OECD Regional Outlook 2023

The Longstanding Geography of Inequalities

Policy Highlights

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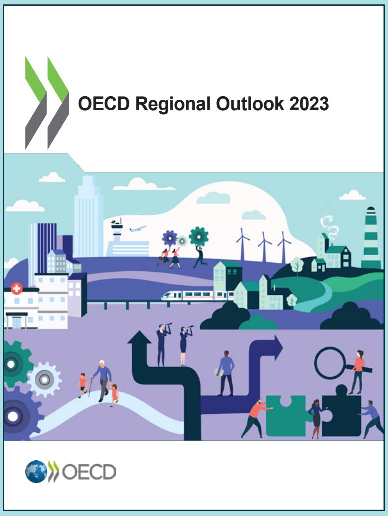
The Centre helps local, regional, and national governments unleash the potential of entrepreneurs and small and medium-sized enterprises, promote inclusive and sustainable cities and regions, boost local job creation, and implement sound tourism policies.

About this policy highlights

This booklet reproduces highlights from the report Regional Outlook 2023 – The Longstanding Geography of Inequalities, which provides novel insights on regional inequalities and challenges and opportunities for regional development. This report falls within the Programme of Work of the OECD Regional Development Policy Committee.

The report accessible at
OECD Regional Outlook 2023



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The twin shocks of the COVID-19 pandemic and the cost-of-living crisis unleashed by Russia's war of aggression against Ukraine have been felt unevenly across regions and come against the backdrop of two decades of persistent regional disparities. Large gaps in regional income are mirrored in other areas, including in access to infrastructure, and services, undermining life chances in many regions, and weighing down on their ability to narrow disparities. Indeed, in many countries, regional inequalities have grown.

With large metropolitan regions in particular pulling away, there are risks that, without action, smaller cities and rural areas may experience vicious cycles of stagnation and decline that are reinforced by megatrends such as the digital and green transitions and demographic, technological and geopolitical changes, generating unsustainable economic and social costs. Against this backdrop there is an urgent need to strengthen and adapt place-based policies to tackle these gaps and enable all types of regions to reach their full potential. And that potential is realisable.

Converging fortunes of countries and diverging fortunes of regions

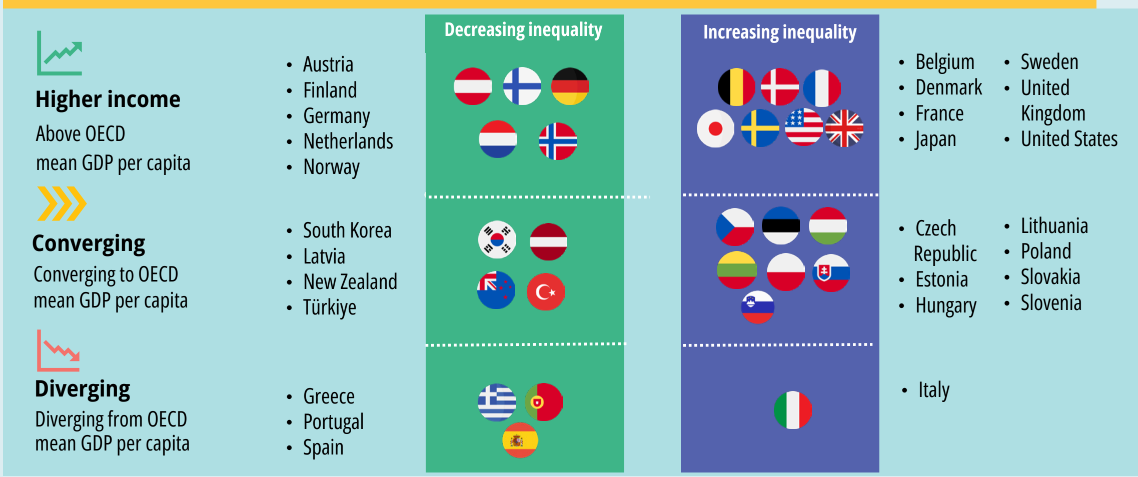
Several decades of convergence between countries have not created equal opportunities for all regions within countries. Over the last two decades, many lower income countries have been catching up to the OECD average: three quarters of OECD countries with GDP per capita below the OECD average in 2000 saw gaps between countries narrow over the last two decades.

