2022 Synthesis Report
World Observatory on Subnational Government Finance and Investment

Highlights

SNGWOFI

World Observatory on Subnational Government Finance and Investment

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Foreword

The World Observatory on Subnational Government Finance and Investment (SNG-WOFI), the largest international knowledge repository on subnational government structure and finance, is a joint endeavour led by the OECD and UCLG (United Cities and Local Governments).

This third (2022) edition of the SNG-WOFI was supported by the Asian Development Bank (ADB), the European Union, the French Development Agency (AFD), the Council of Europe Development Bank (CEB), the French Ministry for Europe and Foreign Affairs, the German cooperation (GIZ), the Swedish International Development Cooperation Agency (Sida), the United Nations Capital Development Fund (UNCDF), and the DeLoG network.

The primary motivation for the Observatory is to increase knowledge and promote international dialogue and peer learning on multi-level governance and subnational finance, by collecting and analysing standardised quantitative data and qualitative information. Other objectives are to help monitor the contribution of subnational governments to the Sustainable Development Goals and other global development agendas.

More specifically, the Observatory has three key objectives:

- Ensure standardised, reliable and transparent access to data on subnational government structure, finance and investment.
- Support international dialogue and decision-making on multi-level governance and subnational finance.
- Serve as a capacity-building tool on subnational governance and finance at the international, national and subnational levels.

The ultimate goal is to support policymaking at all levels of government and help enhance multi-level governance and decentralisation frameworks, particularly fiscal ones.

This 2022 edition expands the country coverage and now includes data for 135 countries, covering 93% of global population and 94% of GDP.

The Observatory includes a fiscal database that covers dozens of indicators on subnational expenditure, investment, revenue and debt as of 2020, as well as on subnational government organisation and reforms as of 2021-2022. The website (www.sng-wofi.org) provides access to the database as well as a tool to compare countries across key dimensions.

The platform also provides country and territory profiles presenting multi-level governance and subnational finance systems in 135 federal and unitary countries. The profiles present structured and harmonised information on multi-level governance frameworks, territorial organisation, decentralisation and territorial reforms, subnational government responsibilities and subnational finance (expenditure, investment, revenue, fiscal decentralisation reforms and fiscal rules), providing a powerful and simple tool to analyse the relationship between political, administrative and fiscal decentralisation.

The 2022 edition includes specific foci on the territorial impact and management of the COVID-19 crisis and recovery, property taxation, subnational public-private partnerships, innovative subnational budgeting practices and an extended analysis for Least Developed Countries. Finally, the World Observatory also provides a synthesis report that presents the key findings of the 2022 edition.

Acknowledgements

The World Observatory on Subnational Government Finance and Investment (SNG-WOFI) is a joint initiative launched by the OECD Centre for Entrepreneurship, SMEs, Regions and Cities (CFE), led by Lamia Kamal-Chaoui, Director, and UCLG (United Cities and Local Governments), led by Emilia Saiz, Secretary General. The World Observatory supports the work of the OECD Regional Development Policy Committee (RDPC), its Expert Group on Multi-Level Governance and Public Investment as well the OECD Network on Fiscal Relations across Levels of Government. It also feeds into UCLG's research and policy work on local democracy and decentralisation, notably through the Global Observatory on Local Democracy and Decentralisation triennial report, as well as yearly reports to the UN High Level Political Forum on the localisation of the Sustainable Development Goals.

For this 2022 edition, the third after the 2016 and 2019 editions, the OECD and UCLG would like to thank their partners – the Asian Bank of Development (ADB), the European Union, the French Development Agency (AFD), the Council of Europe Development Bank (CEB), the French Ministry for Europe and Foreign Affairs, the German Corporation for International Cooperation (GIZ), the Swedish International Development Cooperation Agency (Sida) the United Nations Capital Development Fund (UNCDF), and the DeLoG network – for their invaluable support.

The 2022 edition (available at http://www.sng-wofi.org) comprises 135 country and territory profiles, a database with data on territorial organisation and subnational government finance, a visualisation tool ("Compare your country") and a synthesis comparative report that presents the key findings of this third edition.

At the OECD, the 2022 edition of the SNG-WOFI was co-ordinated by Isabelle Chatry, Head of the Decentralisation, Subnational Finance and Infrastructure Unit, Margaux Vincent and Charlotte Lafitte, Policy Analysts, under the supervision of Dorothée Allain-Dupré, Head of the Regional Development and Multi-Level Governance Division at CFE/OECD. At UCLG, co-ordination was conducted by Serge Allou, Special Advisor, Mathilde Penard and Paloma Labbé, Policy Officers.

