

# Part 2 — The impact of Member State policies on cohesion

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## Table of contents

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Introduction . . . . . 84

Public expenditure implications of national policies . . . . . 84

The regional incidence of government expenditure . . . . . 87

Taxation policy and regional GDP . . . . . 91

Regional development policy in Member States . . . . . 96

Statistical annex to Part 2 . . . . . 101

## Introduction

The concern of this Part is, first, to examine the regional incidence of national policies involving public expenditure and the way that these are financed in different parts of the Union. Secondly, it is to consider the mechanisms in place in different countries for both redistributing income between regions and narrowing disparities in regional economic performance. A third concern, given its potentially important effect on strengthening local economies, is to review the relative scale of foreign direct investment (FDI) across the EU and the accession countries and to assess the extent to which national and regional governments are likely to be able to influence its location.

## Public expenditure implications of national policies

Virtually all the functions performed by government that involve public expenditure have implications for regional balance in the sense that the expenditure concerned takes place in one region or another without this necessarily being a deliberate policy decision to locate spending in a particular place. They equally, it should be stressed, have implications for local areas within regions in that the same autonomous mechanisms are at work at this level as across countries as a whole.

The amount spent on such policies is a great many times larger than the expenditure financed by the Structural Funds, so that the potential effect on both economic and social cohesion within Member States is considerably greater. As demonstrated below, national policies on public expenditure and the way that spending is funded have a major effect in supporting income levels in less prosperous regions. These policies, however, are, for the most part, not directly targeted at regions, even if they have implications for regional balance. Their focus tends to be as much on immediate social problems and supporting income rather than on strengthening underlying competitiveness.

As such, there is a complementarity between these policies and EU cohesion policy, which is centred on tackling more fundamental structural weaknesses, rather than a conflict between the two. Indeed, despite their relatively small size, the Structural Funds have a crucial role to play in combating regional disparities and in strengthening cohesion.

## Public expenditure and cohesion

Even policies which do not involve expenditure directly tend to have indirect implications for spending and through these on cohesion. Within EMU, while the European Central Bank is responsible for monetary policy, national governments are responsible for fiscal policy. One objective of fiscal policy is to help maintain economic stability, to support monetary policy so that it can support growth. The philosophy of the Stability and Growth Pact (SGP) implemented at the time of monetary unification, is to let the automatic stabilisers operate freely over the economic cycle, while at the same time maintaining budgetary discipline in other areas as a permanent feature of EMU.

On the expenditure side of the budget, as distinct from the receipts side, the only item which is expected to react automatically to cyclical fluctuations is spending related to unemployment. Over the next few decades, the progressive ageing of the population will put significant pressure on public spending. Financial discipline, by restraining the growth of spending generally, is a way of ensuring fiscal sustainability in future years.

General macroeconomic performance is not a direct concern of this Part, though it underlies recent trends in overall public expenditure and revenue in Member States as well as changes in the composition of public spending. There is a lack of knowledge about the implications for different regions or for different social groups of fiscal consolidation. While fiscal consolidation has led to reductions in debt interest payments as borrowing has come down, which has potentially freed up financial resources to be spent on other, more socially and economically useful, programmes,

it has, at the same time, put downward pressure on the overall level of spending.

Moreover, although expenditure has generally been reduced relative to GDP as a result of this pressure, the tightening constraint arguably implies an increasing incentive to improve the quality of expenditure programmes, though how far this has resulted in more effective policies for regional cohesion remains an open question. In addition, fiscal adjustment may have curbed economic activity in the short-term to the possible detriment of weaker regions. Even in the short-term, however, fiscal consolidation might be supportive of growth if carried out appropriately and if accompanied by structural reform. In the longer-term, a stable macroeconomic environment created by EMU and the associated policies, is likely to be favourable to growth. All regions stand to benefit from this, even if so far it has not, in the current slowdown, been translated into higher growth rates.

Government expenditure in total, has declined significantly across the EU over recent years. Between 1995 and 2002, it fell, on average, from just over 51% of GDP of Member States to just over 47%, with Portugal alone experiencing any increase (and then by only 1 percentage point) (Graph 2.1 and Table A2.1). This reduction far outweighed the reduction in debt interest payments across the EU (of 2 percentage points). In

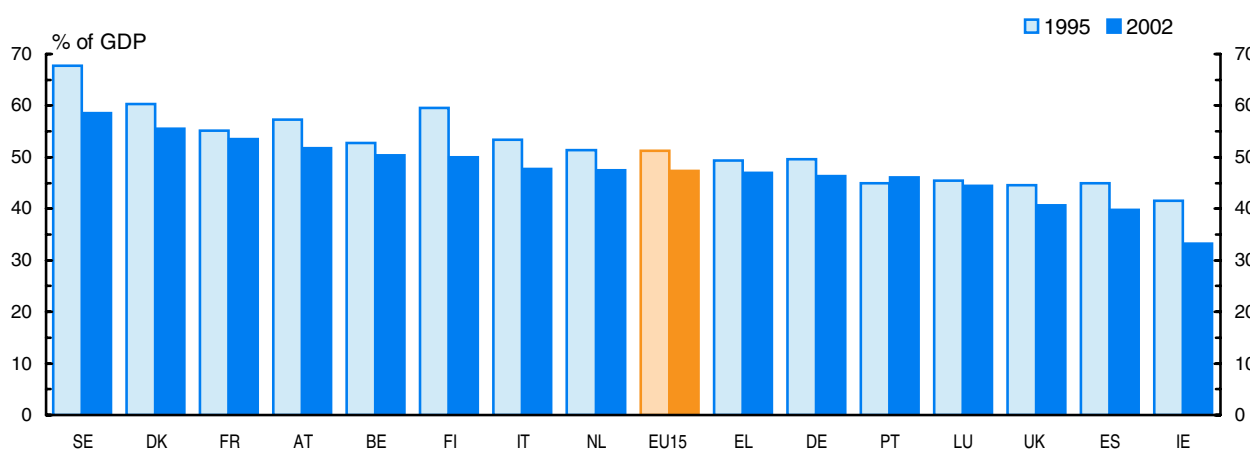
Italy, where such payments amounted to 12% of GDP in 1995 and where the reduction was particularly pronounced (almost 6 percentage points), all of the fall was reflected in lower expenditure.

