or places in rural territory, it is useful to focus on a small number of core policy domains where rural specific policies can be identified that have the potential to offer substantial support to rural people, forms and communities in Korea. They are:

- agricultural policy broadly defined to include farming and fishing and related activities;
- tourism, once again defined to include cultural activities that can attract visitors to rural areas;
- manufacturing, mainly focused on SMEs.

Because rural areas are characterised by low density, long distances and an inability to take advantage of economies of scale they are often challenging places to provide goods and services by typical means in both private and public sectors. This opens an opportunity for non-profit providers to play a larger role. In

addition, it is important to ensure that rural areas are able to keep up with technological change by engaging in innovative activities.

Currently Korea's rural policy focuses on expanding agriculture and tourism, with much of the focus in rural tourism either on landscape amenity or cultural tourism that is linked to traditional farming and fishing locations. These are important strengths for rural areas in Korea, but only having two pillars for rural economies can be problematic. In particular, farming both tends to offer seasonal employment with low wages and preserving traditional farming and fishing practices is now being challenged by an inability to attract new entrants. In principle while tourism and farming could offer the equivalent of a full time job by combining part-time work in both sectors this is in practice difficult, because the peak employment seasons for both sectors overlap to a great extent.

Given the strength of Korea in manufacturing a potential third pillar could be rural manufacturing, but at present rural manufacturing firms struggle to remain competitive (OECD, 2018^[14]). Despite the clear challenges facing rural manufacturing firms they are present in most of the country and there is a considerable rate of new business starts, suggesting that people are interested in manufacturing. While rural manufacturing may not directly employ as many people as farming or tourism, it has the advantage of providing mostly full-time jobs with better wages. Even if wages in rural areas are not as high as in Korean cities, the addition of a third pillar in rural areas would offer an additional source of household income that, in conjunction with farm or tourism sector employment, could raise community and family incomes to a higher level.

In addition, it is important to find ways to stimulate alternative ways of organising firms in rural areas beyond traditional investor owned "for-profit" enterprises. Encouraging a larger role for co-operatives and various forms of social enterprise in rural areas can both increase number and variety of businesses and improve the attractiveness of rural communities to current and potential residents. Returns on investment in rural locations are often low because demand is low, input costs are high and there are few opportunities to achieve scale economies. Various forms of social enterprise can thrive in these conditions because firm owners have a broader objective. In many rural places, some form of community ownership has allowed a vital business to remain in operation and help to stabilise the population.

Box 3.10. Success factors for territorial Smart Specialisation Strategies

Lead actors or institutions that are strongly committed and well positioned to mobilise other stakeholders and resources and to set the strategic framework for further actions normally initiate the process of designing a specialisation strategy. These lead actors may arise, for example, from companies, research institutions, national or regional authorities. The mobilisation and empowerment of key stakeholders and institutions to realise their potential as leading contributors are essential elements to transform a traditional regional innovation strategies into regional innovations strategies for smart specialisation.

Research on the successful adoption of Smart Specialisation Strategies in the OECD finds that the key success factors needed to ensure an efficient contribution from all relevant socio-economic actors involved in the designing of the smart specialisation strategy include:

- The participation of the leading institutions of knowledge: universities and institutions of research and innovation with sound expertise for the skills, scientific and technology frontiers that exist in a country or region;
- The participation of highly skilled experts in the process, given the increasingly cross-sectoral, cross-technology and cross-border dimension of entrepreneurship and innovation activities;
- The need to build trust and reciprocity among all socio-economic actors involved;
- The need to increase transparency on how stakeholders are selected and involved and, especially, what role (empowerment) they are provided during the process.

Source: OECD (2013), Innovation-driven Growth in Regions: The Role of Smart Specialisation, <https://www.oecd.org/sti/inno/smart-specialisation.pdf>. These objectives are to be achieved through regulatory reforms in urban and rural development, education, employment, medical care and agriculture. The zones are intended to spark private-sector investment.

Agricultural policy

Farming has become a smaller part of the rural economy in Korea, just as it has in all OECD countries. But farming remains the largest single use of rural land. In Korea, as in other OECD countries, the farming population is becoming older and fewer children of farmers wish to take over their parents' farms. In some countries the result has been a significant increase in average farm size, with a relatively small share of very large farms producing large quantities of output for domestic and export markets. These countries are typically much larger in size than Korea and have far more favourable agronomic potential. However, even in these countries there is an increase in the number of small farms that produce high value specialty crops and livestock products for either local or on-farm sales to, tourists, local residents or to specialty shops outside the region.

In Korea, where rice farms are the main specialisation and largest land use. there are considerable opportunities' for modernising production techniques that can improve farm household income. This however leads to farm consolidation and a reduction in the number of farm households, which can accelerate rural depopulation. The inherent trade-off between increased farm productivity and stabilising rural populations requires the use of integrated policies that address both issues. Japan has undertaken a project on modernising rice farms described in Box 3.11 that may suggest a model for Korea.

Box 3.11. Rice farming and rural development in Japan

Rice is Japan's most important crop, not only from an economic point of view, but also from a social and environmental perspective. It accounts for only 12% of total value added in agriculture and fisheries, and this share has been gradually and steadily declining. However, rice farming is the largest user of land and water. It accounts for more than 50% of the total cultivated area in Japan and accounts for the majority of agricultural water consumption. Over the last decade, MAFF has sought to increase the productivity of agriculture with policies targeting large-scale farmers and promoting farm consolidation – a major departure from traditional policies, which supported all types of farmers, often enabling low-productivity small-scale and part-time farmers to remain in business, rather than exiting the market in favour of larger, more efficient producers. At present, "business farmers" (i.e. those who make their living as farmers rather than using part-time farming to supplement their incomes) are a minority of all farmers but they now cultivate around half of all farmland; MAFF is working to increase that figure to 80% over the coming decade. However, farm consolidation could undermine the viability of rural hamlets. Given the size of most hamlets, an average hamlet could profitably sustain just one or at most two rice farmers. If the remaining farmers sell or lease their land to such a producer, this accelerates population outflow. To maintain and demonstrate the multifunctionality of agriculture, MAFF designed a second set of policies to ensure payments to hamlets collectively maintaining irrigation and drainage facilities, as well as companion policies focused on rural development. Information provided by the Ministry of Agriculture, Forestry and Fisheries)

Source: (OECD, 2016^[9])

Box 3.12. Supporting Small Farms

Small farms are by far the majority of all farms in OECD countries and account for a significant share of the population in many rural regions (OECD, 2016^[16]). Few of these farms benefit from traditional agricultural policy because it uses support mechanisms that are typically based on the volume of production, hectares operated or number of animals, all of which lead to low payments for small farm households. Even with increases in the rate of support the incremental income for small farms is small, because their production base is small. This means that for the family income of small farm owners to reach national household averages, active engagement in non-farm employment is essential. In multiple OECD countries the average household total earned income of small farms can exceed all but that of very large farms (OECD, 2003^[17]).

Off-farm income provides multiple benefits to the farm household, the community and even the nation (Freshwater and Jette-Nantel, 2017^[18]). For the household off-farm income augments farm income and raises total household income to a level where farming can continue. This allows farm households that would have otherwise had to leave the sector to remain and maintain their preferred way of life. In addition, because off-farm income is uncorrelated with farm income it provides a significant risk mitigation function, further increasing the resilience of small farms (Jetté-Nantel et al., 2011^[19]). Finally, in countries with a slow process of land consolidation that can allow the expansion of larger more productive farms, increasing opportunities for small farm operators to engage in local nonfarm employment can be a way to facilitate a subsequent transition to leaving farming while remaining in a rural area.

For communities facilitating off-farm employment benefits has several benefits. First, farm households are more likely to remain in the community and contribute to retail demand and to local taxes, and equally important, augment the population using local services, such as, schools and hospitals. The higher level of utilisation can contribute to lower per capita costs and maintain a critical mass required to keep these local services functioning. In many countries, farms have become part of local tourism initiatives by offering agri-tourism opportunities, or by providing bed and breakfast stays or farm-based restaurants that offer local cuisine. The labour force contribution of farm families is significant in three ways. First, in a time of a shrinking work force increasing the participation of individuals who might otherwise be outside the local pool of available workers is important. Second, farm families have important artisanal skills from working with equipment and animals that can make them effective workers, even though they may have limited formal education. Third, because they also have farm responsibilities they may be amenable to more seasonal or part-time employment opportunities that can provide a local firm with a more flexible workforce.

At the national level, support for small farm households serves several objectives. First, it can help to maintain regional balance is population by retaining farm families who would otherwise move. Second, small farms can be more effective environmental stewards: because they tend to have a stronger commitment to protecting land that has been in a family for multiple generations, because they tend to follow less intensive cropping and livestock management practices, and because they are more likely to integrate agri-environmental practices into their operation. Third, small farms are more likely to engage in practices that maintain traditional rural culture and land use patterns, which can be important to the entire society. Finally, increasing off-farm income provides government with an effective solution to longstanding problems in targeting agricultural policy benefits to both small and large farms.