While numerous regions within countries have benefitted from that process, across many OECD economies, income gaps between the most successful and least successful regions remained deeply entrenched. Across large (TL2) regions (e.g., states, provinces, landers) within countries, regional inequalities have barely changed over the last two decades. More alarmingly, at the level of small (TL3) regions – which are better aligned to the geographies where people live and work – spatial inequalities in income have widened in many countries over the same period. Over half of 27 OECD countries with available data saw income inequalities between their small regions increase between 2000 and 2020.

Overall, there has been a diverse evolution of regional income inequalities across OECD countries over the past 20 years, categorised by four broad trajectories:

- **High income / rising inequality**: Some countries with GDP per capita above the OECD average – including Belgium, Denmark, France, Sweden, the United Kingdom, and the United States – saw regional inequalities increase.
- **Rising income / rising inequality**: Many countries that have been catching up to the OECD GDP per capita average have seen their regional inequalities increase, including many OECD countries in Eastern Europe that grew quickly.
- **High income / lower inequality**: Other countries, including Finland, Norway, Germany, the Netherlands, and New Zealand, demonstrated that it is possible to sustain high GDP per capita while narrowing gaps between places.
- **Low growth / lower inequality**: Southern European countries like Greece, Spain and Portugal saw regional inequalities fall but in a context of weak overall economic performance.

OECD countries have seen different trends in regional inequalities over the past 20 years



Source: OECD Regional Outlook 2023, https://www.oecd.org/publications/oecd-regional-outlook-2dafc8cf-en.htm

In most countries, metropolitan regions continue to grow

Most metropolitan regions, both large and mid-sized, continue to benefit from agglomeration economies – advantages in productivity linked to size and proximity, including shared infrastructure, better matching of workers with jobs and knowledge spillovers – driving new opportunities and growth.

Metropolitan regions refer to small (TL3) regions where more than half of the population live in a Functional Urban Area. They are considered “large” if more than half of the population live in a (large) FUA of at least 1.5 million inhabitants; and “midsize” if more than half of the population live in a (midsize) FUA of at 250 000 to 1.5 million inhabitants. Other regions are considered non-metropolitan.

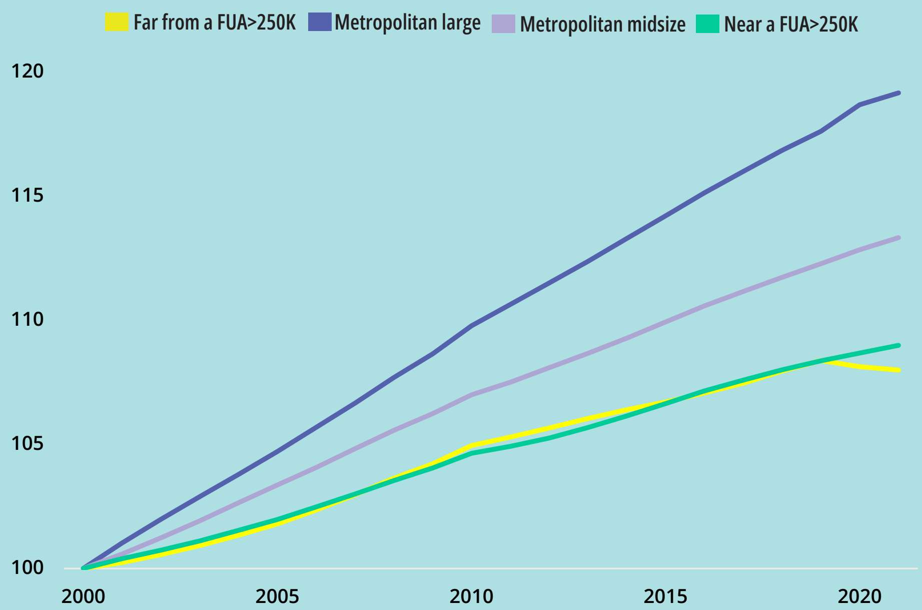
On average, metropolitan regions across the OECD had around 32% higher GDP per capita than other regions, and differences in GDP per capita between large metropolitan and other regions account for the largest share of regional inequality in most countries with large metropolitan regions.