While government expenditure was reduced markedly across the EU, government revenue from taxes and other sources declined only slightly in relation to GDP, implying the broad maintenance of tax rates. Except in Ireland, where the growth of GDP was exceptionally high, in no Member State did revenue fall by more than 2% of GDP and in 6 countries, it increased. Budget deficits were, therefore, reduced throughout the Union and, in a number of cases, transformed into surpluses.

### Changes in the composition of government expenditure

Apart from the fall in debt interest payments, government expenditure on transfers, whether to individuals or businesses, has also declined in recent years in relation to GDP. Between 1995 and 2002, spending on social benefits (just over 16% of GDP in the EU as a whole) was reduced, on average, by almost 1% of GDP, despite the ageing of the population and the growing number of pensioners. This reduction was partly due to a decline in unemployment but it also reflects a general tendency to limit increases in social

#### 2.1 Public expenditure in Member States, 1995 and 2002



Source: Eurostat, Government sector accounts

benefits wherever possible. The reduction in social benefits, however, was by no means general across the EU, with Germany, Greece and Portugal experiencing significant increases and Italy a smaller rise.

While the share of spending on social benefits going to old-age pensions in the EU has tended to rise over recent years as the number of people in retirement has risen, the share going to the unemployed has generally fallen because of a significant fall in their number. According to the latest data available (for 2000), old-age pensions (here defined to include survivor benefits) account for just over 46% of total social transfers in the EU and significantly below 40% only in the three Nordic countries, where social protection is more extensive than elsewhere, and Ireland, where the number of people above retirement age is relatively small (Table A2.2). Only in Italy, however, is the share over half (63%). By contrast, unemployment benefits represent only just over 6% of total social transfers in the EU and under 10% in all Member States apart from Belgium, Spain, Finland and Denmark, in the first three reflecting the relatively large numbers of unemployed, in the last, the high levels of spending per person.

Other transfers apart from social benefits, including subsidies and support for businesses, fell by more, by 2½% of GDP overall, the decline being especially large in Germany (by almost 7% of GDP) and the Netherlands (by over 4% of GDP). In most other countries, on the other hand, there was either a much more modest fall or little change at all, while in Austria and Portugal, spending on this item rose.

By contrast, current expenditure on goods and services remained much the same, on average, relative to GDP (at just under 21% of GDP). Within this, the share of expenditure going on the wages and salaries of public sector employees fell, partly reflecting the contracting out — or privatisation — of some services. Although the reduction in public sector wage bill relative to GDP did not occur in all Member States, there were significant reductions (of over 1% of GDP) in Germany, Spain, Ireland, Austria and Finland. In

Portugal, on the other hand, the public sector wage bill increased significantly relative to GDP.

In comparison with the scale of spending on public sector employment and other current purchases, the amount of public expenditure on investment, on the construction of infrastructure of various kinds, is relatively small throughout the EU. In 2002, it averaged only just over 2% of GDP in the EU and was over 4% of GDP only in Ireland and Luxembourg. Moreover, the amount spent has declined in relation to GDP in recent years. Between 1995 and 2002, it increased more than marginally only in Greece, Ireland and the Netherlands. Nevertheless, the share of total expenditure allocated to fixed investment remained virtually unchanged over this period. This may suggest that in most Member States, public sector infrastructure has not expanded much in recent years and that the stock of public capital may not have been built up as required. Over this period, however, an increasing share of investment in public infrastructure has been carried out by some form of joint public and private cooperation in many Member States. The substitution of private for public investment which this may entail might not necessarily be visible from the figures in the public sector accounts.

The division of public expenditure between these broad categories reflects the functions which governments perform, the services they provide and the type of system for delivering services which is in operation, which varies between countries according to national arrangements. Much of the spending on goods and services, therefore, goes on providing education, health and social services. The way the provision of these services is organised — whether through the direct employment of personnel or through buying in the services they provide, is, therefore, reflected in the size of the public wage and salary bill in relation to other public current purchases of goods and services.

### Government expenditure and social cohesion

A large part of public expenditure in EU Member States, on social protection and social services, in

particular, is associated with the European Social Model and, deliberately or not, makes a major contribution to limiting disparities in real income levels and life chances. In 2001 (the data for 2002 are not yet available), some 40% of total government spending across the EU as a whole went on social protection, while another 24% was devoted to education and health care. All of this spending also has implications, as shown below, for the effective distribution of public expenditure between regions, since the amount spent in any region tends largely to be determined by the number of people living there, their age structure and their need for social support.

Over the past few years, in parallel with the decline in overall public expenditure, spending on most government functions and services has also fallen, including on social programmes. Between 1995 and 2001, expenditure on social protection in the EU (here including administrative costs as well as social benefits) fell, on average, by around 1% of GDP, while spending on health and education remained broadly unchanged. This still implies, however, that the share of expenditure going on these three items increased over these 6 years, from 59% of the total to 64%, with the share going on social protection alone rising from 38% to 40%.

Despite the widespread fall in spending on social protection relative to GDP between 1995 and 2001, its share of total expenditure increased in all Member States, except the Netherlands, Finland and Sweden, in the last two of which the level of spending was well above average in 1995.

Expenditure on health care increased relative to GDP in most Member States over this period, with only Luxembourg, Austria and Finland registering a fall. Nevertheless, the share of expenditure going on health care rose in all of these countries, apart from Austria.

There was a more widespread fall in education expenditure relative to GDP over these 6 years, in part reflecting a fall in the number of children of school age, though spending rose in Denmark, Sweden, Italy, Portugal and the UK. Once again, however, the share of

expenditure going on education over this period increased in nearly all Member States, the only exceptions being Ireland and Finland, where it fell slightly.