Adopting policies that encourage part-time farming and active engagement in local employment opportunities can require modifications to national agricultural and social policies that now favour full-time farms. Local employers may also have to be encouraged to structure work opportunities in ways that allow farm families to participate in off farm employment while maintaining necessary farm

operations. Finally, because farmers are typically highly sensitive to tax obligations it may be necessary to modify current tax regulations to encourage off-farm work.

Source: (OECD, 2003^[17]) Farm Household Income: Issues and Policy Response; (OECD, 2016^[20]) Farm Structures: Managing Transitions and Improving Livelihoods. Background note for OECD Meeting of Agriculture Ministers, April 2016; (Jetté-Nantel et al., 2011^[19]) Farm income variability and off-farm diversification among Canadian farm operators.

Korea would seem well suited to expanding this type of agriculture as a part of its rural development strategy. Small-scale farms provide agricultural output and are also more likely to provide a high-quality natural environment, as well as being a key part of supporting local and national heritage amenities. These multi-functional farms are consistent with a current trend in agricultural policy to move away from direct price support for the production of commodities to an agricultural policy that is more environmentally friendly and that supports broader rural development objectives.

Small-scale farms are also more likely to support broader rural development efforts. Part-time work is common, both in terms of hiring supplemental labour on the farm during busy seasons, and in farm household members seeking temporary or full-time work off the farm to supplement farm income. Small farms also result in a larger local population than do a few large farms on the same area of land. This larger population provides more local demand for retail establishments and for public services, which makes the broader local economy more viable. (See for examples the Box 3.13 and Box 3.14).

Box 3.13. The co-operative model in Trentino (Italy)

The farming structure in the Autonomous Province of Trento (Italy) has always been characterised by the presence of a large number of small enterprises, family based and endowed with relatively small portions of land. Each farm has on average an extension of 1.5 hectares and this condition had a negative influence on the productive structure. Economies of scale were precluded with adverse effects in efficiency and performance. The solution was found in the co-operative system. Co-operatives account for 80% of the provincial agricultural production and manage almost all the marketing and distribution activities of local producers. The evident positive performance of the agricultural co-operatives in Trentino is due to the idea of vertical integration and concentration (economies of scale), implemented over time by the Federation of Trentino Cooperatives and the Autonomous Province of Trento. This means that the first level co-operatives, spread over the territory, have a direct link between members and the co-operative structure, offering advice and resources to the small producers. The second level co-operatives, namely the consortia, are governed by a pact among co-operatives to develop all marketing functions and relations with the value chain. Mastering on the accumulated experience, the second level consortia organised their strategic goals to increase market shares in final product markets through aggressive sales efforts. They were supported by aggregation, facilities operating at optimal scale and efficient managerial functions, enabling co-operatives to reach economies of scale. Consortia focus their marketing strategy on quality factors, in particular those involved in production and reflecting the consumer's preferences, instead of using discounts or promotions to underbid competitors. They avoid to pressure on product prices and address their strategic design and incentives on members to innovate in quality and sustainable production techniques. Being able to capture part of the increased marketing margins, the gains return to the active owners preserving their entrepreneurial responsibility. The third level, the Federation of Trentino Cooperatives, is at the centre of the system composed of first and second level co-operatives. It unites, represents, protects and promotes the interests of the associates. The Federation is a legally recognised organisation that brings together over 500 companies, active in all productive sectors, and a social base consisting of about 280 000 people. This is an element that distinguishes the co-operative movement in Trentino from others. All sectors of entrepreneurship and all the merchandise areas in which the Trentino co-operation operates find in the Federation a unitary centre of representation and assistance. An integrated group of rural and co-operative banks support the system.

Source: (OECD, 2014^[21])

Box 3.14. Fisheries and aquaculture

The Greek government seeks to foster the production of high-quality and high value-added agricultural and fishery products in less-favoured areas or areas with permanent natural handicaps such as rural areas and islands. The Greek Operational Programme for 2014-20 under the European Maritime and Fisheries Fund (EMFF) has two main priorities: sustainable fisheries and sustainable aquaculture. The priority on sustainable fisheries envisages investments in the modernisation of fishing ports, auction halls, landing sites and in the construction of fishing shelters, innovation in fisheries, the creation and monitoring of artificial reefs, and protection and restoration of marine biodiversity. The aquaculture priority aims at fostering environmentally sustainable, resource-efficient and knowledge-based aquaculture. The EMFF supports productive investments in aquaculture, actions to improve innovation in the sector, such as developing technical, scientific or organisational knowledge and the introduction of new aquaculture species with good market potential and new or improved products and processes.

All OECD countries are advancing reforms in their fisheries management systems to improve the profitability and sustainability of the sector. They are also working actively to promote the development of aquaculture, which is seen as the future of fish production. These efforts include regulatory improvements and increased spending on research, as well as cost-sharing with the private sector to encourage investment. Aquaculture has been one of the fastest-growing forms of food production for many years and growth in aquaculture can provide jobs and development opportunities in territories with few economic alternatives. The emphasis is shifting from stimulating growth to putting the sector on a sustainable footing for the future by addressing environmental limits and focusing on new production technologies to increase competitiveness. To do so most countries provide now support to general services to the sector, rather than transfers to individual fishers. Governments invest a significant amount of resources to this kind of support, which includes management, enforcement, research, infrastructure, marketing, community support, education and training, research and development, management of resources.

Source: (OECD, 2020^[22]) Territorial Reviews: Greece 2020; (OECD, 2020^[23]) Environmental Performance Reviews: Greece 2020. (OECD, 2017^[24]) Review of Fisheries, Policies and Summary Statistics, 2017.

Tourism policy

Korea has already taken important steps to increase the role that tourism can play in rural communities. Because most of rural Korea is in close proximity to an urban agglomeration a key focus for tourism could be short-term visits that bring visitors for a weekend or a multi-day midweek stay. In addition, rural communities in Korea could become places where urban families have a summer home they visit regularly, especially if these families have some historic attachment to the community. Most rural regions in Korea cannot offer the kind of compelling, globally recognised tourism experience that makes them a destination for international tourists. However, it may be possible to put together a package of tourism experiences that are collectively more interesting for international tourism. Examples of the approach are: the Bourbon Trail in central Kentucky that offers visits to about 20 different distilleries, barging in Burgundy that allows visitors to take a barge along historic canals and stop in a number of small villages, or the Queensland Heritage Trail in Australia that links multiple communities each of which have an interesting cultural or natural feature. In addition, special events, such as seasonal festivals or concerts can bring people to a region for the first time and provide the motivation for repeated visits or even longer-term investments in a second or retirement home.

Tourism has become an important way to diversify the economic base of rural communities and regions. While it provides mainly lower wage seasonal employment opportunities, these can be an important

addition to household income in a rural labour market where many other jobs are seasonal in nature. Moreover, tourism can be an effective part of a recruitment strategy that tries to attract new residents and businesses. Individuals who visit a place and form a favourable impression are likely to be more interested in a permanent relocation because they have had a direct positive experience and are likely to have developed personal connections in the community.

Box 3.15. A Digitalisation Strategy for Austrian Tourism

Digitalisation is transforming the tourism sector at a rapid pace, with strong implications on both, demand and supply. In view of an active role in this process, the Ministry of Science, Research and Economy together with the Austrian NTO and the Federal Economic Chamber launched a digitalisation strategy for Austrian tourism in September 2017. The strategy has been developed in an open innovation process with the involvement of many stakeholders (national and regional, industry experts from tourism, technology and the creative economy, universities and research, etc.) and pursues three strategic objectives i) to shape digital change ii) to strengthen the innovation capacity of enterprises and iii) to create skills and processes for digital transformation. The strategy defined 22 measures to meet these objectives including nationwide coverage of broadband technology, good information and co-operation structures for data management, support for digital innovation in SMEs, as well as for the development of digital skills for the sector.

Source: Ministry of Science, Research and Economy. OECD (2018), "Greece", in OECD Tourism Trends and Policies 2018, OECD Publishing, Paris. DOI: <https://doi.org/10.1787/tour-2018-19-en>.

Box 3.16. The Seiwa area, Mie Prefecture (Japan)

The Seiwa area of Mie Prefecture is a rural district with a population of about 5 000 and an area of 53.6 km², of which 70% is forested and about 13% is cultivated. The average farm size is roughly 0.4 ha and the main products are rice, tea, Chinese cabbage, cabbage, white alliacious, wheat and soybeans.

