Subnational Government Finance and Investment Webinar
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Opening Remarks (Draft)

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Colleagues from the OECD and ADB, and dear participants

On behalf of the organizing team, I am pleased to deliver the opening remarks on this important topic "**Subnational Government Finance and Investment**". We all know that subnational governments play a key role in delivering important public services. About two-thirds of the 169 SDG targets involve subnational governments.[1] They also account for nearly a quarter of total public spending and more than a third of public investment. Education, social protection, health, and other public services are the primary areas of subnational government spending that link closely with the SDGs.[2] But these subnational governments face enormous challenge in undertaking their mandates mainly due to the weak institutional capacity and inadequate finance and investment among others. Enabling subnational governments to overcome the barriers to mobilize more revenues and access finance is therefore critical, and this calls for a multi-pronged and integrated approach.

The first and foremost is creating an "enabling environment" at the national and subnational government levels:

(i) ***Country or national level*** in terms of preparing national frameworks and institutions to support subnational government finance. It is important to ensure that these frameworks within which they must operate are consistent, and do not offer perverse incentives and undue discretion. It is also important to translate these frameworks and policies into clear operational guidance. Further, fiscal decentralization with clear demarcation of responsibilities and authorities of all government tiers is another important element. There is a broad agreement that many central governments, especially in lower- and middle-income countries,

[1] Jeffrey Sachs et al. 2019. Sustainable Development Report 2019. Transformation to Achieve the SDGs. New York.
[2] OECD/UCLG. 2019. 2019 Report of the World Observatory on Subnational Government Finance and Investment. Paris/Barcelona.

decentralize fewer revenue sources than is justified by fiscal principles and subnational needs. Central government should therefore consider delegating more revenue raising authorities to subnational governments with appropriate legislative and institutional frameworks, as well as technical assistance to strengthen their institutional capacity. ADB, through its ***Asia Pacific Tax hub***, stands ready to assist developing member countries define their domestic resource mobilization goals and strategies, including broad-ranging reforms in tax administration and a road map for digitalization of tax administrations

(ii) ***Subnational government-level.*** While subnational governments in high-income countries raise about 30% of total public revenues, their counterparts in low-income countries raise less than 8% despite the availability of a range of subnational own-source revenues.[3] Even where subnational governments can raise their own revenue, they are often underutilized in view of their weak institutional capacity. Further, poor resource planning and public investment management—characterized by disconnect between development plans, investment projects, and budgets remain a critical challenge in many subnational governments. Therefore, they lack a pipeline of viable and costed projects, and thereby unable to attract private investments. Moreover, due to inadequate fiscal frameworks and weak financial management system they are unable to mobilize financial resources from commercial sources.

Secondly, infrastructure investment requires long-term financing, so subnational borrowing is crucial. Subnational government borrowing is relatively limited in many countries, and the bulk of it is in the form of loans rather than bond financing. Study shows that subnational debt accounts for an average of 14% of total public debt but in many developing countries in Asia and Pacific, the percentage is effectively zero.[4] Promoting subnational borrowing in developing countries will require the adoption of reform policies intended to improve the fiscal capacity and creditworthiness of subnational governments over time.

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[3] ADBI. 2019. *Improving Subnational Government Development Finance in Emerging and Developing Economies: Toward a Strategic Approach*. Tokyo.
[4] ibid

Thirdly, accessing capital market could be a viable option for some selected urban local governments, but for those without direct access to capital markets, they could be served by financial intermediaries, such as the state financial corporations.

Finally, **enhancing subnational development finance must be tailored to the country context**. Moreover, as we have already highlighted, adequate attention and support must be provided to strengthen the institutional capacity of subnational governments as this is key for them to be able to adopt innovative funding and financing mechanisms, including private sector participation in investment projects. ADB is committed to support subnational governments of our developing member countries, and has been providing various support, including policy advisory and technical assistance, including an e-learning program on decentralization, local governance and localizing SDGs for the last 3 years.