The counterpart of the growth in the share of government expenditure absorbed by education, health and social services is a fall in the share going on general government services (ie administration) and other expenditure, comprising debt interest payments, subsidies and transfers other than social benefits, which includes spending on industrial and regional support, the reduction in which was noted above.

### The regional incidence of government expenditure

Most government expenditure which takes place at the regional or local level is a direct consequence of policies determined nationally in relation to the provision of services or income support for people in need. This is the case irrespective of the system of government in place, whether federal or unitary. Although the extent of devolution of responsibility for the provision of services to regional or local authorities varies markedly across the Union according to the degree of decentralisation of political power — which, partly but by no means entirely, reflects whether or not there is a federal or unitary system of government — there is a common concern in Member States to ensure that the level of provision does not differ too much between localities.

In the case of social protection, this is generally achieved by centralising the fixing of rates of benefit and the criteria for eligibility for support, even if the system is administered locally, so that entitlement to benefit and the amount received does not depend, or ought not to depend, on where a person happens to live in a particular country<sup>1</sup>.

Similarly for most services, whether for education, health care or policing, minimum standards tend to be set centrally even where operational responsibility and the delivery of services on the ground is vested in local or regional authorities. In several Member

States, too, some attempt is usually made, to take account of regional differences in the composition of the population, and of other factors influencing the needs of the area for a disproportionate volume of public services if common standards of social welfare are to be achieved. This applies, in particular, to education, where the proportion of the population which is of school or college age is clearly relevant, and health and social services, where the relative number of elderly people is an important determinant of need.

### Differences in systems of government

Systems of government and the degree of decentralisation of responsibility for policy differ markedly across the EU. In federations, like Germany, Austria or Belgium, a significant amount of responsibility for the implementation of policy in many areas lies at the regional or state level. Although the formulation of policy is in general less decentralised, or is a shared responsibility between levels of government, regional authorities in such countries tend to have some autonomy over the measures implemented to achieve common objectives and may have some discretion over the level of priority given to various aims. Differences in regional and local circumstances can, therefore, be specifically allowed for in the deployment of expenditure. At the same time, as described below, there are mechanisms in place in such countries for preventing wide regional differences in expenditure on public services from arising. These take the form of standards or norms set centrally and of equalisation mechanisms to ensure that the financial resources which regions have access to do not vary too greatly.

Following moves to decentralise government over the last twenty years, regional authorities also have a growing amount of responsibility for discrete areas of policy in Spain and Italy, and in Italy further extensive changes are being introduced. At present, their revenue-raising powers are relatively limited compared with the *Länder* in Germany or the Nordic countries, though not as compared with the situation in Belgium, where the three regions finance only a small proportion of their expenditure from revenue raised

locally. Local authorities have especially extensive responsibility for policy in the three Nordic countries, Denmark, Finland and Sweden. Local income taxes provide much of the revenue to finance them, but are complemented by national schemes that equalise fiscal capacity or provide additional resources.

In France, the UK and other Member States, on the other hand, policy-making is much more centralised, even if in both the former two there have been some moves towards devolution. Although regional and local authorities may be charged with implementing policy and with the provision of services locally, their revenue-raising powers are limited as is their discretion over the way they spend the budget for provision of services received from central government.

While there is a general tendency towards more decentralisation of responsibility to the regional and local level, this in most cases is being accompanied by a strengthening of the means to ensure that less prosperous areas are not disadvantaged by having to provide more services. A possible exception to this is Italy, where regional authorities are increasingly being given more autonomy for the expenditure they undertake, without this so far being matched by a comparable increase in the income which the less prosperous regions have for financing spending.

### Regional variations in government expenditure

While these differences in systems of governance across the EU affect both the regional deployment of public expenditure and the amount of revenue for funding spending which is raised locally rather than centrally, in practice, actual spending per head shows only limited variation between regions within countries. Equally, as indicated below, there seem to be no substantial differences across countries in the rates of taxation and charges levied on those living and working in different regions.

The fact that policies are decided nationally in relation to perceived needs means that there tends to be a

higher level of government expenditure in the less prosperous regions in relation to their income than in the more prosperous ones, and in the poorer areas within regions than in the richer ones.

Unfortunately, given the data available, the relative scale of public expenditure in different regions cannot be assessed for all Member States. Nor is it possible to make comparisons of this between countries since the information available tends to be partial and specific to a particular country. The main concern here, therefore, is to demonstrate the way that the public expenditure and taxation system contribute differentially to GDP and, therefore, maintain income in the less prosperous regions relative to the more prosperous ones and to give an indication of the scale of contribution involved. This is done by examining the regional incidence of expenditure in selected countries where data exist and by considering the way that revenue is raised across the Union.

## UK

In the UK, as in the rest of the EU, most of the public expenditure which it is possible to distinguish at regional level (some 85% of the total) goes on social protection, health and social services and education. These together accounted, on average, for 75% of government spending in the regions in the 2000–01 financial year (Graph 2.2 and Table A2.4). In terms of expenditure per head across regions, this tended to

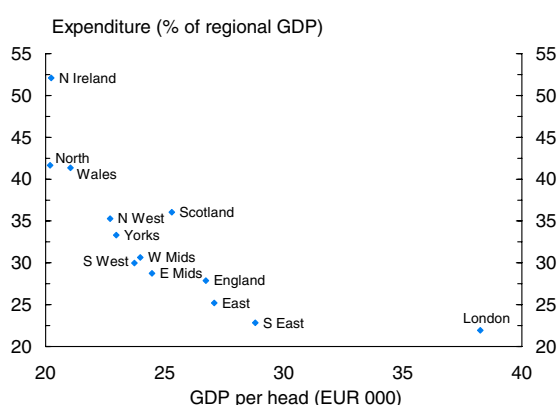
be higher than elsewhere in the less prosperous regions, such as Northern Ireland, Scotland, Wales and the North and North-West of England, partly because of higher spending on social protection, reflecting the larger numbers of unemployed and those not in work, though also because of the additional expenditure on health care and administration in the first three regions. Expenditure per head was also above the national average in London, again reflecting in part higher spending on administration because of the large number of government offices located there, though over the years efforts have been made to decentralise these.