By the early 2000s, Seiwa found itself facing an ageing and declining population, a lack of successor farmers and the growth of abandoned farmland, which, in turn, contributed to the encroachment of wild animals into cultivated areas. In response, the ten small hamlets in the area formed the Seiwa Rural Resource Management Association, which has put in motion an impressive array of local projects.

In an effort to enhance the landscape and protect farmland, the association organised maintenance of the canals and farm roads, including the planting of flowers on unused land, the creation of a biotope and the introduction of multi-use of irrigation water for community purposes (firefighting, environmental uses, etc.). Some farmland has been returned to a wild state, but co-ordinated land management has made it possible to do this efficiently and without harming the land that remains under cultivation. Household garbage is now composted. In an effort to do more than just preserve agriculture, the Association has moved in the direction of the sixth industry, organising local festivals and building a market for distinctive local produce. This, in turn, has reinforced environmental performance, as the farmers found that it was better to market green produce than to use pesticides and this has also helped to promote green tourism in the area and to improve the quality of the water.

What began as a resource preservation exercise in the face of farm abandonment has thus led to a wide range of new activities. Though backed by the municipality, the Association has not relied much on municipal or central government funds, though it has attracted sponsorship for some activities from Sharpe.

Source: Information provided directly by Seiwa Rural Resource Management Association. (OECD, 2016^[9]), OECD Territorial Reviews: Japan 2016.

Rural manufacturing policy

Manufacturing is a recognised strength of the Korean economy and there is a significant amount of manufacturing already taking place in rural Korea. There are opportunities to broaden the range of manufacturing, particularly by SMEs that could complement existing subsidiaries of large firms (Box 3.17). While subsidiary establishments can provide employment to a large share of a local labour market in a rural area, the nature of the work is typically highly specialised, which leaves workers with a skill set that is not very useful to other employers or for becoming an entrepreneur. Moreover, because branch plants are integrated into national or global supply chains opportunities for forward or backward linkages within the community or region are limited. As a result, multiplier effects for the local economy are small.

Box 3.17. SMEs in Korea

The 2018 OECD Economic Survey of Korea (OECD, 2018^[14]) provides a comprehensive assessment of the state of SMEs. Korea has relied upon a relatively small number of large manufacturing business groups- the chaebols, to drive its economic growth. These firms dominate the manufacturing sector and account for the majority of Korean exports and a large share of employment and innovation. However, their ability to continue to propel the economy is now in question. In Korea, as in all OECD countries, SMEs account for the largest share of employment, but in Korea they: provide the largest share of total employment in the OECD; exhibit a much lower rate of productivity than large firms, and one that is declining, as well as being one of the lowest in the OECD; and, are concentrated in low-wage, labour intensive activities, particularly services at 90% of all service sector firms. Multiple factors contribute to the limited role that SMEs have played in the past. Some include: national and local government policies that while providing high levels of support have stifled growth through strong regulations, and support mechanisms that penalise expansion. High levels of support and the prevalence of older workers being squeezed out of regular employment in large firms or the public sector have contributed to a high rate of SME start-ups. However, many of these firms are undercapitalised and have weak business models, which limits productivity and their contribution to economic growth. Despite these underlying weaknesses, Korea has the lowest rates of business exits in the OECD.

Demographic decline in Korea increases the importance of enhancing the role of SMEs, particularly increasing their rate of productivity. Current low productivity rates of many SMEs mean that wages are low relative to larger firms, where higher productivity levels allow higher wages. But several things must happen for productivity and wages to rise. The first is that SMEs will have to improve the technical efficiency of their operations, by adopting new production, management and marketing technologies, and improve working conditions. At the same time the average level of skills of workers employed in SMEs will have to increase to support the investments in improving technical efficiency. Not all SMEs will be able to do this and as a consequence “churn” in SME numbers from new entries and exits will have to increase, at least in the short term. A worker shortage will increase the pressure to reduce under-employment in SMEs, and to better match new worker skills with employer needs. Currently, Korea has a relatively high rate of youth unemployment that reflects a dual labour market, where there is strong competition for high wage and good benefit public sector and chaebol jobs, and an aversion by young people to working for, or starting, an SME. The result is one of the lowest youth employment rates in the OECD and a particularly high rate of young people with tertiary education who are neither employed, nor in education or training. Delaying participation in the labour force imposes large costs on these individuals and on society, especially in an environment where the underlying worker replacement ratio is low.

To its credit, Korea has embarked on major reforms to improve the performance of SMEs. These include: regulatory reform, efforts to enhance rates of entrepreneurship, improving SME access to financial resources, expanding the role of R&D in SMEs, and strengthening linkages to foreign markets, and all are important. But Korea should consider an explicit regional dimension to its SME strategy. More rural areas are particularly reliant on SMEs because they have limited capacity to host large enterprises. SMEs in rural areas are also more likely to experience difficulty in discovering new technologies, less likely to have access financial support, and more likely to have high rates of entrepreneurship that is driven by weak employment prospects, rather than a perceived market opportunity. This latter point can be particularly important for older workers who may be more productive in formal employment than as owners of a marginal small business.

Source: (OECD, 2018^[14]), OECD Economic Survey of Korea, 2018.

Other OECD countries with strong manufacturing sectors have found ways to combine large scale manufacturing plants in more urban regions having large labour forces, with smaller export-oriented firms in more rural regions with smaller labour forces. Notable examples are Germany and Italy. Many of these small firms are family owned and focus on producing highly specialised products that have small but profitable markets. The manufacturing processes typically combine sophisticated technology with skilled labour, and strong customer service, making it difficult for potential competitors to enter the market. The *mittelstand* in Germany (Box 3.18) provides a useful example. Key to the success of these firms is access to new knowledge, and while German firms have developed this capacity over time it will be important for Korea to support firms of this type initially with government programs. The manufacturing extension service in the United States provides an example of a way to do this (Box 3.19).

Box 3.18. Manufacturing in *Mittelstand* (Germany)

Large German manufacturing firms have a global presence in automobiles, engineering and chemicals, but a group of smaller German firms loosely termed the *mittelstand* play a major role in Germany and in manufacturing export activity. *Mittelstand* firms are SMEs (employment is less than 500), but not all German SMEs are *mittelstand*. While 99% of all German firms are SMEs and account for half of German output and 60% of employment, the *mittelstand* share is about 70% with a concentration in construction manufacturing and services (Berlemann, Jahn and Lehmann, 2019^[25]). What characterises the *mittelstand* is a particular type of business model that: entails owner-operators from multi-generational families, has a focus on long-term firm viability, engages in strong worker training efforts, and provides a narrow product or service that involves high level of customer support (Parella and Carmona Hernández, 2018^[26]). In addition, a large share of *mittelstand* firms are found outside large cities in smaller towns.

Mittelstand firms are a key part of the social responsibility model of German capitalism, where the firm has responsibilities to its workers and to the broader society, and not just to its owners (Parella and Carmona Hernández, 2018^[26]). This is both a key strength and a possible weakness. Firms are strongly involved in workforce training and offer high wages and stable employment opportunities to retain highly productive workers. But these workers can be highly specialised in their skills, since they are employed by a firm that produces a specific niche product (Heider et al., 2021^[27]). Similarly, *mittelstand* firms invest in making steady improvements in their product in response to customer suggestions, but this form of incremental innovation can leave them vulnerable to radical shifts in the market.

The *mittelstand* offers an interesting opportunity for Korea. It is based on a family business that involves steady efforts to make product improvements to meet customer needs. In a time where labour shortages are imminent, the practice of developing strong worker skills may become more attractive to businesses that need to increase labour productivity. Similarly, if workers are to work for a longer period before retiring it may also become more attractive to engage in workforce practices that retain workers. Finally, the *mittelstand* offers an export-oriented manufacturing model that is based on SMEs that can successfully operate outside the large labour markets of metropolitan areas.

Source: Own elaboration.

Box 3.19. Manufacturing Extension Partnerships (USA)

The Government of the United States created the Manufacturing Extension Partnership (MEP) program in 1988 to support small manufacturing firms, with a focus on those in less urbanised areas. The MEP is loosely patterned on the Cooperative Agricultural Extension Service, which is a federal, state and county partnership that supports agriculture across the entire country and has been in existence since 1916. In the case of the MEP the main partners are national and state governments, augmented by state specific mixes of non-profit organisations, industry groups and universities and community colleges (Shapira, 2001^[28]). The MEP offices in each of the 50 states are jointly funded by the US Commerce Department and by state funds. While some services are provided at no cost to firms, there are charges for more firm-specific consultations. Over time the MEP program has focused more on innovative activities and the adoption of new technologies that are priorities for each state. Thus in a sense its approach is consistent with EU's efforts to induce European regions to adopt smart specialisation strategies based on existing, or emerging, competitive advantages.

