

Innovative infrastructure funding and financing in regions and cities: Unlocking investment in subnational government infrastructure during the COVID-19 recovery, and beyond

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Opening remarks

Ministers, Regional President, Mayors, G20 Delegates, Distinguished Guests, and Colleagues, it is my great honour and pleasure to present to you at this high-level conference on local infrastructure today.

As highlighted in the OECD's most recent economic outlook¹ — released last week — the global economic recovery remains strong, yet it is too uneven. COVID has had an uneven impact both across and within countries – this calls for stronger public investment in regions and cities.

Role of subnational governments

As major infrastructure operators and public investors – who are responsible for 59% of public investment in G20 countries² – regional and local governments have a core role in the recovery, but unlocking subnational government investment requires overcoming barriers to investment and supporting innovation in the use of funding and financing.

Today, I will draw on our upcoming report on *innovative infrastructure funding and financing*, prepared to support Italian Presidency of the G20, and present a few highlights from the report.

¹ OECD (2021) OECD Economic Outlook, Interim Report September 2021 : Keeping the Recovery on Track, <https://www.oecd.org/economic-outlook/>

² OECD (Forthcoming), Innovative infrastructure funding and financing in regions and cities: Unlocking investment in subnational government infrastructure during the COVID-19 recovery, and beyond.

Challenges faced by subnational governments

Subnational governments are *local* actors who have an essential role to tackle *global challenges*, including from COVID, climate change and demographic shifts. Through place-based policy and investment, they can address the tragic impact of COVID on local economies and communities.

The impact of the crisis has not been equal across regions. It has highlighted existing spatial inequalities in access to infrastructure – particularly in broadband and health care. In G20 countries, peak download speeds for broadband are 40 percentage points slower in rural areas than in cities³.

Subnational governments are also key actors to support the transition towards net-zero: In the OECD, they are responsible for 64% of climate and environment related public investment⁴. In addition, they have a key role to meet the challenges of demographic change and urbanisation by matching local infrastructure provision with expected population changes.

Globally, the OECD has forecast that the urban population will increase by 1.5 billion people by 2050⁵. This creates a significant need for new and upgraded infrastructure in many urban areas. At the same time, many rural regions are shrinking, and aging. In the OECD, 57% of regions will shrink by 2050⁶. This can reduce subnational government revenue, make it difficult to fund maintenance and means that existing infrastructure must be adapted to new needs.

Current economic stimulus

Current economic stimulus provides an important opportunity to partner with subnational governments to address these challenges. Globally, trillions of dollars of economic stimulus has been committed to support the recovery, much of which is for infrastructure, where subnational governments have a major role. Meeting the challenges I have outlined requires targeting public investments towards priority sectors, such as health, digital and low-carbon infrastructure.

It is critical that we learn from the 2008 financial crisis, which was followed by a sharp reduction in fiscal support for subnational governments. Public investment by subnational governments then stayed below 2008 levels for almost a decade⁷ – which reduced infrastructure investment and maintenance in many regions and cities. Although thus far during the COVID crisis, subnational governments have received substantial fiscal support, the outlook remains uncertain⁸.

³ OECD (Forthcoming), Synthesis report on existing digital divides

⁴ OECD (2019), “Financing climate objectives in cities and regions to deliver sustainable and inclusive growth”, *OECD Environment Policy Papers*, No. 17, OECD Publishing, Paris, <https://dx.doi.org/10.1787/ee3ce00b-en>.

⁵ OECD/European Commission (2020), *Cities in the World: A New Perspective on Urbanisation*, OECD Urban Studies, OECD Publishing, Paris, <https://dx.doi.org/10.1787/d0efcbda-en>.

⁶ OECD (2019), *OECD Regional Outlook 2019: Leveraging Megatrends for Cities and Rural Areas*, OECD Publishing, Paris, <https://dx.doi.org/10.1787/9789264312838-en>.

⁷ OECD (2020), *OECD Regions and Cities at a Glance 2020*, OECD Publishing, Paris, <https://dx.doi.org/10.1787/959d5ba0-en>.

⁸ OECD (2021), *The territorial impact of COVID-19: Managing the crisis and recovery across levels of government*, OECD Publishing, <https://www.oecd.org/coronavirus/policy-responses/the-territorial-impact-of-covid-19-managing-the-crisis-and-recovery-across-levels-of-government-a2c6abaf/>.