The OECD developed the overall methodology and templates for the data collection and country and territory profiles. The OECD also collected data and prepared 75 country and territory profiles (including OECD and EU countries, OECD partner countries, Balkan countries, and countries from Asia Pacific, Northern Africa and the Middle East and West Asia), developed the database and web platform, and provided quality control for all the country and territory profiles. UCLG collected data and prepared country and territory profiles for 60 countries from different regions of the world, in particular Africa, Latin America, Euro-Asia and Middle East and West Asia. UCLG also provided comments and inputs on the methodology, templates and the synthesis report. It also translated the methodological guide and the templates for data collection from English into French and Spanish.

Synthesis Report

The synthesis report was co-ordinated by Isabelle Chatry, under the direction of Dorothée Allain-Dupré. It was drafted by Miquel Vidal-Bover, Isabelle Chatry, Charlotte Lafitte and Margaux Vincent with valuable contributions from Courtenay Wheeler, all from the CFE/OECD Secretariat. Statistical analyses were conducted by Miquel Vidal-Bover. The report benefitted from comments from Nadim Ahmad, Deputy Director of CFE. It was reviewed by Serge Allou, Kader Makhlouf and Paloma Labbé from the UCLG World Secretariat and by Christel Alvergne, Nan Zhang and Mkhululi Ncube from UNCDF (Chapter 5 on Least Developed Countries). Paloma Labbé also provided country examples to inform the report.

The World Observatory Steering Committee

The OECD and UCLG would also like to extend their gratitude to the World Observatory Steering Committee that gathers national governments, in particular members of the OECD Regional Development Policy Committee and the OECD Network on Fiscal Relations across Levels of Government, subnational governments, international organisations and networks, development banks and donors and think tanks. Putting multi-level governance into practice, the Steering Committee has followed and validated the different steps of the work.

The third meeting of the Steering Committee was organised virtually on 20 January 2022. The following institutions were represented and actively participated in the discussions:

- **Representatives of national governments:** Australia, Chile, Estonia, France, Italy, Poland, Sweden, and United Kingdom.
- **Representatives of subnational governments:** Antioquia, Colombia
- **Representatives of associations of subnational governments:** Council of European Municipalities and Regions (CEMR), Fonds Mondial pour le Développement des Villes (FMDV), Local Governments for Sustainability (ICLEI), Mercociudades, Metropolis, Network of Associations of Local Authorities of South East Europe (NALAS), United Cities and Local Governments Africa (UCLG-Africa), United Cities and Local Governments Asia Pacific (UCLG-ASPAC), United Cities and Local Governments Middle East and West Asia (UCLG-MEWA)
- **EU institutions**: European Commission (DG Regio), EU Committee of the Regions
- **International Organisations and institutions:** Congress of Local and Regional Authorities of the Council of Europe, Council of Europe, United Nations Capital Development Fund (UNCDF), UN-Habitat.
- **Development banks and co-operation agencies**: African Development Bank (AfDB), Agence Française de Développement (AFD), Asian Development Bank (ADB), Council of Europe Development Bank (CEB), Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ), European Investment Bank (EIB), Inter-American Development Bank (IADB), World Bank.
- **Foundations, institutes, and other networks**: DeLoG Network, Lincoln Institute of Land Policy, Local Government Revenue Initiative – University of Toronto, Local Public Sector Alliance, Cities Alliance and individual academic experts.

Highlights

Over the past four decades many countries have undergone multi-level governance reforms to improve their institutional, territorial and public management frameworks. In many countries, this has also translated into reforms that devolved powers, responsibilities and resources to subnational governments. This process of decentralisation has seen subnational governments assume responsibility for many core service and infrastructure provision responsibilities, including areas that are essential for development, such as education, social protection, health, economic development and environmental protection. In turn, they are playing an increasingly significant role in public spending, investment, and revenues but also in addressing significant socio-economic challenges, crises and megatrends.

This was starkly illustrated in the wake of the COVID-19 pandemic, which put subnational governments on the frontline of crisis management. More recently, just as they were beginning to support an inclusive, resilient and sustainable recovery from the pandemic, they have been hit by the profound global economic shock that has reverberated from Russia's large-scale aggression against Ukraine. Whilst this is first and foremost a humanitarian crisis it has also precipitated an energy crisis and, in turn, a cost-of-living crisis.