Small manufacturing firms, especially those in rural areas, can have a hard time growing beyond their initial level of production and finding new markets. If they are able to expand they create more local jobs and income and can provide an encouraging signal to potential entrepreneurs who may be uncertain about the local business climate. Firms in urban areas are more likely to be able to find consultants to support them or tap the expertise of peer firms to become more productive. In particular small manufacturing firms face challenges in: obtaining or training workers with specific skills a firm requires, identifying suppliers of essential inputs that cannot be locally sourced, keeping up on technological advances that can make them more productive, breaking into new markets outside their region and, making general improvements in firm management (Sargent, 2019^[29]).

Source: Own elaboration.

In the future a smaller local labour force may make it more difficult to support larger branch plants in rural communities. However, smaller, niche product manufacturing enterprises could provide a path to a stronger rural manufacturing economy. For this to happen a multi-part support program is required. The first element is to provide encouragement to young (but also senior people) to consider entrepreneurial behaviour, rather than seeking a job in a large corporation or in government. Once nascent entrepreneurs exist a second step is to provide them with the support to take their business idea to a stage where it can actually be implemented. The third step is to provide the support for them to implement their business plan. At this stage incubators and funding can be crucial factors for a successful business launch. The final step is to assist young, promising companies and help them to grow either in size or to broaden the number of products or services they provide.

Expand the role of social enterprise

The social economy or social enterprise serves as a complementary alternative to either for-profit firms or government as a provider of goods and services. In rural areas social enterprise can be particularly important when neither for-profit firms nor government are prepared to serve the community in a manner that meets local needs. Because social enterprises are embedded in their local community and are owned and operated by people who also use the good or service produced they can thrive when other typed of provider withdraw. The main advantages of a social enterprise are: that it can rely on volunteers for at least part of its labour needs, it can obtain financing from members or through grants that need not receive a market rate of return, and it can tailor its activity to the specific needs of the member-owners. Social enterprises that provide services are often more closely related to government, such as co-operative

schools or community owned health care facilities. Other social enterprises, such as community shops or farmers marketing co-operatives are more like for-profit businesses in their orientation. In all cases a social enterprise should cover its costs and generate sufficient funds to make investments to allow it to grow but does not distribute a profit.

Some brief examples of successful social enterprise in rural regions of OECD countries can provide a context for developing a broader use of the concept as tool for rural development in Korea.

- **Appalshop, Whitesburg, Kentucky USA.** Appalshop was founded in Whitesburg in 1969 to teach young people in the region to make films that documented local history and culture. In the process it would teach people marketable skills. By 1975 it had 20 full-time employees and had expanded to provide support for artists, theatre and other creative work. Today it operates a radio station, sponsors a music festival and in 2019 installed a net-metred renewable energy system. The guiding principle of Appalshop is that supporting cultural development is also a means to supporting economic development.¹
- **Gotland's Broadband Initiative, Gotland, Sweden.** By the mid-2000s small communities on the island of Gotland realised that major telecommunications operators in Sweden were not interested in providing last-mile fibre-based broadband to rural households. In response villages organised to develop a framework where they would be responsible for installing the fibre in their community through volunteer labour with each household providing 3 days of work. Starting in 2010 and ending in 2017 broadband has been installed in all 92 parishes with a high rate of homes connected for a modest fee. In 2017 the project was one of five winners in the European Union annual European Broadband Award.²
- **Candover Valley Community Shop, Hampshire, England.** In 2013 the only village shop in the area decided to close, which would have left about 2 000 people in 5 villages and 4 hamlets with no local sources of food or other services. The shop owners agreed to continue in business until the community could develop a plan to take it over. Residents formed a committee to investigate taking over the shop as a community owned business. Subsequently local people raised GBP 120 000 and GBP 105 000 was obtained from grants to build a new shop that would also host the post office. The new shop opened in 2019 and is staffed by 40 volunteers and has 250 member-owners.³
- **iCoop, Korea.** iCoop Korea is the second largest consumer co-operative in Korea with more than 170 000 members, it focuses on ensuring that Korean households have access to high quality foods produced in a sustainable way. The co-op contracts with farmers to produce food that meets its desired standards and means of production. One of its main activities has been to find ways to produce rice in more environmentally friendly way. Research was sponsored to develop new production methods that improved biodiversity in rice paddies and subsequently farmers received contracts to produce rice using the new methods. iCoop believes that its effort is helping consumers and helping to maintain a viable agriculture in rural Korea.⁴
- **Greencraig Community Wind Turbine, Falkirk, Scotland.** The turbine project is a partnership between a local social enterprise, the Bespoke Community Development Corporation that focuses on enhancing green travel in the area and on employment training, and Locogen a for-profit renewable energy specialist. A new community investment corporation will operate the project with 65% of profits flowing to community development purposes. Bespoke received grants from the Scottish government to cover most of its share of the investment and will receive a minimum payment of GBP 37 500 over the life of the project to support its activities. Power from the project will be fed into the grid at prevailing prices.⁵
- **Social Traders, Melbourne Australia.** Social Traders is social enterprise that acts as a certifier of individual social enterprises that provide goods or services and as a platform that connects these certified businesses with public and private supply chains across all of Australia. This

intermediation function is vital for many social enterprises that have not fully developed a market niche. It also allows companies and governments that want to buy from social enterprises to certain that the firms they deal with are legitimate. Their objective is to facilitate more than \$5 billion in demand for social enterprise in Australia by 2030. This will lead to major increases in employment and in related job training as well as providing other community benefits.⁶

Across the OECD there is untapped potential within social economy organisations and social enterprises that requires policy action to unlock. These entities can help build more inclusive and sustainable society in each region. Much of the policy needs concern the development of enabling ecosystems. Building a conducive ecosystem for social economy development includes: 1) Raising awareness and visibility of social economy organisations, including social enterprises. This can be done through dedicated and enhanced framework laws or national strategies that define the nature, mission and activities of social economy organisations and therefore help policy makers to more effectively target their support. This can also be done through lighter policy options such as setting up communication campaigns or providing specific support to networks that connect social entrepreneurs to investors and public-sector representatives. 2) Providing business support to social enterprises throughout their developmental phase. Specific public support for structures such as hubs, accelerators or incubators can facilitate the development of social enterprises across territories and activity sectors. 3) Supporting a diversification of financial sources. While public support (predominantly through grants and subsidies) is a major financial source for a number of social enterprises, an increasing number now seek to access financing provided by mainstream or new funders (e.g. commercial banks or impact investors). Still, mainstream funders or impact investors perceive social enterprises – especially in the early stages – as high-risk clients and are therefore reluctant to invest in them. Policy makers need to raise awareness through capacity-building, along with efforts to share the risks with mainstream funders, impact investors and commercial banks, for example through guarantee schemes. 4) Fostering social-entrepreneurship skills in the education system. In the long run, education and skills that breed entrepreneurial behaviours need to be developed. For example, educational programmes on social entrepreneurship can provide students with opportunities to develop new solutions to unresolved social challenges and learn about business-creation processes and planning at the secondary and higher education levels. 5) Ensuring institutional continuity and political support for social enterprise development (OECD, 2020^[22]).

Political impetus can act as a catalyst for both nascent and/or well-established ecosystems, fostering and accelerating favourable conditions for the growth of social enterprises. However, challenges may emerge when political support for developing the sector of social enterprises fluctuates owing to government changes. Sustained policy support is essential to establish an enabling ecosystem allowing social enterprises to thrive over time. Concerning policy actions that are specifically designed to support the employment creation role of social economy organisations, policy makers could promote: 1) Funding stability. Ensure that public financial support goes beyond short-term contract funding so that longer term employment plans can be developed; 2) Public procurement. An important tool to sustain social enterprises is public procurement, for example including “social clauses”, using “reserved contracts”, or applying “best quality/price ratios” so that social enterprises can compete in getting public contracts; 3) Employment subsidies. An ecosystem favourable for social economy can be also facilitated through the use of employment subsidies for social enterprises working with disadvantaged individuals to offset the costs stemming from the loss of productivity associated with hiring individuals whose job performance is less than normal (OECD, 2020^[22]).

Foster innovation in rural areas

With a shrinking population it essential that rural regions find ways to increase productivity and remain competitive if they are to remain viable communities. Innovation is a major way to achieve this objective. But innovation can be difficult in rural regions because they lack most of the underlying characteristics, such as, formal research and development organisations, pools of investment capital and a core group of

scientific and engineering professionals. Innovation in rural areas comes from a number of sources. In some instances, it diffuses from urban areas where it originates. In other instances, research in urban areas is focused on applications in rural areas – for example research in agriculture, forestry or mining is typically undertaken in an urban location. Finally, there is innovation that originates in rural areas by the efforts of rural people. It is this latter form of innovation that is most subject to influence by rural society since both the actors and the locale are rural. In particular, there is a strong link between rural innovation and entrepreneurship (Box 3.21).