Although many OECD countries were already highly urbanised, the share of people living in metropolitan regions has continued to grow in all countries except Greece over the last two decades. Population growth in metropolitan regions is partly driven by productivity advantages, but also the amenities they provide, including better access to public and private services, culture and social hubs and events, making investment in such amenities integral to their success. However, on average, among metropolitan regions, growth is being concentrated in the largest of these areas as they increased their population by 19% between 2000 and 2021, six percentage points more than in midsize metropolitan regions, and twice the growth of the rest of regions.

Yet while the largest metropolitan regions have benefited from stronger growth than other regions, they too are facing major challenges linked to their success – including in housing affordability, congestion, and, indeed, in inequality inside the regions.
In the 26 OECD countries with available data, capital-city regions were the most unequal of all places in terms of disposable income.

Large metropolitan regions saw the highest increase in population

Index of population growth in TL3 regions by type, 2000-21



Source: OECD Regional Outlook 2023, https://www.oecd.org/publications/oecd-regional-outlook-2dafc8cf-en.htm
Note: Based on 35 OECD countries with available data. Metropolitan regions are classified into metropolitan large, if more than half of the population live in a (large) FUA of at least 1.5 million inhabitants; and metropolitan midsize, if more than half of the population live in a (midsize) FUA of at 250 000 to 1.5 million inhabitants.

Many countries are likely to face shrinking populations

Source: OECD Regional Outlook 2023, https://www.oecd.org/publications/oecd-regional-outlook-2dafc8cf-en.htm
Note: Change is calculated as the difference between years over the initial value.

In half of the 26 OECD countries with available data, capital-city regions were the most unequal of all places in terms of disposable income. This emphasises the need to not only narrow gaps between the most and least successful regions but also for targeted spatial policies inside large metropolitan areas to prevent diseconomies of agglomeration, which can undermine performance.

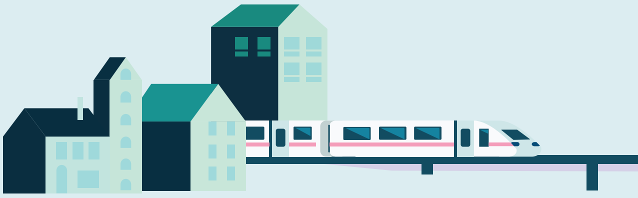
Growth in rural regions close to metropolitan areas lagged metropolitan regions since before the 2008 Financial Crisis. Even in regions far from metropolitan areas, which outpaced metropolitan areas in the years immediately after the Great Financial Crisis, disparities have grown again since 2013, partly reflecting internal migration as people have moved to cities. Stronger economic growth in these regions is crucial to rebuild the attractiveness of shrinking regions and, in turn, counter additional challenges around ageing.

Fourteen OECD countries are likely to experience declining populations by 2040 and 18 by 2100, with the largest decreases in Eastern and Southern European countries, Japan and Korea. They are already shrinking in many places, especially in remote rural regions: between 2001 and 2021, nearly 40% of remote regions in the OECD had shrunk. Remote regions also represent the highest share of regions with old age dependency ratios above 50% on average.

Shrinking is increasingly a problem for mid-sized and smaller cities as well as remote regions. Between 2001 and 2021, 22% of functional urban areas in OECD countries saw their population shrink and in 11 countries more than 40% are shrinking. In all cases, population shrinkage brings additional complications, undermining local public revenues while pushing up the costs of maintaining public services and infrastructure, with important implications for fiscal frameworks. It also generates a need to tackle issues of dereliction and blight, which can be costly to fix.

Yet within countries there are also many examples of non-metropolitan regions adapting to, and overcoming, challenges related to shrinking. In Finland and Germany, many shrinking remote regions recorded the highest growth rates in income per capita between 2001 and 2019, including through investment in more capital intensive production, helping to overcome labour supply challenges. In Estonia, Latvia and the US, non-metropolitan regions close to small and medium-size cities recorded the highest growth rates, and in Austria, Hungary, Korea, Portugal and the Slovak Republic, non-metropolitan regions close to a metropolitan region recorded the highest growth rates. In many cases, success in these areas has also been driven by their ability to capitalise on urban-rural linkages, “borrowing” agglomeration effects from nearby cities.
ability to capitalise on urban-rural linkages, “borrowing” agglomeration effects from nearby cities.