Compared to OECD forecasts from December 2021, global GDP is now projected to be at least USD 2.8 trillion lower in 2023 (OECD, 2022[1]). In many economies, inflation in the first half of 2022 reached levels not seen since the 1980s, and those pressures are broadening beyond food and energy prices, with businesses passing through higher energy and transportation costs, as well as rising labour costs from tight labour markets to a broad range of consumer products. For subnational governments, higher rates of inflation, and indeed higher borrowing costs will put further pressure on fiscal spaces, which were already being squeezed by the pandemic, and in turn put pressure on their ability to deliver essential services and critical investments, in particular those that can drive inclusive digital and green transitions and deal with asymmetric subnational impacts. Understanding the scale of that fiscal space, the multi-level governance frameworks within which subnational governments operate, and the scope and need to address funding and financing challenges, is a pre-requisite to address the legacy of the COVID-19 crisis, the crisis precipitated by Russia's aggression, megatrends, as well as persistent and long-standing spatial inequalities and disparities.

This third edition of the OECD/UCLG World Observatory on Subnational Government Finance and Investment is a powerful evidence-based resource that can help drive that understanding and, in turn, address those challenges. In addition to its rich internationally comparable data and analysis for 135 countries, it provides insights into ways to strengthen the resilience of subnational public finance and provides a specific focus on the impact of the pandemic on subnational governments, the territorial dimension of recovery plans, property taxation systems, innovative subnational budgeting practices, subnational public-private partnerships, and a special chapter dedicated to 31 Least Developed Countries.

The fiscal impact of COVID-19 has been asymmetric between and within countries

- **The fiscal impact of COVID-19 has been asymmetric both between and within countries**. Urban and rural regions, capital cities, metropolitan areas, larger and smaller municipalities and rural areas have all shown differentiated impacts from the pandemic. Moreover, their geographical location, their participation in global value chains and exposure to tradable sectors as well as their subnational finance profile have determined the size and nature of COVID-19 effects. For example, compared to interior regions, the public finances of coastal regions in Spain and Italy suffered an intense blow due to the travel restrictions and the closure of hotels, thereby reducing tourist flows, which is one of their main sources of subnational revenue.

- **The pandemic has prompted debate on how to reform multi-level governance systems so that they are better able to manage crises and emerging risks.** Multi-level governance frameworks were put under considerable stress by the pandemic. Highly decentralised systems were stressed by significant co-ordination challenges, while highly centralised systems experienced a lack of flexibility and room for manoeuvre to experiment at the local level. The pandemic re-emphasised the importance of effective intergovernmental co-ordination for crisis management. In some countries, subnational governments have been able to foster co-ordination by involving subnational governments and other stakeholders in the design and/or implementation of their response, usually by setting up or reactivating joint inter-governmental fora. In addition, the rigidity or ambiguity of multi-level governance frameworks have in some cases hampered or paralysed concerted action, underlining gaps that limit the emergence and the effectiveness of vertical and horizontal co-ordination.
- **The COVID-19 pandemic has led many subnational governments to experience, to different degrees, a "scissors effect" of simultaneous rising expenditure and dropping revenue.** The size of this effect is contingent upon the level of decentralisation as well as the five main differentiating factors of the subnational finance system in place, including the spending responsibilities and the resources to fulfil them, the degree of diversification and stability of revenue sources, the fiscal health of each subnational government prior to the pandemic, the flexibility or suspension of fiscal rules, and the scope of solidarity mechanisms such as equalisation policies. The scissors effect has also been reduced in countries where central governments have propped up local finances (see below).
- **More decentralised countries have seen subnational government expenditure increase between 2019 and 2020 as a result of COVID-19.** Although this varies significantly across countries, subnational expenditure increased on average by 2.6% in real terms between 2019 and 2020 for 61 countries. On the other hand, the sample includes a minority of countries that have opted to re-centralise tasks that were once subnational responsibilities, thereby leading to an increase in central government expenditure and a decrease at the subnational level.
- **Between 2019 and 2020, the increase in subnational spending in 61 countries** was mainly due to the increase in current expenditure (2.7% on average in real terms), with almost no increase in capital expenditure. Current social expenditure ballooned by up to 4.0% in real terms on average in 53 countries and so did subsidies and current transfers by 24.0% in 56 countries as a result of COVID-19 response measures that were implemented. By contrast, subnational direct investment on average in 56 countries decreased by 0.4% in real terms, with 28 countries experiencing increases and the remaining 28 experiencing decreases.
- **To counter the impact of the crisis on subnational expenditure, central governments adopted a range of measures** such as supporting temporarily some spending costs (e.g. credit interests), granting subnational governments a grace period for debt repayment, or easing spending responsibilities devolved to subnational governments. Fiscal rules have also been temporarily eased for subnational governments in several OECD and EU countries in 2020, lifting expenditure ceilings for coronavirus-related operating expenditures and investments.
- **On the revenue side, subnational revenue fell in a great number of countries in 2020 around the world.** The extent of the impact however varies across countries, depending in particular on the capacity of central/federal governments to step in to support subnational finance. In several

countries, the drop in taxes and user charges and fees was compensated by an increase in inter-governmental transfers and the support of emergency and compensation funds. For example, while subnational tax revenue decreased by 5.0% in real terms between 2019 and 2020 on average in 58 countries and user charges and fees decreased by 10.4% on average in 59 countries, these drops were compensated by a strong increase (10.4%) of grants and subsidies on average. Accordingly, total subnational revenue relatively stable, with an increase of 0.6% on average in 61 countries in 2020 compared to 2019.