One way to enhance innovation is to try to attract innovative people to a rural region by offering them an environment that is conducive to their efforts. Box 3.20 illustrates an approach taken in one community in Japan. Another approach is to try to induce people who might not think of themselves as being entrepreneurial or innovative to consider a new activity. Box 3.22 provides some recommendations for increasing entrepreneurial activity by the elderly. Innovation is typically understood as the creation of a new product or new form of production, but it can also include a new service or a new way of delivering services. In rural areas all forms of innovation are important especially as a shrinking supply of labour and pressures to adjust to the effects of climate change are making current ways of providing goods and services less effective. Box 3.21 provides a number of examples from the OECD Review of the Northern Sparsely Populated Areas of Finland, Norway and Sweden (OECD, 2017^[30]) that illustrate innovative practices in remote rural areas.

Box 3.20. Attract entrepreneurs in knowledge-intensive services in Kamiyama (Japan)

Kamiyama, a rural community in Tokushima Prefecture on the island of Shikoku (Japan) set out to attract IT start-ups. The programme was launched by Green Valley, a non-profit private group, and was designed to revitalise the town by offering abandoned houses to IT engineers and other workers as satellite offices. The project is small but it has attracted 10 IT ventures to this town of 6 100 since 2010 years. Underlying Kamiyama's bucolic appeal is an advanced IT infrastructure built with the help of the prefectural government's drive to extend broadband access to its entire territory. Fibre optic cables were installed in each house and data speed in Kamiyama was faster than Tokyo. The tech cluster has attracted international attention, but it is also significant that Green Valley's revitalisation strategy goes beyond attracting IT firms: its efforts to attract and retain highly skilled workers by offering a good quality of life also extend to the promotion of cultural activities and exchanges, including an artist-in-residence programme. An important part of Kamiyama's focus is on changing the structure of the population: revitalisation may slow the decline of Kamiyama's population or even reverse it. (OECD, 2016^[10]).

Source: (OECD, 2016^[9])

Box 3.21. Examples of Rural Innovation from Finland, Norway and Sweden

Finnfjord AS: Finnsnes, Troms, Norway. Finnfjord has become the most energy-efficient manufacturer of ferro-silica in the world by investing in a waste heat recovery to electricity project. The company is locally owned and has about 130 employees, but competes with multinationals in a global market. Ferro-silica production requires large amounts of electricity to operate a smelting furnace that in turn produces large amounts of waste heat. By capturing the waste heat and using it to generate electricity from a steam powered turbine the firm has reduced its net electricity consumption by 40% and sells 340 gWh of renewable energy back into the grid. A second phase of the project will take waste heat from the turbine and use it to heat tanks where algae will be produced as a feed source for farmed salmon, capturing even more waste energy and

further increasing the energy efficiency of the plant. This is a clear example of rural innovation that was driven by the desire of the firm to reduce its costs and increase its competitiveness. The firm has no formal R&D activity but was able to find engineering expertise to support its project and bring the idea to reality. Funding from the national government for innovative activity helped support the process. In the second stage the firm is collaborating with aquaculture experts at the University of Tromsø to develop the algae tanks, showing the value of strong business-university linkages.

Nordkapp Maritime Training Centre - Oil Spill Recovery: Honingsvåg, Finnmark, Norway. The Nordkapp Maritime Training Centre has added a new specialised training program to its existing programs for sailors. Concern with the possibility of significant oil spills off the coast of Norway increases as drilling expands and tanker traffic grows in volume. Containing oil spills in an Arctic environment, particularly in winter when daylight is short, is a difficult task. While the Norwegian government maintains a fleet of ships and equipment for this purpose, a training program for crews was needed. In addition, Norway has recruited fishing boats as a supplemental resource and their crews also require training. The Maritime Centre uses a sophisticated simulation system that allows multiple ships to co-ordinate their efforts to contain spills under a range of conditions. Funding for the program comes from Eni the Italian oil company that operates the first offshore oil field in the Barents Sea. The training program is an example of how modern resource economies require sophisticated skills to deal with the challenges of day-to-day operations. These skills have to link traditional skills, such as ship operation, with new needs like oil containment. Locating the training in close proximity to where the actual work will occur is a key advantage, especially since local people are the obvious candidates for the jobs. Using an existing maritime school and adding new equipment for the particular training function fits the school because these resources can have multiple applications and benefit the oil company and regulatory process because it is an approach that is more likely to embed additional complementary skills that go beyond the specific training in oil spill recovery.

Wild Food: Koillismaa, Lapland, Finland. This project connects producers of wild foods from forests to local restaurants and food processors as a way to aggregate small-scale production of game, berries, mushrooms and fish into a larger regional presence that can be used as a “brand” to increase tourism and ultimately build export markets. The participants recognise that broadening the tourism offer is important for small remote regions that are expensive destinations. The growing consumer interest in: international foods, local foods and gastronomic tourism is a way to broaden the current tourism experience in Lapland. Participants also recognise that simply producing natural food from the forest will not be enough, and to be successful in increasing sales, jobs and incomes requires a strong investment in promoting and marketing the concept, both to tourism operators in other countries and to potential visitors over the internet. There are multiple useful ideas in this project. The first is the effort to take an underutilised resource and expand demand for it. The second is that in order to expand demand it is necessary to aggregate production from a large number of small-scale producers into a regional brand that can be marketed internationally. A third idea is the recognition that the Wild Food offer has to be bundled into a broader tourism experience, because by itself it is not going to attract many people. However, its value as an addition to more traditional experience-based tourism in Lapland can be significant. Finally, the project recognises that progress will necessarily be slow because it will take time to build the network of producers and processors, and to promote the Wild Food brand in international markets.

Ilosaarirock Festival: Joensuu, North Karelia, Finland. The festival, started in 1971, is held in early July of each year at a local park over three days. It attracts over 20 000 people and is largely organised by about 1 500 local volunteers. There are five stages that host over 50 international artists from Europe and North America offering a range of musical genres. A key feature of the festival is that it occurs at a time of the year when there is daylight almost the entire day. The festival fills local hotels and restaurants and acts as a major attraction for visitors to the region. The festival provides a way to attract people who might not come to Joensuu otherwise and diversifies the types of tourism available. It also is a way to create cohesion within the community because large numbers of volunteers participate each year in setting up and staffing the event. Profits from the festival are used to support local musicians and musical events, which further

improves cultural opportunities. Because it is such a large event, it also generates national and international media coverage that can raise awareness of Joensuu and North Karelia. Notably the festival is an example of a place undertaking an activity that is well outside its usual framework. In doing so it achieves both local and external recognition for being more innovative than is expected.

Association of Local Authorities: Vaster-Norrland, Sweden. The seven municipalities in Vaster-Norrland have formed a voluntary association to find ways to collaborate on local service delivery and better manage their administrations. The association is governed by the seven mayors and seven leaders of the opposition party to ensure that changes in administration do not adversely affect the association. The main direction of the work is to establish ways for delivering a uniform set of public services across all seven municipalities. This is a challenge because the populations of the seven municipalities are quite different and there is considerable range of settlement sizes and connectivity among settlements. In addition, the municipalities have recently created a unit that delivers training for all municipal employees for the seven municipalities to reduce costs and to help support the joint service delivery effort. Small municipalities are always challenged by higher unit costs for administration and service delivery. By forming an association it can be possible to capture some scale economies if uniform procedures can be followed. This can be a preferable alternative to formal amalgamation because it does not lead to excessive centralisation and preserves local cohesion and local democratic processes. As professional standards become stricter for people engaged in public administration, the importance of a sound training scheme for employees will become a bigger challenge for many local governments. Once again, finding a way to jointly deliver training can be an important step.

Swerea-MEFOS: Lulea, Norrbotten, Sweden. The Swerea Group is a public private partnership between the Swedish Ministry of Enterprise and Innovation (43% of Swerea AB) and five industry associations (57% of the company) that undertakes research and pilot development analysis for the member companies. The group has five branches with each one focused on the one of the five industry associations. Swerea-MEFOS focuses on metals and steel applied R&D to support the large primary steel industry in Norrbotten County and in other parts of Sweden. In 2015 funding came from industry (48%) national programmes (44%) and the EU (8%). MEFOS concentrates on metallurgy, developing pilot plant process technology, and energy and environmental issues for the metal industry. Some of its research is specific to particular company, but much of it is valuable to any company in the metals sector. This latter work has public good aspects which can justify government support. Swerea is majority owned by five trade associations, each of which represents a key sector in the Swedish economy. All these firms require steady improvements in technology to remain competitive, but a lot of this technology has public good attributes, which reduces the incentive for any single firm to fund it. The Swerea Group provides a solution to this dilemma by making its results available to member firms and undertaking research that is driven by member interests. Public funding is acceptable because the work benefits all firms, and indirectly strengthens the Swedish economy by making these firms more competitive.