The geography of inequalities is multi-dimensional



Deep structural inequalities between places are stretching beyond economic outcomes, with impacts on broader well-being. Cities fare better across many areas, including access to talent and skills, but also access to infrastructure and services like health and education.

These gaps are all connected. When public services and infrastructure are of poor quality, it is harder for lagging regions to attract and retain the people, skills and investment needed to break a vicious cycle of stagnation and decline.

Health

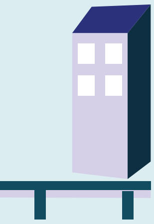
In OECD countries, travel times to healthcare facilities are obviously much larger – five times larger – in remote rural areas than in cities. This contributes to the fact that close to a third of rural residents in OECD countries reported health problems that prevented them from doing things people their age normally do compared to only a quarter of city residents. Moreover, the gap in the availability of hospital beds per capita between cities and remote regions – which stood at 50% in 2020 – has been increasing since the 2008 Great Financial Crisis. The number of hospital beds per capita in remote regions has fallen on average by 0.7% per year, while increasing in metropolitan regions. Bridging access gaps in places can however be achieved, for instance by offering different types of related services in a single location and expanding digital services such as telemedicine.

Skills & education

In many rural areas, residents struggle to access good education and training. Students in city schools obtained higher scores in reading than their peers in schools located elsewhere in all but two OECD countries with available data. Investing in quality transport infrastructure, especially public transport, is an important lever to improve access to education in rural communities, but the quality of schools also needs to improve in such areas to provide a platform for future growth, and to boost their attractiveness to potential new residents and investment.

Digital connectivity

Data from regulators in 26 OECD countries show a persistent rural-urban divide in connectivity speeds: on average a third of households in rural areas do not have access to high-speed broadband and only 7 out of 26 OECD countries have secured access to a high-speed connection for at least 80% of rural households. In Mexico and Canada, people in rural areas have connection speeds 40 percentage points slower than the national average. These gaps in digital access mean these areas will struggle to benefit from new remote working and telemedicine opportunities that could help them compensate for a lack of physical connectivity to jobs and services, and, moreover, stifle entrepreneurship and potential investment.



Service gaps undermine productivity, creating vicious cycles of stagnation and decline

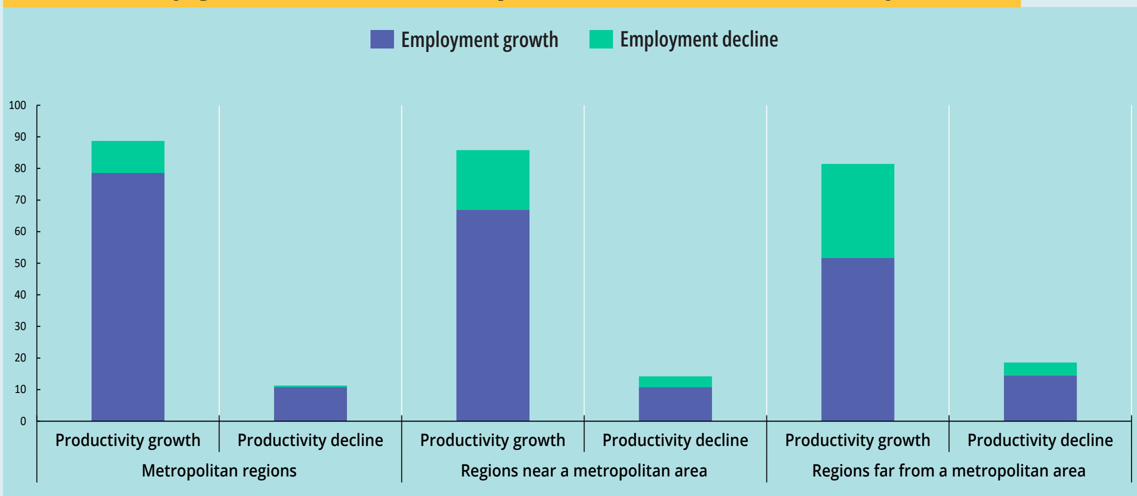
Gaps in access to services, infrastructure and amenities, weigh down on productivity in many regions, underpinning the longstanding geography of inequalities.