Although there is some variation between regions in spending per head on education and health care, this is comparatively limited across the English regions at least, as is the variation in environmental and transport expenditure.

The implication of the expenditure per head figures is that spending relative to GDP varies markedly across UK regions. Even leaving aside Northern Ireland, which is a special case because of recent history and ongoing political problems, expenditure in 2000–01 ranged from just over 41% of GDP in Wales and the North of England to 21–22% in London and the South-East. Accordingly, on this measure public expenditure contributes almost twice as much to income in the former two regions, which are the least prosperous in the UK, than the latter two, primarily because of their much lower level of GDP per head and, to a lesser extent, their greater need for social spending.

At the same time, much of this additional expenditure, it should be noted, consists of current rather than capital spending — ie it goes to consumption rather than to investment — and as such is likely to have a only a limited effect in strengthening underlying competitiveness. For example, an average of only 1% of GDP was spent on roads and transport and in no region was the figure above 1½% of GDP. On the other hand, it is also the case that some expenditure classified as current, such as that on education and training, R&D or support for business development, is more similar to

**2.2 Government expenditure by region in the UK, average 2000-2001**



Source: see Table A2.4

investment and can potentially make an important contribution to increasing productive potential in the region concerned. Nevertheless, even allowing for this, most regional expenditure can be regarded as having social rather than economic objectives.

## Italy

A similar picture emerges in Italy, though the variation in the relative scale of public expenditure across regions is slightly less systematic than in the UK and differences in the effective contribution of spending to GDP smaller, despite the wider regional variation in GDP per head. It should be noted, however, that the public expenditure data are more complete than in the UK, where 15% of total spending is not allocated between regions, which could affect the comparison if the outlays concerned were concentrated in London and other more prosperous regions. Nevertheless, the factors at work are much the same in the two countries.

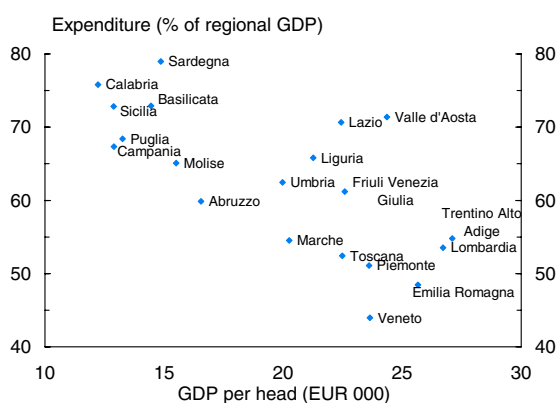
While social protection expenditure per head varies between Italian regions, it is less affected by differences in unemployment rates than in the proportion of the population above retirement age, since the unemployed receive a comparatively low level of benefit and pensions are relatively high. Moreover, the relative number above retirement age is markedly larger in the more prosperous northern regions of Italy than the less prosperous southern ones, unlike in the UK where regional differences in numbers are relatively small. In addition, pensions tend to be more related to previous income in Italy than the UK, where the basic state pension is a fixed amount. Expenditure per head on social protection in 2000, therefore, was almost 85% higher in Liguria, where some 25% of the population is 65 or over, than in Campania, where the figure is only 14% (Graph 2.3 and Table A2.5). While spending per head on social protection in most northern regions was above the national average, in all southern regions it was significantly below, (although higher than average in the latter group as a percentage of GDP, as noted below).

In the case of education and health care, differences in expenditure per head were less marked, though it remains true that in education, in all southern regions except Sardegna, spending per head was below the national average and in health care, it was below the average in all of them. These differences, however, may reflect lower wage and other costs in the south than in the north rather than any difference in the standard of service provided.

Spending per head on transport, the environment and other programmes also tended to be less in southern regions than in northern ones. Nevertheless, the difference in these areas of expenditure as in social protection, health and education was generally smaller than that in GDP per head, so that overall government spending was in most cases — but not all as noted below — higher in relation to GDP per head in the less prosperous parts of Italy than in the more prosperous ones. Expenditure relative to GDP, therefore, ranged from 35% above the national average in Sardegna and 30% above in Calabria, the region with the lowest GDP per head, to 25% below average in Veneto, a slightly narrower difference between extremes than in the UK<sup>2</sup>.

At the same time, while all southern regions have above average public expenditure relative to GDP, not all northern regions have a level which is below average, despite the above average GDP per head which all of them enjoy. Indeed, in Valle d'Aosta and Lazio,

### 2.3 Public expenditure\* by region in Italy, 2000



\* includes public corporations as well as General Government  
Source: see Table A2.5

spending in relation to GDP was over 20% above average in 2000 and higher than in Puglia or Campania. Expenditure was also comparatively high in relation to GDP in Liguria, largely because of its relatively high level of spending on social protection (due to its large number of people in retirement), which amounted to over 23% of regional GDP in 2000, more than in all southern regions except Calabria.

In Italy as in the UK, therefore, government expenditure generally has the effect of narrowing disparities in GDP per head, even if the effect seems to be smaller (though the qualification noted above should be borne in mind). As also in the UK, however, it goes much more to supporting consumption than investment, spending on roads and transport, for example, amounting to only just over 2% of GDP on average and under 5% of GDP in all regions, more than in the UK, but still relatively small.

## Spain

In Spain, the same factors are evident in determining the regional incidence of expenditure as in the UK and Italy, even though data are available for a more restricted range of spending than in these two countries. In this case, as in Italy, there is no close (inverse) association between spending per head on communal services and the level of regional prosperity, or lack of it, though the intervention from the Structural Funds, which is significant and relatively concentrated in the

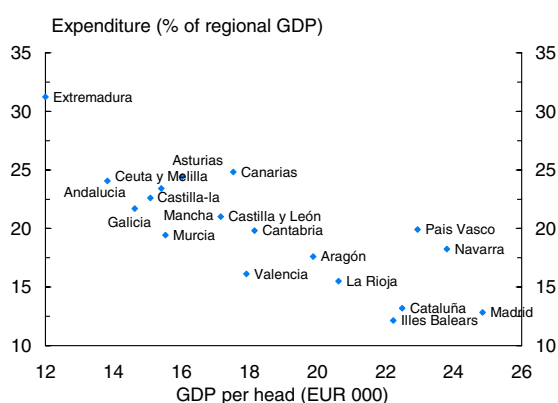
poorer Objective 1 regions, serves to make the association closer. Nevertheless, public expenditure tends to contribute markedly more to GDP in the less prosperous regions than the more prosperous ones and so has the effect of strengthening social cohesion.