Source: (OECD, 2017^[30])

Box 3.22. Entrepreneurship and innovation in rural areas

Innovation in rural areas relies to a great extent on the action of local entrepreneurs. While some innovations are imported from urban places either by the local branch plants of large multinational companies or by the transfer of ideas developed for initial use elsewhere, these innovations tend not to be fully embedded in the local economy. By contrast, innovations that come from local people are more likely to be based on better uses of local resources, or on new ways to solve problems for which an existing solution is not available.

The key issue for public policy is identifying ways to stimulate latent entrepreneurs to act on their ideas and to develop better support mechanisms for them when they do choose to act. There are two distinct motives for rural entrepreneurs that must be recognised. The first is a simple profit motive where the entrepreneur perceives that there is a current gap in the market that can be filled by his or her actions. The second is known as “user innovation”, where an individual has a problem in their life or business for which no adequate solution is available, so they invent one. It is only after the invention that the idea of becoming an entrepreneur occurs.

Essentially support for innovative rural entrepreneurs takes two forms.

The first entails ensuring that existing support for innovation does not discriminate against rural entrepreneurs. Forms of discrimination include: a focus only on formal innovation systems where science-based research and development activity is a prerequisite for support, focusing support only on innovations that have the potential for rapid growth (gazelles), requiring that an innovation be novel in a national or international context before it can be supported, establishing high minimum funding levels and complex application procedures that can be difficult for individuals or small firms to deal with, and concentrating efforts to promote innovation in urban areas.

The second is more broad-based support for small rural business, including assistance in moving from identifying an idea – the latent entrepreneur – to then acting on that idea and developing a business plan and to actually starting a business. In rural areas the first of the three steps can be the most difficult. In many rural areas there is not a strong tradition of entrepreneurship, and in almost all rural areas there are few peers who can be looked to by someone interested in starting an innovative business.

Financing a start-up can be a particular challenge in rural areas because the financial intermediation system is weak. Incomes are lower in rural areas, leading to less ability for the entrepreneur to raise equity funds from own sources or family and friends. Banks tend to be less capable of assessing business plans and are more risk averse. Start-up costs can be higher in rural areas because facilities may have to be constructed rather than rented and equipment must be imported. Mainstream venture capital is designed to bridge this gap but is primarily designed for high-growth/high-return ventures which are also not normally evident in rural areas.

Many rural areas have bridged this gap through the creation of community development finance institutions (CDFI) which provide revolving loan funds to local SMEs and start-ups. The initial capital for the institution may be raised from the local community, other financial institutions and government. CDFIs can be banks, credit unions, loan funds, microloan funds or venture capital providers. CDFIs are normally accountable to their local community and operate on a not-for-profit basis with legislative and funding support from governments.

Source: Elaboration based on US Treasury (2016), “Community Development Financial Institutions Fund”, www.cdfifund.gov/Pages/default.aspx (accessed 9 January 2016). (OECD, 2020^[22]).

Box 3.23. Promoting senior entrepreneurship: pointers for policy development

To increase entrepreneurship by older people, policy should:

1. Create a positive awareness of the benefits of entrepreneurship for older people among older people themselves, and in society in general.
2. Assist business start-ups by older people by supporting relevant business networks for older entrepreneurs and providing training to fill knowledge gaps on entrepreneurship skills for those who have spent their working life as employees.
3. Ensure that older entrepreneurs have access to financing schemes, recognising that some groups of older entrepreneurs (e.g. those starting a business while unemployed) may need start-up financing while others (e.g. those with high incomes) may not.
4. Highlight the possibility of acquisition, rather than start-up of a business, as a means into entrepreneurship for an older person as it may be quicker, less risky and can facilitate another person retiring who may wish to do so.
5. Encourage older people to play a role in promoting entrepreneurship by others by becoming business angels or by mentoring younger entrepreneurs.
6. Ensure that tax and social security systems do not contain disincentives to entrepreneurship for older people, including investment in other businesses.
7. Reduce the likelihood that a failed venture will leave the entrepreneur destitute – the risk of losing home, life insurance and other savings is particularly serious towards the end of one's career.

Source: (EC, 2012^[31]) Entrepreneurial Activities in Europe - Policy Brief on Senior Entrepreneurship.

Improving the rural labour force

With increased global economic integration, more developed economies lose their comparative in less-skilled activities over time making an upskilling of their work force imperative. Demographic decline is increasing the pressure to improve workforce skills to allow higher productivity to drive future economic growth. With fewer available workers appropriate policy responses are to increase the labour force participation rate, so that a larger share of potential workers are actually employed, and to improve skill levels to increase the productivity of those workers. Geographic differences in local labour markets between rural and urban places make it important that policies to accomplish these objectives reflect the differing conditions.

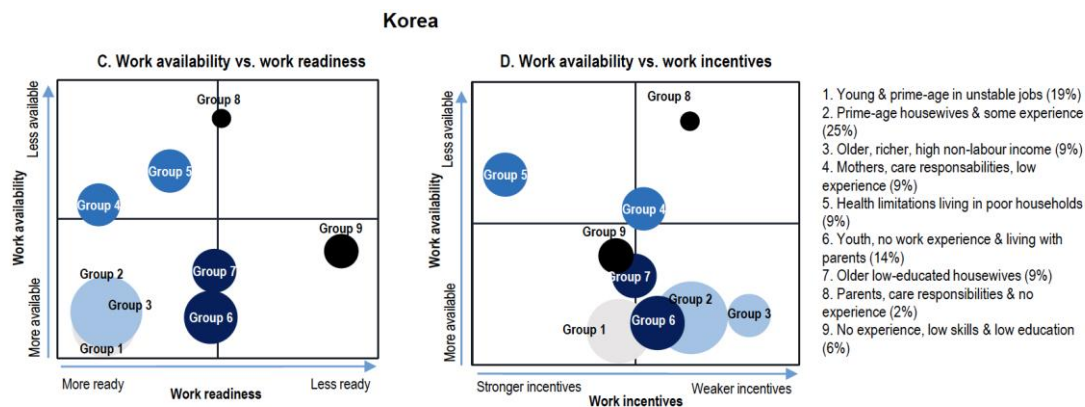
Figure 3.1, below, based on Fernandez, Hijzen, Pacifico and Theswissen, 2020, looks at two dimensions that affect participation rates – work readiness and incentives to seek work. The left side of the figure shows that in Korea there are 3 groups (5, 8 and 9) that will require additional support to improve their skills if they are to be employed. The right-side figure considers the incentives that people have to work. These can be considered as factors that affect the reservation wage, which is the lowest wage people require for their participation in the labour force. Many factors can affect work incentives: including high family income that reduces the need for another person to work, significant family responsibilities that have to be offset by hiring external help, or a lack of suitable work opportunities. In Korea, Group 2 (prime age housewives with some experience) is the single largest group with low incentives for work.

Typically, the idea of local labour markets is not extended to rural regions, even though the combination of long distance, low density and small local economies makes it difficult for many workers in rural regions to find work within a usual commuting range of under 1 hour. The cost of commuting in rural regions is also

an impediment to work especially for lower wage, lower skilled workers because public transport is not available. Even if people wish to relocate to another labour market, they may face difficulties in identifying employment opportunities or finding affordable housing. The result is a set of small weakly connected local labour markets distributed across rural territory with limited potential for people to Skill development within rural regions is particularly important because local labour markets are small and weakly connected. This can make it difficult to attract workers from other regions, and hard for people with skills that are not in demand to find work.

Given the anticipated worker shortages and evolving employer needs, efforts to match the development of youth skills with changing skill needs in the local economy is particularly important. In many rural regions boys often believe that formal skill development is not needed because they can obtain artisanal skills through on the job-training just as their fathers did. However even if jobs in the industries their fathers worked in are still available, it is likely that the skills workers today and tomorrow require are very different and are based on a strong formal education. For girls, the common experience is that they finish school with a strong education but find it difficult to obtain local work that offers an opportunity to use their skills. Consequently, young rural women have high propensity to move to cities, which reduces the size of the local labour force and has implications for future population growth. To retain these young women the economy has to evolve in ways that offer them better opportunities. Doing so should help both labour productivity and increase the potential for them to raise a family in the region.

Figure 3.1. Work availability vs work readiness and work incentives in Korea



Source: (Fernandez et al., 2020)^[32]

Improving the matching process may be the single most important element of labour force development in rural regions. With a small semi-autonomous labour force and an evolving set of job skill requirements a good matching process is needed to avoid unemployment and underemployment. At present, less effort is placed in formal matching processes in rural areas than in urban locations. This may reflect the slower pace of change in rural areas and the greater reliance on informal “word of mouth” recommendations. A smaller number of people also tends to increase the unit cost of a formal matching service because fixed costs must be spread over a small number of individuals. On the other hand, the costs of a poor matching process in rural areas are likely to be high, because workers can end up in sub-optimal careers harming both themselves and their employer, and ultimately weakening the community.