- **Other revenue-side measures** included tax measures (shared and own-source taxes) and the activation of rainy-day funds and fiscal reserves. In some countries, equalisation and stabilisation mechanisms have also mitigated the differentiated impact of COVID-19 among subnational governments.
- **Debt borrowing rules have generally been relaxed** to facilitate the use of debt for short and long-term needs, especially for subnational governments whose fiscal health prior to the pandemic was already struggling. Countries around the world have also reduced their debt burden, set up credit lines, developed access to long-term borrowing and capital markets and/or established municipal liquidity facilities. On average, total outstanding debt in 47 countries increased by 7.6% in real terms between 2019 and 2020 and total financial debt (currency and deposits, loans and bonds) also increased by 9.7% in 46 countries.
- **Subnational governments play an active role in the COVID-19 recovery by being key recipients of stimulus funds and designing their own place-based recovery plans.** These often contain social and green objectives that consider the social and economic shocks on local economies. This is particularly the case in EU countries, where 37% of the Recovery and Resilience Facility in EU countries is allocated to climate action.

Resilience of multi-level governance and finance frameworks needs to be boosted to cope with recent shocks and future crises

- **The COVID-19 crisis has generated momentum for central/federal and subnational governments to rethink their multi-level governance frameworks.** The crisis has highlighted the need for a place-based approach to crisis management and recovery and stressed the importance of having an effective multi-level governance system based on flexibility, adaptability, co-ordination, and consultation across and among levels of government. Regular multi-level and multi-stakeholder dialogue, when using shared evidence as well as embracing a forward-looking perspective, can be particularly helpful to avoid fragmented policy responses.
- **For subnational resilience to be enhanced, multi-level governance frameworks must strike a balance between the responsibilities and the resources available to subnational governments, to avoid underfunded or unfunded mandates.** Balancing decentralised responsibilities and sources of funding is key to setting up a resilient subnational finance system. The crisis has revealed that having a diversified funding system based on a basket of revenues made of grants (for delegated functions or priority objectives), tax revenues, tariffs and fees and property income also diversifies risks and contributes to coping better with external shocks. It also makes the continuity of public service delivery more likely during a period of crisis.
- **Flexible and efficient horizontal or vertical equalisation mechanisms help mitigate the territorially differentiated impact of a crisis.** In several countries the activation of equalisation mechanisms has alleviated the heterogeneous impact of the pandemic among subnational governments (e.g. Austria, Germany, Switzerland). However, equalisation mechanisms have not always had the expected effects, depending on equalisation formulas. Their effect could be limited,

as many equalisation systems are susceptible to contractions in economic activity and may thus have a pro-cyclical impact on subnational finance.

- To prepare for the next exogenous shock, **fiscal space will need to be rebuilt**. This is particularly challenging in a context of rising interest rates and consolidation of public finance. However, the overhaul of subnational finance systems should lead to the establishment of stabilisation mechanisms, such as rainy day funds and reserves funds, which accumulate reserves in periods of growth and disburse them in times of fiscal stress to compensate for declines in subnational revenues. This has been the case in Japan, Mexico, and the United States.
- **Given the tight fiscal space after COVID-19, facilitating access to external financing for subnational governments to provide quality infrastructure investments is key.** This requires an enabling environment created by flexible and adaptable multi-level governance systems that can effectively identify innovative funding and financing sources, including external sources and private sector collaboration (OECD, 2022[2]).
- **Gathering reliable data on subnational government finance is vital for central and subnational governments to assess the strengths and weaknesses of their public finances as well as to better anticipate external shocks and build their resilience to counter them.** However, in many countries especially in Africa, Asia Pacific and Latin America, subnational government finance data are not regularly updated, hard to access and not publicly available.