Expenditure on health and social services was, therefore, higher relative to GDP in most Objective 1 regions in Spain over the period 1992 to 1999 than in others (Graph 2.4 and Table A2.6), in part reflecting the larger numbers of unemployed.<sup>3</sup> Nevertheless, there were some exceptions. In particular, spending on health and social services was below the national average in Valencia, an Objective 1 region, and above average in Navarra, which has the second highest level of GDP per head of all Spanish regions.

Expenditure on infrastructure also tended to be relatively high in Objective 1 regions, though again a few non-Objective 1 regions also had above average levels. In Spain, as in the UK and Italy, however, the amount spent on infrastructure investment was uniformly low in relation to GDP, the figure exceeding 3% of GDP only in Extremadura and Ceuta y Melilla, and then only slightly.

Overall, taking account of expenditure financed by the EU, average spending over the period ranged from 31% of GDP in Extremadura (the region with the lowest GDP per head in Spain) and 25% in the Canarias to 13% in Madrid and Cataluña and just 12% in the Illes Balears.

**2.4 Government expenditure by region in Spain, average 1992-1999**



Source: see Table A2.6

## Taxation policy and regional GDP

Although data on government expenditure in Member States are incomplete, those available indicate clearly that public expenditure makes a differential contribution to GDP across regions which helps to reduce disparities and maintain social cohesion.

The key question is how far the higher expenditure relative to GDP in the less prosperous regions is

accompanied by higher taxes and other charges to fund this higher level — or how far, in other words, the effect of the higher spending is offset by higher charges levied on income in the regions concerned.

Although this question is difficult to answer given the data available, an insight can be gained into the regional incidence of the funding system in operation from data on the division of taxes between central and regional or local government. In principle, therefore, the more that regions are responsible for covering the cost of the spending carried out at regional or local level by levying taxes or charges on the people living there and the businesses located there, the more are any beneficial effects from higher expenditure relative to GDP likely to be offset<sup>4</sup>. These higher taxes may, of course, themselves be offset by policy decisions to increase transfers from central government, or to set up an equalisation fund to reduce the extent of differences between regions in the income available to finance expenditure.

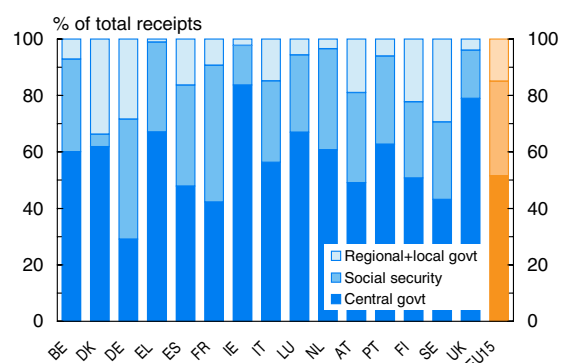
Where rates of taxation, or of social contributions, are set centrally, the problem does not arise in the sense that those living in less prosperous regions — or indeed in poorer areas within more prosperous regions — will tend automatically to pay a smaller amount in tax than those living elsewhere because their income in aggregate is lower. If there are common rates of tax and contributions applying to income and expenditure, and tax revenue, therefore, is the same in relation to GDP in the region as elsewhere, the tax system will have a neutral effect on the income available to fund expenditure and will, accordingly, not serve to offset the contribution of spending to GDP. If tax rates are progressive rather than proportional, in the sense that they increase as income rises, then the tax system will reinforce the differential effect of expenditure on regional levels of GDP.

How far the tax system in different Member States is progressive as opposed to proportional is difficult to determine, depending as it does on the interaction of income taxes, which are typically progressive,

expenditure taxes, which are typically proportional, even though they might vary with the composition of spending, and social contributions, which are also typically proportional at least up to a certain level of earnings<sup>5</sup>. The evidence suggests that tax systems in most countries in the EU are mildly progressive and in others are broadly proportional, or at most only slightly regressive<sup>6</sup>. As such, they may add in some cases to the differential effect across regions resulting from policy on public expenditure and in others are unlikely to offset it much if at all.

In practice, in most EU Member States, taxes are predominantly levied centrally and revenue from regional and local taxes represents only a small proportion of the total finance raised to fund public expenditure. In the EU as whole, only 15% of finance came from regional and local sources in 2001, with only the federal states of Germany and Austria, the three Nordic countries, where local authorities have significant responsibility for expenditure, and Spain, where the regions are important, having proportions larger than this (Graph 2.5 and Table A2.7). Moreover, except in a few countries, the share of revenue raised from regional and local sources has remained much the same over recent years and the main change in the composition of government receipts has been a shift from social contributions to taxes in order, in part, to reduce the tax burden on employment.

**2.5 Receipts from taxes and social contributions by level of government, 2001**



Source: Eurostat, Government sector accounts

The only countries in which there has been a significant increase in the importance of regional and local taxes are Denmark, Spain and Italy, in the last of which their share of revenue almost doubled between 1995 and 2001. This reflects a policy in Italy of devolving more responsibility for raising the revenue for funding government expenditure to the regions, a policy which has continued since then, so leading to an increasing proportion of tax being levied regionally rather than centrally and giving rise to a growing possibility of effective tax rates being higher in less prosperous regions where taxable capacity is less.

In Italy, as in other countries in which a significant level of responsibility for generating tax revenue is devolved to the regional and local level, there is a need for an explicit mechanism of transfers from more to less prosperous areas if the latter are not to be disadvantaged by having either to impose higher taxes or accepting lower levels of public expenditure and the lower standards of service which this is likely to imply.