The combined effects of demographic decline and technological change are likely to increase the average skill requirements of most workers and to make ongoing training an integral part of a person’s career. This suggests that aptitudes should be identified fairly early in the educational process and potential career paths that match these aptitudes suggested to the individual. Certainly, individual interests and potential opportunities can change over time so flexibility is important. Further mid-career assessments and

supplemental skill development are likely to be increasingly important as technologies and production methods evolve. While these investments may be expensive the imminent scarcity of younger workers makes them essential.

Building rural communities capacity

Rural communities are small places but must still carry out most of the functions of larger places, although in different ways and with less complex procedures. These include providing public services, but also developing a strong civil society and supporting economic development. In larger communities most of these functions are carried out by paid professionals who work for the community. In smaller places some functions are carried out by paid workers, others by volunteers and others are not provided. Co-ordinating these tasks in a way that improves the quality of well-being for residents is a particular challenge for most rural places. (See for example the Comprehensive Rural Village Development Program in Korea, Box 2.9)

In general, rural communities face a shortage of leaders, who are often volunteers and who lack a background in public management or in other professions that would facilitate their role. In addition, in comparison to larger places, rural communities have a more limited capacity to influence their evolution. In most OECD countries rural places have a small tax base that is required to be spent on mandated services and very little other own source revenue. They are often too small to be eligible for some national government grants or programs and can lack the capacity to generate a strong application for those that they are eligible for. Local firms are typically too small and limited in number to be able provide much voluntary support to the community and there are few individuals with professional skills. Moreover, local financial institutions typically do not provide many functions beyond deposit taking and a limited range of consumer and business loans.

While some communities are able to manage to make significant progress over time despite these capacity constraints, others do not. This makes national government support for capacity building an important function. Various programs have been introduced across the OECD countries, such as LEADER in the European Union (Box 3.24) and Community Futures in Canada (Box 3.25), with the goal of strengthening local economic development. The hallmark of these programs is they provide a modest amount of money for a specific period of time to allow the recipient places to undertake a development activity that is both community defined and endorsed by a large share of the local population. As a result, not only does the community gain from the specific program, but it also benefits from a strengthened sense of cohesion and a recognition that positive change is possible.

Box 3.24. The European Union's LEADER approach

The acronym 'LEADER' derives from the French phrase "Liaison Entre Actions de Développement de l'Économie Rurale" which means, 'Links between activities for the development of rural economy'. It was introduced in 1991 by the European Commission in response to the failure of traditional, top-down policies to address problems faced by many rural areas in Europe.

The idea was to engage the energy and resources of people and local organisations as development actors rather than beneficiaries, empowering them to contribute to the future development of their rural areas by forming area based Local Action Group (LAG) partnerships between the public, private and civil sectors. These Local Action Groups are the main tool for the application of the LEADER approach to area development directly involving local representatives in the development and delivery of local strategies, decision-making and resource allocation. The added value of this approach is associated with local empowerment through local strategy development, delivery and resource allocation.

From 2007 LEADER was extended to fisheries policy and made a mandatory component of the EU's rural development policy. From 2014 the applicability of the LEADER approach was further extended as Community-Led Local Development (CLLD) in rural, fisheries and urban areas.

As LEADER has developed so too have the mechanisms to support the approach; formal networking structures through National Rural Networks and the European Network for Rural Development provide technical support and other networking services for LAGs. ELARD, the European LEADER Association for Rural Development, is an international co-operation forum of LEADER areas.

The LEADER approach or method is based on seven specific features and is dependent on all of these being present and employed together. These seven features define LEADER as a methodology and separate it from being simply a funding programme.

1. **Bottom-up approach.** The bottom-up approach is at the heart of LEADER. LEADER conceives that local people are the best experts to drive the development of their territory. This bottom-up approach means that the local community and local players can help define a development pathway for their area consistent with their needs, expectations and plans. Doing this through a collective approach with delegated decision-making enables them to take charge of their own area's future. They make decisions about the local strategy and the selection of the priorities to be pursued.
2. **Area-based approach.** LEADER and Community Led Local Development is based on a different way of doing things, linking the three elements of a local area, partnership and development strategy within a single approach. The area forms the basis for the development of the local partnership and strategy, creating a positive vision for what could be backed up by an active alliance of local stakeholders. Under the 'Area-based approach' the programme funding targets the priorities of the area as a whole, not specific projects or groups of projects (thus it is distinct from a 'project-based approach'). The area chosen must have sufficient coherence and critical mass in terms of human, financial and economic resources to support a viable local development strategy. The area must have clearly defined geographic but not necessarily administrative borders.
3. **The local partnership.** The local partnerships for area development work through a specific and structured governance mechanism referred to as the Local Action Group (LAG). Involvement in the partnership means that the people who were previously the passive 'beneficiaries' of a policy become active partners and drivers of their area's development; this is a defining characteristic of Community-Led Local Development. A LAG should comprise partners from public, private and civil society; it should be well-balanced and broadly representative of local interests and the different socio-economic sectors in the area. The LAG's legal form may vary from country to country, but it is often a non-profit, registered organisation.
4. **An integrated and multi-sectoral strategy.** The Common Provisions Regulation (EU No 1303/2013) specifies that CLLD be carried out through integrated and multi-sectoral area based local development strategies.
5. **Networking.** Networking lies right at the heart of what LEADER is and how it works. The LAG is a network of local partners which through its strategy and activities promotes links between local actors and others in the development chain. With the advent of CLLD wider networks involving links with non-rural areas can bring new possibilities.
6. **Innovation.** Innovation applies to what is done, the types of activity supported, the products or services developed etc. but importantly it also applies to how things are done.
7. **Co-operation.** Inter-territorial and international co-operation adds a wider dimension to local development in rural areas.

Source: EU Network for rural development, https://enrd.ec.europa.eu/leader-clld/leader-toolkit/leaderclld-explained_en.

Box 3.25. Community Futures Network (Canada)

Community Futures is a Programme which operates 267 non-profit offices across Canada that provide small business services to people living in rural communities. Each office delivers small business loans, tools, training and events for people wanting to start, expand, franchise or sell a business. Funding for Community Futures offices and the CFNC Network is provided by the Government of Canada's Regional Development Agencies. The Network is guided by a Board of Directors made up of Community Futures representatives from across the country.

CFNC provides a wide range of member services including specialised professional development and training. With the assistance of its Best Practices Committee, a key focus of the Community Futures Network of Canada (CFNC) is to gather and share information online on a wide variety of new and improved CF initiatives, processes and practices that will provide benefit to both staff and volunteers of CF/CBDCs across Canada. Through its national website, as well as its best practices portal (CFNCZone), the CFNC is able to offer easy access to a wide range of tools and resources that have been developed, tested and successfully utilised by local groups throughout the country.

Source: <https://communityfuturescanada.ca/>

Effective governance adjustments

The absence of an internal capacity to introduce new activities and create an effective program delivery mechanism is a crucial weakness of many rural local governments. While this weakness was less evident in periods of relative stability when the demand for new programs and new ways of delivering services was absent, the new environment of an aging population and rapid technological and social change is difficult for rural leaders to comprehend, let alone manage. Appropriate responses in rural regions are likely to be different from those adopted by metropolitan regions, which means that rural local governments will have to develop their own solutions for their specific situation. Associations of local governments can play a useful role in creating a forum for smaller regions to develop and share approaches. Funding from national and state/provincial governments to support these forums and build local capacity, as well as to help implement effective responses will also be important.

With demographic decline the capacity of smaller local governments to carry out existing responsibilities becomes questionable. Revenues will decline as responsibilities increase, because transfer payments are typically based on local populations and the local tax base will shrink as the economy contracts. The appropriate response is to explore some form of consolidation of local governments to achieve some minimum efficient scale. But consolidation in rural areas can often result in few cost savings because people are widely dispersed. Various studies across OECD countries show that forced municipal consolidation can lead to weaker local governments in terms of popular support and weaker social cohesion (Charron and Rothstein, 2018^[33]) (Dollery and Crase, 2004^[34]) (Douglas, 2007^[35]) (Zimmerbauer and Paasi, 2013^[36]). This in turn can make efforts to improve local economic conditions more challenging and exacerbate incentives for outmigration.