Subnational government structure and organisation around the world

- **The study has identified 663 639 subnational governments** in the 135 countries included in the database. This includes 648 741 municipal entities, 12 385 intermediate governments and 2 513 state and regional governments.
- **Nearly half of the countries in the sample (61 countries) have both a municipal and regional level.** In 38 countries (i.e. 28%), there is only a municipal level. In 36 countries (i.e. 27%), there is an intermediate level between municipal and regional levels.
- **Decentralisation frameworks have continued to evolve in many countries across the world.** Many of them have been reformed to allocate responsibilities across levels of government more clearly and to assign the corresponding necessary funding to fulfil them (e.g. 3DS reform in France in 2022, Ghana in 2020). Avoiding the emergence of unfunded or underfunded mandates (i.e. the mismatch between responsibilities and resources available) is of the utmost importance to create operational decentralised frameworks that ensure effective public service provision at the subnational level. For example, other countries, especially in Africa, have further reformed their decentralised systems to enhance democracy and citizen participation (e.g. Kenya, Uganda).
- **As countries decentralise, territorial reforms such as municipal amalgamations but also municipal partitions take place**. A large majority of municipal partitions can be found in the regions of Africa and the Middle East and West Asia, mostly to respond to demographic changes in certain regions and/or municipalities but also partly as the result of on-going processes of decentralisation. In turn, municipal mergers are more common in Europe and Euro-Asia where municipal mergers are often encouraged through fiscal incentives in an attempt to benefit from economies of scale, efficiency gains and cost savings. Whilst these gains may indeed materialise, mergers or partitions are not a panacea to generate local economic growth and depend on factors such as the size of amalgamated territories, the technical capacity of local administration and the active involvement of local government decision-makers and all local stakeholders from the beginning of the amalgamation or partition process.

- **As an alternative to mergers, many countries are implementing inter-municipal co-operation in widely diverse forms**, from the softest ones such as co-operative agreements to the strongest forms of integration, such as supra-municipal authorities with delegated functions. This enables municipalities, both in rural and metropolitan areas, to benefit from economies of scale and scope. Inter-municipal co-operation is particularly beneficial in enabling small municipalities with scarce public resources to efficiently deliver quality public services and infrastructure. Metropolitan governance reforms are one particular form of inter-municipal co-operation. Effective co-operation between municipalities within metropolitan functional areas has become a priority topic in many countries, especially those confronted by a high level of urbanisation and administrative fragmentation.
- **Regionalisation reforms continued apace, driven by multiple factors (economic, political, cultural, etc.),** especially in the OECD and Europe, but also in Asia, America and to a lesser extent Africa. Several countries are creating a new decentralised regional level (e.g. Chile, Finland, Morocco, Ghana, etc.) while others are improving the governance of the regional level (France, Greece, Lithuania, etc.). Currently, several countries are debating regional governance reforms – debates that have been either stopped or, on the contrary, reinforced with the COVID-19 crisis (e.g. Bulgaria, Portugal, United Kingdom, Senegal). Regionalisation reforms also take the form of territorial reforms, such as regional mergers (e.g. France, Norway).
- **Countries are increasingly adopting asymmetric governance arrangements**, at the regional and metropolitan levels. In other words, more and more countries tend to provide different political, administrative or fiscal powers to governments at the same subnational level (regional/state, intermediate or municipal). The objectives are to transfer more responsibilities or specific tasks to subnational governments with greater capacities, to recognise a different status for territories with a particular history, a strong identity or a particular geography or to protect and promote special rights, such as the special right of Indigenous Peoples to manage their own territory. Asymmetric regional governance appears more "natural" in federal countries but is growing in unitary countries. Asymmetric arrangements are increasingly being used for metropolitan governance to recognise the specificities of metropolitan areas and city-regions, in particular in large cities and capital districts.

Subnational government spending represents over 21.5% of total public spending around the world

- **In 2020, subnational spending accounted for 21.5% of total public spending and 8.3% of GDP on average for the 122 countries in the sample with available data.** In federal countries, subnational governments accounted for 41.9% of public spending or 16% of GDP. In unitary countries, subnational expenditure is slightly below the global average: 6.6% of GDP and 17.1% of public expenditure. Staff expenditure is the most important expenditure item accounting for 35.3% of subnational government spending in 2020. That confirms the important role of subnational governments as public employers.
- **Subnational spending has increased from 8.6% to 9.1% in terms of GDP whereas it has decreased from 24.1% to 23% in terms of total public expenditure,** when comparing the same 106-country sample of the previous edition of this report between 2016 and 2020 data. This may be explained by the decrease in the ratio of subnational expenditure to total government expenditure due to a global increase in total public spending to respond to the COVID-19 pandemic as well as the reorientation of public spending carried out at the central level during the COVID-19 pandemic. Since GDP has also fallen due to the COVID-19 crisis, the data reflect an increase on average.