In most Member States countries, however, the relatively small proportion of revenue raised at the regional and local level, coupled with the characteristics of the tax system, implies that differences between regions in the contribution of public expenditure to GDP are not counteracted by the way spending is funded.

### **Discretionary mechanisms for transferring income to regions**

The above conclusion tends to be confirmed by an examination of the means in place for the overall management by central government of the expenditure carried out at regional and local level and for determining the revenue available to fund this. In all Member States, conscious efforts are made to increase the revenue available in areas where the local tax base is considered insufficient to meet spending needs or where the costs of services which need to be provided are greater than normal because, for example, of the nature of the terrain or for other reasons. In addition, specific support for economic development may be given to certain regions.

The scale of government transfers to different regions or local areas is determined in slightly different ways in different countries, though common principles are evident in the form, in particular, of assessment of needs and of local taxable capacity. In addition, in all countries, regional and local authorities, irrespective of the extent of funding provided from central government and irrespective of how closely needs are assessed, have some discretion of how they actually spend the transfers they receive.

In Germany, the process of equalisation is designed to adjust the revenue available to the Länder though there is also some allowance for special needs, such as for the city states. Because, however, the Länder have considerable autonomy, they do not necessarily spend the same amounts on different public services as assumed in the calculation of equalised per capita expenditure. Much the same is true in Austria.

In the three Nordic countries, as well as a number of other Member States, the system has a similar aim to that in Germany, but operates between much smaller authorities — municipalities or counties rather than Länder.

In Sweden, the main local source of revenue for local government is local income tax and the transfer system is aimed at boosting the revenue of those municipalities where income, and taxable capacity, is relatively low by transfers from wealthier areas. In addition, there has also been a policy of relocating certain national government offices to the less prosperous municipalities in order to assist their development — and add to their tax base — further.

Similar equalisation arrangements operate in Denmark, though between even smaller local authorities. Here, there are 14 counties, two special status regions (Copenhagen and Frederiksberg) and 271 municipalities, which all have their own income and property taxes and, consequently, a relatively large amount of autonomy<sup>7</sup>.

In Finland, municipalities have a sizeable tax base but do not have the power to determine tax rates. Accordingly, wealthier regions generate more revenue than they are considered to need for spending, which is then effectively transferred to less wealthy regions with smaller tax proceeds.

### The criteria for assessing regional and local needs for expenditure

In all Member States, the need for spending at the regional and local level is assessed centrally as a means of determining the amounts of transfer which the authorities concerned should receive. The methods used are very similar, in most cases involving the estimation of a standardised level of service per head of population, though there are differences in the way — and in the level of sophistication — that these estimates are made.

In the Netherlands, for example, central government transfers to provinces and municipalities account for most of their income and are determined by a wide range of indicators (such as size, population density, soil quality, social structure and degree of urbanisation as well as their local taxable capacity). The sole aim of the system, however, is to equalise the income they have to spend, given their needs.

In Portugal, a general fund allocates resources to the three NUTS level 1 regions, largely on a per capita basis, but with additional criteria that benefit the two island regions (see below). This general fund also uses a range of criteria to determine allocations to municipalities within each region. A second fund, with explicit cohesion aims, is limited to less developed municipalities, while two additional funds are intended to ensure that the municipalities have adequate resources. Broadly, transfers are inversely correlated with income per head, with Lisboa e Vale do Tejo, the wealthiest region, receiving less than a third per head of population of the amount going to Alentejo, the least wealthy. (In relation to GDP, transfers to the former amount to barely 1%, to the latter 6%.)

In many Member States, such as with the city Länder in Germany, particular regions or local areas receive preferential treatment when transfers are allocated. For historical or cultural reasons, Italy, Spain and the UK accord special status to certain regions, giving rise to greater devolution of powers and, in most cases, different funding formulae (to Northern Ireland, Scotland and Wales in the case of the UK). This also is true to a lesser extent in Finland, where the Åland region has special status and treatment in relation to the rest of the country, in Portugal, in the case of the Açores and Madeira, and in France, in the case of Corse and the ‘DOM/TOM’. Some of these special status regions receive larger transfers from central government than other areas, even though they are comparatively wealthy — Trentino Alto Adige in Italy as well as Åland in Finland is an example. While such payments might not seem justified in terms of economic or social cohesion, they may be important in preserving political cohesion.

The budgets of the French regional authorities are financed mainly through transfers from the State. In the French overseas territories, public spending per head is around three times the average for metropolitan France and in Corse, 3.5 times the average. Transfers to most other regions vary relatively little. Although the less wealthy tend on average to receive relatively more in relation to population, there are several anomalies and the correlation between income per head and public spending is weak. In particular, Ile de France receives a premium over the national average — arguably because of higher service delivery costs — while in Lorraine, spending per head is well below average.

### Aligning transfers with Community support

In countries which receive substantial amounts from the Structural Funds, some national policies are closely tied to EU funding. In Spain, therefore, the inter-territorial compensation fund allocates complementary funding only to Objective 1 regions (although there is also a special ‘Teruel’ fund which provides support to that part of the Aragón autonomous region,

### Equalisation in Germany

In Germany, the principal channels through which money is transferred both between the Länder themselves and between Federal Government and the Länder is the Financial equalisation system, the *Länderfinanzausgleich*. In its current form, which dates from 1995 when the separate systems in east and west Germany were merged under the *Solidarpakt*, it comprises a mix of pure horizontal equalisation and federal topping-up.

The computation of the respective positions of each Land takes account of taxable capacity based on the taxes which are either exclusive to the Land or shared with Federal Government. The primary allocation consists of shared taxes on income, profits and turnover. Some 75% of the revenue raised from these is distributed between Länder according to population, with the balances reserved for 'financially weak' Länder. This ensures that the revenue of each Land is increased to at least 92% of the average.