Whilst different sector specialisms partly explain productivity differences between regions, other factors, including differences in local infrastructure, skills, and investment, can lead to productivity gaps across regions. Indeed, 75% of productivity differences between firms occur within the same sector. This implies that place-based policies can play a significant role in driving productivity even without developing new industries and sector specialisms.

But higher productivity does not automatically translate into better employment outcomes in all types of regions. In recent years, similar shares of metropolitan and non-metropolitan regions have seen productivity growth.

However, while in urban areas productivity and job growth have typically gone hand-in-hand, in non-metropolitan regions a combination of automation and competitive pressures from lower-income economies have resulted in fewer regions generating jobs' growth as productivity has grown. At the same time, these areas have struggled to attract and retain the higher-skilled workers needed to develop new industries and opportunities for growth.

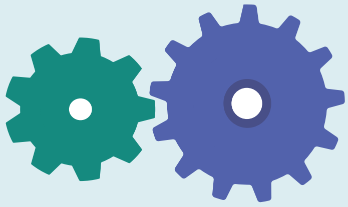
Productivity growth in non-metropolitan areas has been less jobs-rich



Source: OECD Regional Outlook 2023, https://www.oecd.org/publications/oecd-regional-outlook-2dafc8cf-en.htm
Note: Labour productivity is GVA per employee in USD at constant 2015 prices and PPPs. Countries included are AUT, BEL, CZE, DEU, DNK, ESP, EST, FIN, FRA, GBR, GRC, HUN, ITA, LTU, LVA, NLD, NZL, POL, PRT, SVK, SVN, SWE and USA. Growth rates for GBR are for the 2004-19 period.

Action on several fronts can help boost productivity. Place based policies to address skills, digital, infrastructure and communication gaps, as well as in access to finance, knowledge and innovation networks, and the quality of public services and local government can improve the attractiveness of all regions, and encourage inward FDI, and support businesses to invest, export, innovate or adopt innovations and scale-up. In addition, the net zero transition can offer new opportunities for regions to boost productivity (OECD, 2023), while remote working also provides potential to entice high skilled workers away from metropolitan regions to mid-sized cities.

The longstanding geography of inequalities is becoming too costly



The aggregate contributions of lagging regions and regions trapped in a vicious cycle of long-term stagnation or decline to national economies is important. Moreover, many of these areas are continuing to perform valuable economic functions upon which other places – and indeed countries – depend, including agriculture and industry. Neglecting these areas presents risks as well as a missed opportunity to make the most of untapped economic potential.

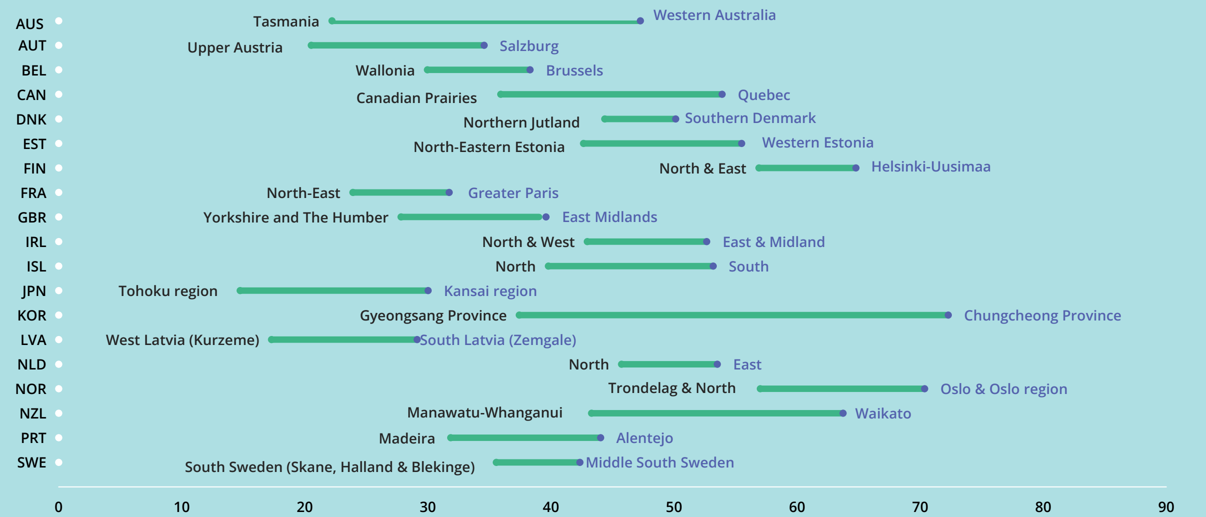
Better connecting these regions to well-functioning cities through urban-rural partnerships and unlocking their innovation potential are some of the ways to improve their productivity and competitiveness and make them motors of regional, and in turn national, development.