Building local support for collaborative development efforts can improve local governance and increase willingness for inter-municipal co-operation (Lackey, Freshwater and Rupasingha, 2002^[37]). Over a period of time the OECD Rural Programme has identified a number of useful policies and actions that both national and local governments can adopt to improve the performance of rural local governments. Most of these policies and actions are generally desirable, but in an environment of where demographic decline is

a major issue they can be particularly effective in helping facilitate a smoother transition to a new environment.

Consider new ways to deliver rural services

As noted previously rural locations often face difficulty in providing services to people and firms. Often, they are required by national or state governments to adopt specific delivery mechanisms that are designed to be effective in urban contexts, but which do not work well in a large area, sparsely settled, small population contest. If national and state governments adopted regulatory systems that focused on the desired outcomes from services, rather than on the specific service delivery mechanisms, then local providers could choose the most appropriate way to provide services in their specific context. Areas where this approach could be useful include; tele-health, tele-education and other internet-based approaches; but also, core infrastructure, such as water and waste-water treatment facilities, and solid waste disposal; and public transit. Delivering public and health services through a single site as is being done in France is a way to find new delivery methods (see Box 3.8).

Encourage collaboration with other proximate communities to deliver services on a regional basis as a way to provide services more effectively and reduce costs

Small communities in close proximity often fail to work together to produce and deliver services despite opportunities to reduce unit costs and improve quality. Barriers to collaboration take several forms. The first is a fear that a neighbouring place may benefit by hosting a specific serve for the larger group of settlements. Conversely, in the case of an undesirable facility, such as a solid waste disposal site, each community may fear it will be forced to accept others' waste. In addition, higher-level governments that either set regulations governing service provision or provide funding may not create incentives for collaboration. Finally, despite close physical proximity there is often little experience in local government collaboration. Each of these impediments is a significant barrier, but none is insurmountable, especially if national or state/provincial governments provide incentives to collaborate. The example of local authorities collaborating in Vaster-Norrland, Sweden described on Box 3.21 shows the benefits of collaboration.

Identify ways to determine which services it is essential to provide by government, and which might be provided by local NGOs or the private sector

Few governments consider the possibility of finding alternative providers of public services, despite the potential for significant cost savings and an opportunity to reallocate scarce public funds to higher priority actions. In rural areas local governments may be unable to provide services that are easily provided in a larger community because they lack funding or the ability to attract individuals with the skills to actually provide the services. However they may be able to provide equivalent services by relying on a different mechanism such as local volunteers, a private contractor or a sharing agreement with a number of nearby places in a similar situation. . Rural transport services are difficult to provide using conventional bus systems, but some form of public transit is essential in most rural areas. Box 3.26 provides an innovative example from Korea.

Box 3.26. The 100 Won Taxi

In many rural areas a large share of the population does not have ready access to a car and public bus service does not exist or is infrequent. This makes it difficult for people to shop, arrange medical appointments or visit friends. Where scheduled transport is not available many local governments have tried to implement service on demand programs. These programs are similar to a taxi service where vehicles are sent to a customer when they are required. But in rural areas distances are long and demand is infrequent and potential riders have limited income making it difficult to operate a conventional taxi company.

In Seochon County, Korea the local government established the “Taxi of Hope” program in 2013 to subsidise the local taxi company to provide service to rural residents. Each resident pays KRW 100 – about 9 cents (US) for a ride, with the balance of the cost of each trip paid by the county Government. The majority of the riders are elderly people who live in small villages with no local shops or other services. The taxi service allows them to remain in their homes reducing the need for assisted living facilities. Because the program was so successful it was adopted in many other rural areas in Korea and has received funding from the national government. In 2020 more than 2.7 million passengers used the service across Korea. Similar types of subsidised programs have been implemented in the Czech Republic, Switzerland, the United Kingdom and other countries.

Source: Choe Sang-Hun. 2021. It’s a Godsend: 9-cent Taxi Rides in Rural South Korea. NY Times Sept. 11 2021. available: Oct 19, 2021 <https://www.nytimes.com/2021/09/11/world/asia/south-korea-100-won-taxis.html>.

Ask for devolved authority from national/state governments to allow greater flexibility in how services are provided

National or state/provincial governments often mandate specific technologies or ways of delivering public services that they devolve to local governments. Typically, these rules specify best available technologies or specific levels of service to ensure uniform treatment across the entire jurisdiction. However, in many cases small communities are unable to meet the standards either because it is not technically possible or because the cost of compliance is too high. However it may be possible to provide similar levels of outcome by alternative delivery mechanisms if regulations are relaxed.

Seek greater own source funding sources to reduce reliance on transfer payments that have restricted uses

In most OECD countries local government have very limited revenue capacity and rely on “ear-marked” grants and transfers from higher levels of government to carry out their activity. This is a particular problem for small local governments in rural areas where transfer funds based on population do not go as far, because per capita service costs are higher than in more densely settled, higher population communities. A source of local funding is essential if these communities are to be able to make the locally specific investments that can enhance their productivity and attractiveness. In the European Union the LEADER programme has provided a new source of funding to rural areas that has allowed many regions to undertake new activities that could not be financed from national sources.

Recognise that good local services are a foundation for economic development because quality of life is important to firms and workers

Too often small places accept that they will not provide very high-quality services because they lack revenue or face high costs. But without a strong foundation of good services their economic future is perilous. Not only do they face difficulty in attracting outside investment, but they are likely to experience high rates of outmigration by young people who seek a better quality of life. Box 3.8 expands on this point.

Conclusions

Demographic decline is occurring at a time when the nature of work is changing to allow some individuals greater choice in where they work as a result of electronic communication. At the same time other individuals face more stringent conditions on where and how they work as technology better fuses human labour with complementary forms of mechanisation. COVID-19 has demonstrated the uneven nature of these changes with some individuals largely avoiding many of the impacts of the pandemic while working from home, while others were significantly exposed to the virus by virtue of their working conditions. In both cases, technology has changed the nature of work, but in some instances, it provides more flexibility, and in other it imposes more rigidities. Typically, higher skill workers benefit from increased flexibility, while lower skill workers increasingly work at a pace set by machines.

National demographic decline will not result in equal rates of decline across regions. Some regions may even grow in the short term if current migration patterns remain in place. This may lead to continued rates of outmigration from rural areas to large cities. However, within a few years, the population of rural areas will have shrunk considerably, and the age composition shifted enough that there will be few young people left. At this point cities, particularly those that have a very low local fertility rate, will experience a large decline in the number of new young workers.

Demographic decline may increase the number of workers having non-routine jobs, but only if the share of the labour force with advanced skill levels increases. For those with lower skills working conditions will remain difficult, even though wages may rise due to a reduced supply of labour. However, wages may not increase by a lot because higher wages create an incentive to adopt technology to reduce the number of workers required.

Efforts to increase the number of women in the workforce by increasing female participation rates are likely. But so too are efforts to increase fertility rates. Whether women working longer hours will be compatible with higher fertility rates will largely depend on the availability of cheap high quality childcare and society changing so that men provide a greater share of household responsibilities. Similarly increasing the share of women in paid work will reduce their ability to provide care for the elderly and ill, shifting these burdens onto paid providers.

Finally, a higher productivity labour force is generally seen as the best way to address an imminent worker shortage. But at least in the short run bringing more marginal workers in terms of skills into the labour force will tend to lower average productivity. And increasing the share of workers in child care and elderly care will also lower productivity unless the way we provide this care changes significantly to increase labour productivity.

In framing the next generation of sectoral policies, it will be important to link sector specific policies to the necessity to incorporate adaptations to demographic decline. This will require a stronger linkage to labour market development policy than has typically been the case, especially for skill development to allow fewer workers to be more productive. Because rural labour markets are, small, more specialised and only weakly connected to each other, different approaches will be required both for skill development and for matching firms and workers.

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Notes

¹ For more information see: <https://appalshop.org/story>.

² For more information see:

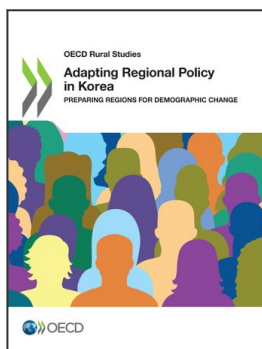
https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=&ved=2ahUKEwiiqd-n6dvzAhUTWs0KHxtMDaUQFnoECA8QAQ&url=https%3A%2F%2Fatenekom.eu%2Fwp-content%2Fuploads%2F2018%2F02%2F07_GovDay2018_Gotland.pdf&usg=AOvVaw2V8jTN_fBIhWJy_wz7pJPsg.

³ For more information see: <https://plunkett.co.uk/candover-valley-community-store/>

⁴ For more information see: <https://stories.coop/cooperatives/icoop-korea/>

⁵ For more information see: <https://www.localenergy.scot/projects-and-case-studies/case-studies/community-owned/greencraig-community-wind-turbine/>

⁶ . For more information see: <https://www.socialtraders.com.au/about-us>



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