There is then a secondary stage of financial equalisation to correct the primary tax distribution to ensure equal per capita tax distribution between the Länder. Because city Länder (Berlin, Bremen and Hamburg) are considered to have special needs, however, they effectively receive 35% more per head of population. A further stage then consists of transfers from the Federal Government designed to raise the revenue available in Länder which have below average income or face special circumstances. These transfers are of three kinds:

- gap-filling grants' (*Fehlbedarfsbundesergänzungszuweisungen*), which lift revenue in the less wealthy Länder to at least 99.5% of the average;

- compensation for special burdens (*Sonderbedarfsbundesergänzungszuweisungen*), covering the cost of political management in small Länder and the cost of unification in the new Länder (*teilungsbedingte Sonderkosten*), as well as giving Bremen and Hamburg additional revenue because of their debt problems;
- transitional grants (*Übergangsbundesergänzungszuweisungen*), paid to the less wealthy west German Länder since 1995, though designed to fade out over time at a rate of 10% a year.

The transfers are substantial. In 2000, Berlin received a total transfer equivalent to 6.4% of its GDP, while net transfers to the eastern Länder average around 5% of GDP. However, because it benefits greatly from a special supplementary programme for regeneration, transfers to Bremen amount to 6.5% of GDP. For Hessen — the Land which pays proportionally most in *Finanzausgleich* — the effect is to reduce fiscal capacity from 126% of the national average to 106%, a reduction equivalent to 1.5% of its GDP.

These net transfers, however, cannot be compared directly with the figures presented above on public expenditure in UK, Italian and Spanish regions because they leave out of account a large element of spending undertaken directly by the Federal Government or under the social insurance scheme for social protection. These, as demonstrated in the case of the countries examined, are likely to add significantly to the differential contribution of public spending to regional GDP.

even though Aragón as a whole is not designated under Community regulations).

In Greece, the main national instrument for promoting economic and social cohesion is the Public Investment Programme (PIP) which finances large infrastructure projects in transport, education, health, culture and other key sectors of the economy at national and regional level. Most of the funds allocated

by the PIP go through Community Support Framework (CSF) III. Those regions which receive the highest Community transfers per head under the current CSF (Dytiki Makedonia and Voreio Aigaio), receive 5–6 times more than the Attica region. In Ireland too, proportionally more from the national budget is allocated to the Border, Midlands and West region than to the Southern and Eastern region to make up the matching funding for Structural Fund programmes.

## Regional development policy in Member States

Policies to promote economic development are pursued by all levels of government in Member States, using a variety of means and with diverse targets. They include, among others, assistance for technology and innovation, help for restructuring industries facing difficulties or long-term contraction, support for SMEs and incentives to inward investment. Some of these are explicitly classified as state aid and, therefore, subject to legal restrictions imposed by the EU to avoid unfair competition. These are considered elsewhere in this report (Part III).

Other measures, so long as they do not provide direct financial support to particular companies, are not controlled in this way. Subsidies paid to individuals or to public bodies, general subsidies and assistance provided by one private body to another are all excluded from this definition. Some forms of assistance to private entities are, in addition, allowed under the Treaty, notably for services of general interest and to stimulate development of eligible regions.

The approach to territorial development differs between Member States, in part reflecting institutional factors, notably the degree to which responsibility for economic development policies is decentralised, as well as changing views about the factors determining economic development.

Although devolution has been a common theme throughout the EU, there are major differences between countries in the autonomy conferred on lower tiers of government. In Austria, Denmark and Belgium, while central government exercises some oversight, sub-national governments are responsible for the planning and financing of regional policies. In this way, spending is mainly tied to the overall financing ability of each provincial government, so that reducing disparities between regions (provinces, counties or municipalities) is not necessarily a central aim.

By contrast, in the UK and France, the allocation of resources is largely determined centrally, although implementation of policy is increasingly the responsibility of regional bodies: regional development agencies in England and devolved authorities in Scotland, Wales and Northern Ireland; and regions in France.

There is not always a good correspondence between national and EU designations of 'territories' for regional and other forms of economic development assistance. In France regions favoured by domestic policy are largely different from those that benefit from Community policy whereas in Germany the correspondence is close. In Spain, as in the other Cohesion countries, the framework of the Structural Funds is largely adopted for national policy. But in the UK and the Netherlands, urban areas — especially — are designated on different criteria from Community policy.

In the Netherlands, moreover, regional development issues are addressed on the basis of the perceived needs of the country as a whole. Expenditure on regional policy as such is, therefore, modest, with the main emphasis on small areas with specific economic problems (mainly urban areas with high unemployment).

Support for innovation and new technologies has emerged in several areas as a primary instrument in recent years. The Flemish region in Belgium has been especially prominent in this regard, as have the Austrian Länder, with an increasing focus on innovation as a means of stimulating endogenous regional development and with federal support for R&D. Often such strategies are directed primarily at SMEs and encompass horizontal policies such as encouragement of cooperation between research institutes and the corporate sector, rather than explicit subsidies.

A focus on employment creation and the attraction of big investment projects has been characteristic of a number of areas in which unemployment is high. Wallonie is an example and Ireland has long had

a strong focus on using FDI to foster economic development.

'Clustering' is a feature of policy in many countries. In Steiermark, in Austria, the provincial government overhauled its development strategy in 1996 and created a cluster network linking various parts of the automotive industry, which proved effective. Upper Austria followed the example with a comprehensive provincial strategy and incremental increases in technology and networking subsidies.

In Sweden, government policy has shifted in recent years to supporting the development of growth poles and clusters in different regions whereas previously it was centred on maintaining a high level of public sector activity in the northern, sparsely populated regions in order to combat outward migration.

In Italy, significant reforms have recently been made to territorial policies. These are administered and funded by the central government and now focus largely on capacity building through public investment instead of incentives to businesses, as in the past. Although regional incentives to companies still go disproportionately to the south, public investment programmes often favour regions in the north, giving rise to a possible conflict between national policy and EU cohesion policy.