Evidence is mounting on the broad-reaching costs of failing to tackle regional underperformance. These include reduced employment and earnings, social mobility, and life satisfaction, and higher prevalence of welfare dependency and health issues. Persistent inequalities also challenge the capacity of subnational governments to provide adequate access to key public services and infrastructure. This is true in economically dynamic regions that may struggle to cater to the large numbers of people they attract and in lagging regions and/or those in decline where public services become stretched, of low quality or difficult to access.

The longstanding geography of inequalities is generating social tensions and large regional variations in trust in government. For example, regions with poor long-term economic outcomes often experience lower levels of government trust. This is also true in places that are still relatively well-off but that have seen their economic fortunes drop over time. These disparities in trust can generate disengagement, strain social cohesion and undermine democracy over time.

There are important regional disparities in trust in national government

% with the highest and lowest level of trust by country



Source: OECD (Building Trust to Reinforce Democracy: Main Findings from the 2021 OECD Survey on Drivers of Trust in Public Institutions, 2022), Building Trust to Reinforce Democracy: Main Findings from the 2021 - OECD Survey on Drivers of Trust in Public Institutions, https://doi.org/10.1787/b407f99c-en
Note: Proportion of respondents that "trust" the national government based on an aggregation of responses from 6-10 on the scale, based on responses to the question: "On a scale of 0 to 10, where 0 is not at all and 10 is complete, how much do you trust each of the following? The national government". "OECD" presents the unweighted average across countries. Finland's scale ranges from 1-10 and the higher trust/ neutral/ lower trust groupings are 1-4/ 5-6/ 7-10. New Zealand shows trust in civil service as respondents were not asked about trust in the national government (note that trust in civil service on average tends to be higher than trust in national government). Colombia, Luxembourg and Mexico are not shown due to data unavailability.

Building the resilience of all regions to face shocks and adapt to megatrends

Recent economic shocks have undermined prospects for many places, which also risk missing out on new opportunities arising from the green and digital transitions. During the COVID-19 pandemic, cities were more able to switch to remote working to protect jobs and businesses than rural areas, while recent rises in energy and gas prices have been particularly painful for rural regions, due to lower household incomes and savings, as well as higher fuel use. The experience of the Great Financial Crisis suggests that the impact of these shocks may be long lasting. Even on the eve of the pandemic, unemployment rates had not recovered in half of OECD regions.

Meanwhile, poorer regions are struggling to seize the new jobs and opportunities arising from the green and digital transitions. While around a third of jobs are greenin Stockholm, Luxembourg, Paris, London and Oslo, this share is far lower in poorer and remote regions, which also tend to host more polluting jobs at risk from the transition to net zero.

Similarly, poorer places are falling behind in the digital transition, due to a lack of digital infrastructure and skills. In Europe on average 66% of individuals in cities had basic or above digital skills, versus only 30% in rural areas

Policymakers need to work to build regional resilience to better prepare them for these transitions and the shocks that lie ahead. A strategic foresight exercise in this report for 2045 shows how better developed, more agile policy frameworks can be established to build the resilience of places to what lies ahead.

Three priority avenues emerge to future-proof regional development policy and build up resilience in the next 20 years

Fiscal systems & investments

National governments will need to ensure that subnational fiscal frameworks and grant allocation mechanisms are responsive to changes in local needs – including the increased costs of maintaining infrastructure and services and tackling dereliction in declining places. At the same time, they should allow all places to leverage private investment to finance supporting infrastructure (e.g., through land value capture mechanisms and public-private partnerships). Locally, subnational governments should also seek to broaden their revenue bases to better insulate their finances against shocks.

Governance

As places grow, shrink, and restructure in response to shocks and transitions, governance systems must continue to evolve. For example, in many countries, the geography of local administrations is slow to adjust to new economic realities, resulting in fragmented and inconsistent approaches across functional urban areas, and presenting a barrier to the rationalisation and consolidation of services in rural areas. Regular review mechanisms should be established to ensure that governance mechanisms remain fit for purpose.