- **The degree of subnational public spending varies greatly across countries,** depending on whether the country is federal or unitary, its size and territorial organisation, the degree of decentralisation and the nature of decentralised responsibilities (health, social protection, education, etc.**).** Denmark and Canada stand apart from the rest of countries in terms of their particularly high subnational spending as a percentage of GDP and of total public expenditure. In most federal countries, as well as in a few unitary ones (Finland, Japan, Korea, Norway, Sweden and Viet Nam), subnational governments were responsible for over 30% of public spending — accounting for between 15% and 30% of GDP in 2020. In general, high income countries tend to have a larger subnational share in total public spending than low income countries.
- At the other end of the spectrum, **there are 58 countries where local authorities have limited spending responsibilities** (less than 8% of GDP and 20% of public spending), mostly from Africa but also Latin America. In seven OECD countries, subnational government spending accounted for less than 5% of GDP in 2020 (Costa Rica, Ireland, Republic of Türkiye, Chile, Greece and New Zealand). Smaller and usually more centralised countries (e.g. Malta, Mauritius, Gambia, Eswatini, Dominican Republic) also tend to show rates of subnational government spending lower than 2% of GDP in 2020.
- At the global level, **education, general public services (mainly administration) and social protection are the primary areas of subnational spending as a share of GDP.** However, the main areas of subnational spending differ greatly across countries.
- **Subnational governments are increasingly using their budgetary policies as a tool to achieve their strategic aims, fulfil their climate objectives and increase citizen participation and transparency**. Although most budgetary policies are intended to reform financial management systems, innovative subnational budgeting policies (such as gender, green and participatory budgeting) are starting to emerge, mostly in decentralised and decentralising countries, as a tool for subnational governments to achieve environmental and climate objectives and increase accountability.

Subnational governments play a key role in public investment, but such investment remains low in many regions

- **Subnational governments have a key role to play in public investment. In 2020, subnational government investment amounted to 39.5% of total public investment** and the level of subnational investment exceeds 50% of total public investment in 29 countries, and even 65% in 14 countries (36 and 17 countries respectively in 2016), mainly in high and upper middle income economies. The share of subnational government investment is greater in federal countries, reaching 59%. Disparities across world regions are considerable: in Africa, subnational public investment represents less than 25% of total public investment, whereas it amounts to 47.2% in Asia Pacific.
- **However, compared to investments required to meet new-zero targets, the share of subnational public investment in GDP remains low in many countries.** Indeed, at a global level, over USD 95 trillion in public and private investment in infrastructure will be needed between 2016 and 2030 to sustain growth/well-being and help achieve the Sustainable Development Goals (OECD, 2017[3]). Subnational public investment represents only **1.5% of GDP** around the world. It accounts for even less in low income countries. In 2020, it accounted for 0.7% of GDP on average in Africa. It was comparatively higher in Latin America (1.1%) and over three times as high in Asia Pacific (2.4%).
- **In OECD countries, subnational public investment has increased on average between 2016 and 2020 from 620 to USD 845 PPP per capita in real terms, and from 13.1% of public investment in 2016 to 15.6% in 2020.** Nonetheless, this increase is expected to slow down after

2020, as the COVID-19 pandemic and other shocks that unfolded in 2022, such as the energy crisis (see above), recede.

- **Subnational public-private partnerships (PPPs) are being promoted in some countries as a means to stimulate subnational investment in tight subnational fiscal environments.** The use of this instrument is more widespread in federal rather than unitary countries. A large reliance on grants and subsidies as a main source of subnational revenue, the lack of supporting legal frameworks or technical skills are the main obstacles for subnational governments when seeking to implement PPPs. Yet, PPPs are not a magic bullet: they require the right capacities at the subnational level to be carefully designed and implemented at the right scale.

Subnational governments still depend largely on grants for more than half of their revenue