Framework conditions to support subnational investment

As we move beyond current stimulus, there will be an increasing need to overcome current obstacles. We identified four obstacles that can hold back subnational government investment and can limit the use of innovative funding and financing:

- First, that in some countries subnational governments may need to have a degree of fiscal space to fund investments.
- Second, that infrastructure investment requires specialist capabilities, especially to use innovative funding and financing instruments. Smaller subnational governments, in particular, often do not have sufficient investment expertise. In France, 80% of municipalities have less than 2,000 inhabitants, which limits their scale and ability to access to specialist knowledge, such as knowledge of project financing. This calls for capacity building, in particular from national governments. In 2016, only seven OECD countries had national infrastructure units with a mandate to strengthen the capabilities of subnational governments to run public-private partnerships and other infrastructure projects.⁹
- Third, that many countries do not have legal and regulatory frameworks to support the use of innovative funding and financing at a subnational level, permit the use of subnational public private partnerships, or support inter-municipal cooperation for joint investment projects.
- Finally, that infrastructure is a shared responsibility, so there is often a need for increased coordination across levels of government. In a survey conducted by the OECD and the Committee of the Regions of the European Union last year, 90% of 300 local and regional governments surveyed in the EU reported that coordination in the design and implementation of measures among all levels of government was the most important dimension for successful recovery strategies.¹⁰ In addition, local infrastructure projects can be fragmented across jurisdictions and lack economies of scale, as already underlined. Stronger cooperation among jurisdictions, in particular between municipalities, is needed to support investment at the right scale.

Funding and financing

Alongside improvements in framework conditions, subnational governments will need to innovate in the use of funding and financing. Improvements in framework conditions are pre-conditions for innovative funding and financing mechanisms to be mobilised.

To support subnational governments, we assessed 13 areas where funding and financing innovations can occur, highlighting innovations from G20 and OECD countries. We found that while many common and innovative funding instruments exist, they are often under-utilised by subnational government.

In our upcoming report, we seek to provide a full spectrum of funding options, from the “basics” – including as grants, taxes, and user charges – to more innovative approaches – such as land value capture, better using existing assets, and increasing asset revenue. For example, we identified interesting examples of land value capture mechanisms in Brazil, India, Canada, Germany or the United Kingdom, as well as practices of leveraging existing assets in Australia and China.

⁹ OECD (2016), *OECD Survey of Infrastructure Governance*, https://qdd.oecd.org/subject.aspx?Subject=GOV_INFREG (accessed on 28 September 2021)

¹⁰ OECD (2020), “The impact of the COVID-19 crisis on regional and local governments: Main findings from the joint CoR-OECD survey”, *OECD Regional Development Papers*, No. 05, OECD Publishing, Paris, <https://dx.doi.org/10.1787/fb952497-en>.

Choosing a funding source requires deciding who will pay for infrastructure – which is not an easy decision and has implications for accessibility. For example, while user charges mean that users will pay costs of infrastructure, in some cases these charges can also reduce accessibility for the most vulnerable in society.

We also covered financing innovations – including the use of loans, bonds, credit enhancement, and different types of finance providers or investors. Increasing subnational government access to finance through innovations is important to spread the high up-front costs of infrastructure investment over time.

Finance is often underutilised by subnational governments. Subnational government debt only represents approximately 20% of total government debt in G20 countries¹¹. In particular, the use of bonds by subnational governments, especially by municipalities, is limited in many countries. Bonds represent 23% of subnational government debt in G20 countries, but bond financing is very uneven in G20 countries at local level¹². It is quite widespread at subnational level in countries like the United States, Canada, Japan, Korea and Argentina. In several countries, the use of green and social debt financing is growing, and subnational governments are becoming increasingly active in this market, such as in France, Japan, Sweden and the United States. Subnational government bond issuance represented 6% of the total green bond issuances in 2020.

One interesting approach to improve access capital markets is the use of *subnational pooled finance mechanisms*, which include local government funding agencies and bond banks. These mechanisms have existed in Scandinavia for a long time, and are being increasingly adopted by countries such as France, Japan, the United Kingdom and New Zealand¹³.

When considering the use of funding and financing to support subnational infrastructure, it is important to note that funding is often the key barrier for subnational governments. Having sufficient funding essential to both pay for infrastructure and unlock the use of financing.

Conclusion

As we emerge out of this crisis, it will be important to support subnational governments to continue to make infrastructure investments. We think that this requires action in four areas:

- First, improving framework conditions for subnational government investment. This requires tailored approaches, adapted to each country's specific needs.
- Second, supporting subnational governments to adopt funding and financing instruments. We believe there is a need for policy toolkits targeted towards the specific challenge of subnational government funding and financing, which can bridge existing information gaps.
- Third, improving data related to subnational public finance and investment. In 2022, we will release the third edition of the World Observatory on Subnational Government Finance and Investment, which has data on over 120 countries.
- Fourth, better understanding the regional disparities arising from the COVID crisis, so that we can target investment to places most in need. We will soon release a Regional Recovery Platform to explore disparities in the impact of COVID on regions and monitor the regional dimension of the recovery, including for public investment.

¹¹ OECD (Forthcoming), Innovative infrastructure funding and financing in regions and cities: Unlocking investment in subnational government infrastructure during the COVID-19 recovery, and beyond.

¹² As above

¹³ OECD (Forthcoming), Innovative infrastructure funding and financing in regions and cities: Unlocking investment in subnational government infrastructure during the COVID-19 recovery, and beyond.

I would like to thank the Italian G20 Presidency for focusing on this important topic this year, and for hosting this high-level conference. I look forward to continuing this discussion on local infrastructure over coming years to improve wellbeing in all cities and regions. I look forward to hearing the panel discussions. Thank you.