Capacity

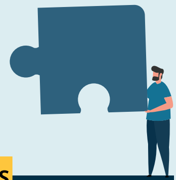
All places need to invest in the capacity to develop and implement coherent plans to nurture growth and navigate the green and digital transitions. However, the areas with the greatest need to set a new course are often those with the weakest capacities in key areas such as foresight, evidence gathering and analysis, planning, project management, finance and monitoring and evaluation.

Five policy priorities to address regional inequalities now and in the future

Place based policies must be strengthened to tackle the longstanding geography of inequalities and adapted to a new context of global shocks and transitions. Regions often struggle, not just on one front but on many.

Mitigating regional inequalities effectively while sustaining the prosperity of the most dynamic regions will require action across five complementary policy levers.

Five policy levers to mitigate regional inequalities



Ensuring equitable access to quality public services and infrastructure in all regions

Public programmes to boost economic competitiveness are likely to fail unless they first ensure that public services, infrastructure and amenities are of sufficient quality to attract and retain new, skilled workers.

Boosting productivity and competitiveness

Regions need to be well connected – to workers, international markets, ideas and the digital domain. Policies need to support these connections by providing the right infrastructure, advice and networks.

Providing the right skills and quality job opportunities in regional labour markets

Regions need to ensure that their workforce is well prepared for the world of work – now and in the future. Training, education and employment services need to work together with employers to anticipate local needs and skills gaps and encourage and support local entrepreneurship in emerging sectors.

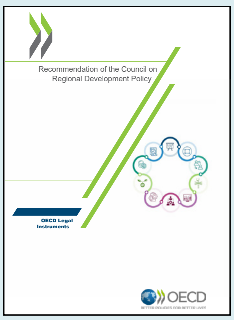
Improving the quality of multi-level governance systems

Governments must ensure that economic development responsibilities are well aligned with functional economic areas, and that there are structures in place to agree priorities across and between different levels of government.

Strengthening capacity at national and subnational level

Designing and delivering effective place-based policies require a range of skills, including in planning, management, and finance. Governments at all levels should regularly review capability, to identify and resolve capacity gaps in particular places and subjects.

Going forward, the **OECD Recommendation on Regional Development Policy** can serve as a compass to guide governments' efforts at different levels to promote and implement effective place-based regional development policy that improves the contribution of all regions to national performance and reduces inequalities between places and between people.



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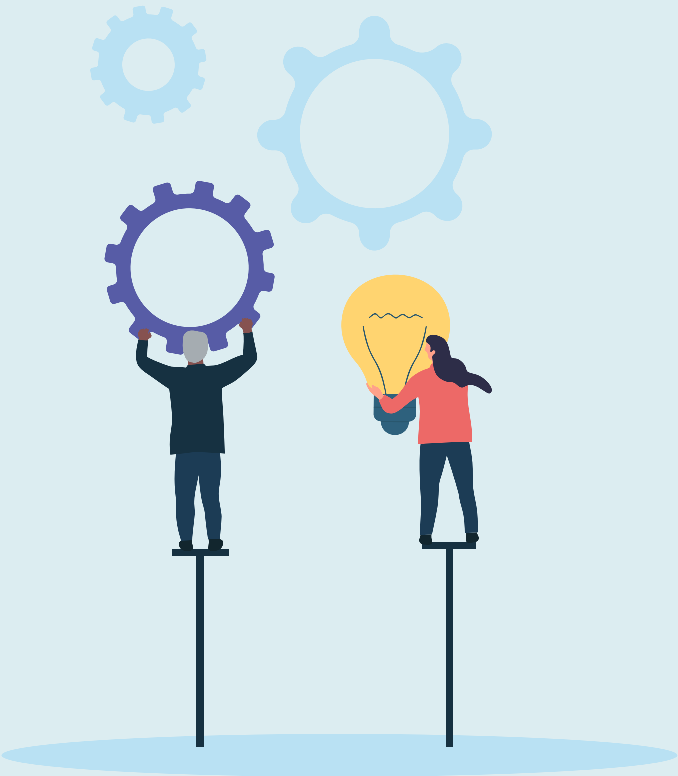

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