- **Subnational government revenue represents 25.9% of total public revenue,** i.e. 8% of GDP on unweighted average in the 122 countries included in the sample with available data.
- **Subnational revenue has increased** from 8.6% to 9.3% in terms of GDP and from 25.7% to 28.1% in terms of total public revenue, when comparing the same 104 country sample of the previous edition of this report between 2016 and 2020 data**.** This may be explained by an overall increase in grants from the central government to support subnational governments responding to the pandemic in 2020, as well as a drop in GDP.
- **Grants represent more than half (51.5%) of revenue of subnational governments, followed by taxes (31.5%), user charges and fees (10.3%) and property income.** In federal countries, the share of grants and subsidies in subnational government revenue is lower (44.9%), while it is slightly higher in unitary countries (53%).
- **Subnational government tax revenue accounts for 2.9% of GDP on average with large disparities across countries.** In 53 countries out of 116, it accounts for less than 1% of GDP and in 15 countries, it exceeds 8% of GDP, the highest levels being found in Canada, Argentina, Sweden, Denmark and Germany.
- **On average, subnational tax revenue represents 14.5% of public tax revenue**. In the People's Republic of China, Germany, Switzerland, Canada, Argentina and India, subnational governments account for over 50% of public tax revenue while in 45 countries, it is less than 5% of public tax revenue.
- **Subnational tax revenue encompasses both shared taxes and own-sources taxes**. However, the size of tax revenue *per se* is not indicative of the level of discretion that subnational governments can exercise over their tax revenue. Indeed, the extent to which subnational governments can set their tax base and rates varies across countries, thereby generating differences in tax autonomy at subnational level. Tax autonomy is lower with tax sharing arrangements (e.g. on personal income tax, corporate income tax, excise taxes or VAT) as tax rates are defined nationally as well as shares that are redistributed to subnational governments. It is greater with own-source tax on which subnational governments have a certain leeway with regard to setting the tax base or rate. However, this taxing power can also be regulated and restricted in some countries.
- **Property tax is a cornerstone of local taxation in many countries in the world**. At global level (87 countries), recurrent property taxes account for 0.7% of GDP, 34.1% of subnational tax revenue and 8.2% of subnational government revenue as an unweighted average. However, **the property tax, despite its merits as a local government revenue source, remains largely untapped in many countries**, especially developing countries due to obstacles related to its practical implementation, management and collection. In Latin America and Africa, the recurrent property tax

represents a high share of subnational tax revenue, but a very low share of their GDP. To further benefit from this important source of local revenue, many countries are undertaking reforms of their property tax systems. Some reforms have involved the valuation of the tax base (e.g. Kenya, the Philippines), the extension of the tax to new assets (e.g. Germany, Poland), the collection system, the improvement of cadastre systems and land registries (e.g. Angola, Cambodia, Italy).

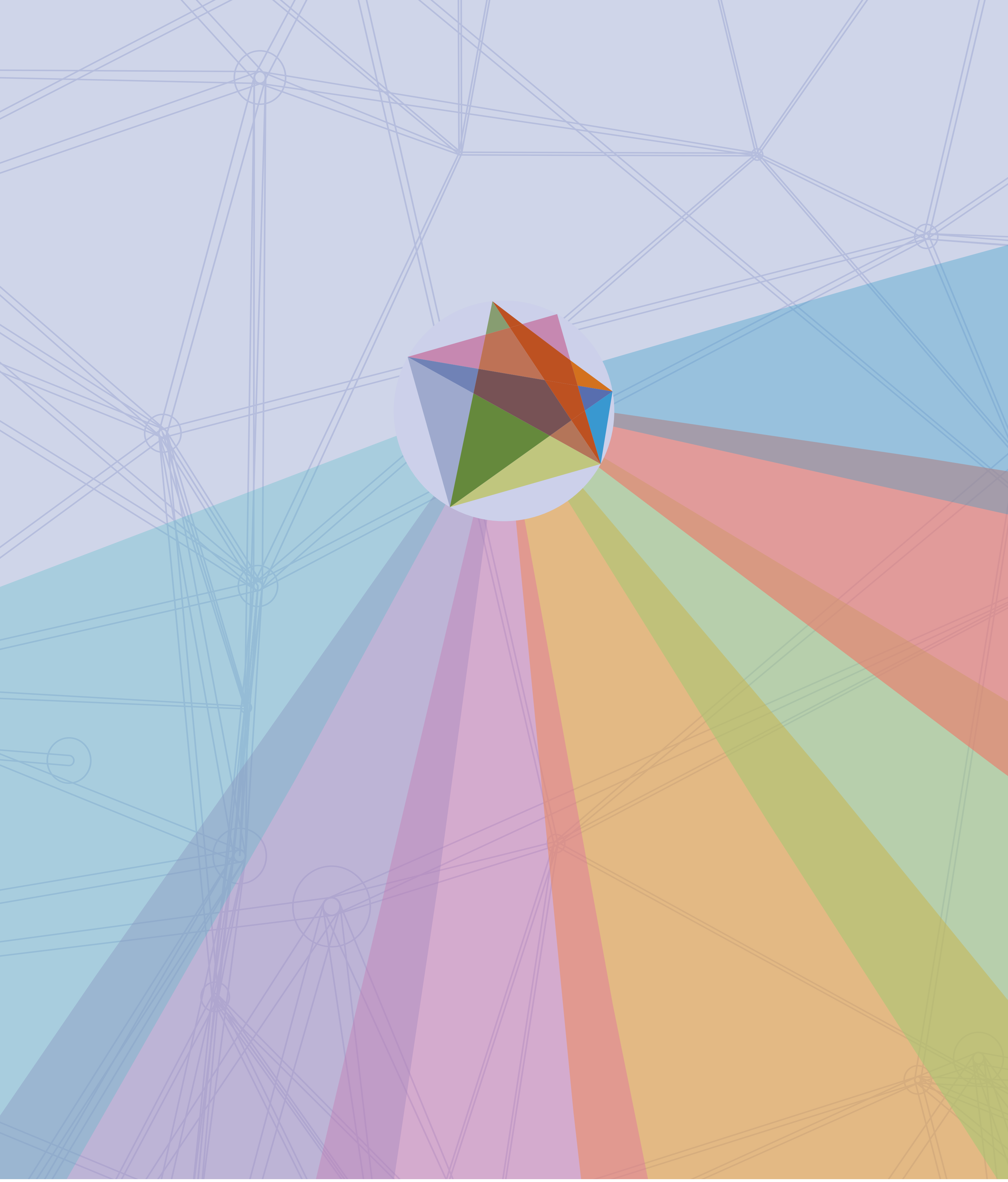
Subnational government debt remains low

- **Subnational outstanding gross debt is limited compared to central government debt** and accounted for 7.9% of GDP and 9.8% of total public debt in 2020 in the country sample (75 countries). It is very unevenly distributed among countries, ranging from almost no debt to debt reaching 75.8% of GDP and 53.6% of public debt as is the case of Canada.
- **Subnational outstanding gross debt has slightly increased from 7.5% to 7.9% in terms of GDP** whereas it has decreased from 11.5% to 9.8% in terms of total public debt, when comparing the same sample of the previous edition of this report between 2016 and 2020 data. A part of this increase in terms of GDP is driven by large COVID-19 support expenditures.
- **In 2020, subnational debt amounted to 20.3% of GDP and 22.7% of public debt in federal countries** while it accounted for 4.6% of GDP and 6.2% of public debt in unitary countries. Local government debt, when compared to state or regional government debt, is significantly lower in both federal and unitary countries, accounting for 4.5% of GDP and 6.1% of total public debt in 2020.
- **Loans make up the bulk of subnational government debt (53.4% of debt stock)**, followed by “other accounts payable” (29.2%) and “bonds/securities” (11.4%).

Least Developed Countries

- **The 31 LDCs in the database are mainly unitary countries, with the exception of Ethiopia, Nepal and Somalia.** Most of them have undergone decentralisation reforms in an attempt to pursue democratisation and enhance service delivery. Many countries have implemented a system falling between decentralisation and deconcentration.
- **LDCs are almost exactly divided among one-tier, two-tier and three-tier systems**. Different historical legacies as well as different geographies and land extensions have resulted in a wide diversity of territorial organisation and institutional structures.
- **Unclear divisions of responsibilities, unfunded or underfunded mandates, and lack of subnational government participation in programme budget processes** are issues that are particularly common in LDCs, even though these affect or have affected most countries included in this report.
- In many LDCs, **total subnational government expenditures accounted for a low share of GDP compared to the rest of countries included in this report**, i.e. less than 1% of GDP in 11 countries and between 1% and 3% of GDP for 6 other countries in 2020.
- **The role of subnational governments in public investment varies markedly across the 10 LDCs for which investment data are available**, from Nepal’s subnational investment accounting for over half of total government investment while it accounts for less than 10% of total public investment in Mali, Uganda, Senegal and Togo.

- **Subnational government revenues in most LDCs are limited compared to the rest of countries included in this report**. 15 out of 21 unitary countries have revenues that amount to less than 2% of GDP and 10% of general government.
- **LDCs are heavily dependent on intergovernmental transfers from the central government, both for federal and unitary countries**. Most low income countries also receive international aid and donations, most of which are channelled first through the central government. Tariffs and fees constitute a sizeable portion of subnational revenues in some LDCs, making up to a maximum of 41% of total subnational revenue. By contrast, tax revenue is rather limited.
- Although data in LDCs remains scarce especially for debt, borrowing is generally allowed at the subnational level to finance capital investments provided that prior approval is obtained from the Ministry of Finance. In practice, **even in countries where borrowing is legally possible, local debt is very limited**.
- **LDCs must improve the creditworthiness of their subnational governments** in order to expand their access to external financing at the subnational level and establish an enabling regulatory framework that allows them to borrow. This requires having sufficient and diversified sources of revenue. Once this is achieved, creative forms of finance can be envisaged, such as blended finance.



ADB ASIAN DEVELOPMENT BANK

AFD AGENCE FRANÇAISE DE DÉVELOPPEMENT

CEB COUNCIL OF EUROPE DEVELOPMENT BANK BANQUE DE DÉVELOPPEMENT DU CONSEIL DE L'EUROPE

DECENTRALISATION & LOCAL GOVERNANCE

Sweden Sverige

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