### Foreign direct investment

Policies to attract foreign direct investment (FDI) are typically an important part of regional development strategy. Indeed, a significant aim of regional support is precisely to increase the attractiveness of problem regions for foreign investors. FDI not only brings income and jobs to regions but, in many cases, it is also a mechanism for transferring technology and know-how. Through spill-over effects, this can potentially have a significant impact on the productivity and competitiveness of resident enterprises in the region concerned. A substantial part of FDI, therefore, takes the form of multinationals investing in the region, either through acquiring an existing business and its

production facilities — and, indeed, its customer base — or through setting up new facilities. Either way, multinationals, particularly when investing in less developed regions, tend to bring with them up-to-date techniques of production and working methods.

Although the benefits associated with FDI tend to be greatest in the less favoured regions, the comparative advantages to multinationals of investing in such regions are not always sufficient to attract them to locate there. Much depends in this regard on the primary reason for the investment so far as the multinational is concerned, whether to supply the local or regional market however extensively defined (whether confined to a small area, at one extreme, or the whole of the EU, at the other) or whether to take advantage of specific factors of production which are on offer — such as low labour costs, particular skills or certain natural resources.

If the reason has to do with supplying a relatively large market in geographical terms, then a multinational might be open to persuasion where in a particular country or broad geographical region it decides to locate. A national government might then have little difficulty in persuading a multinational to locate in a less favoured area. If the reason, however, has to do with the specific attraction of a particular place, then it can often be difficult for a national government to persuade the multinational concerned to locate elsewhere if the place in question is not in line with overall regional development policy. In this case, the risk might be to discourage the multinational from investing in the country concerned at all. This tends to be a particular dilemma for governments in the Cohesion countries or, still more, in the accession countries, where there is a potential trade-off between wanting investment to go towards the less developed regions to provide a stimulus and help them catch up, and the fact that investment tends naturally to be attracted to the regions which are most dynamic.

Although data on the regional location of inward investment into the EU are incomplete, they suggest that FDI inflows have tended to go disproportionately

to the economically stronger regions both within countries and across the EU as a whole. Ireland is somewhat of an exception in that it attracted large-scale inflows throughout the 1990s despite, initially at least, its relatively low GDP per head, although inflows went disproportionately to the eastern part of the country, to Dublin and the surrounding area. Ireland has continued to be a major destination for investment as its GDP has risen.

Over the three years 1999 to 2001, FDI in the 15 EU Member States amounted to around 7% of GDP, on average, if inflows from other parts of the Union are included (and under 2% of GDP if they are not). In Ireland, however, inward investment averaged over 20% of GDP over these three years (Graph 2.6). The next highest levels of FDI, at over 13% of GDP, were in Denmark, the Netherlands and Sweden, in the first two of which GDP per head was the third and fourth highest in the EU, behind Ireland and Luxembourg, which with Belgium, also had a level of FDI well above the EU average relative to GDP.

In the Cohesion countries, other than Ireland, FDI was much lower, averaging just over 4% of GDP in Portugal over this period and only 1½% of GDP in Spain and just 1% of GDP in Greece, the lowest level in the EU together with Italy.

Within all these countries, as elsewhere in the Union, the evidence available suggests that inward investment went disproportionately to the more prosperous regions and relatively little went to lagging areas. Although the regional data are not ideal because inflows are often classified to the region where a company's headquarters is located rather than to where the investment actually goes, the evidence is, nevertheless, striking. In Germany, investment was concentrated in a limited number of Länder, with Nordrhein-

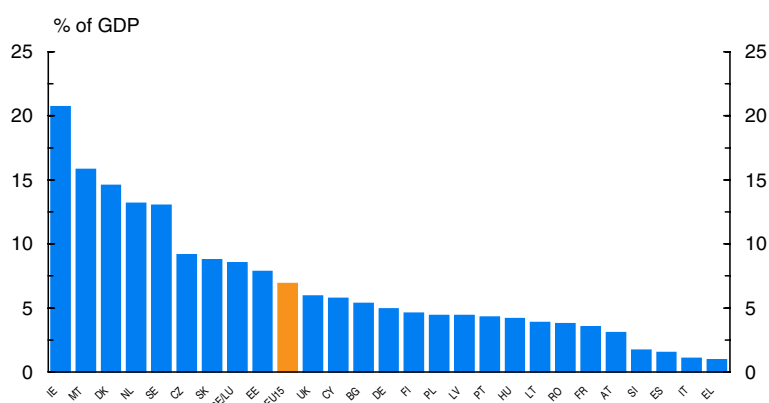
Westphalia, Hesse and Baden-Württemberg accounting for 71% of all inward FDI inflows in the years 1998 to 2000 and Bayern and Hamburg for another 17% (Table A2.8). By contrast, the 5 Objective 1 regions in the east of the country accounted for only just over 2% of total inflows between them.

In Spain, around 70% of FDI inflows in the years 1999 to 2001 went to Madrid and a further 14% to Cataluña, while Objective 1 regions accounted for well under 10% between them (and for very little at all outside Valencia and the Canaries). Similarly, in Italy, where the data relate to employment in foreign-owned enterprises rather than FDI inflows, multinationals are concentrated in the north of the country and under 4% of employment in foreign-owned companies was in the southern Objective 1 regions in 2000.

### FDI in the accession countries

Much the same tendency is evident in the accession countries as in the EU, at least for regions within these countries, though the distribution of investment across countries varies less closely with GDP per head than in the EU, despite appearances to the contrary. According to the latest data, almost 70% of FDI inflows to these countries goes to just three of them — Poland, which alone accounts for 35% of the total, the Czech

**2.6 FDI inflows into Member States and accession countries, average 1999-2001**



BE/LU: data are for 1998; DK: data are for 1999-2000; ES: data are for 1998-1999; HU and SK: data are for 2000-2001; RO: data are for 1997-1999  
Source: Eurostat, Balance of payments statistics

Republic and Hungary (Table A2.9). (The figure of 70% includes an estimate for Romania, for which no data are available for the years since 1999.)

Nevertheless, if related to GDP, this apparent concentration is no longer so evident. In Poland, therefore, FDI amounted to an average of 4½% of GDP over the three years 1999 to 2001 and in Hungary, to just over 4%, less than in most other countries. Although in the Czech Republic, FDI was higher than anywhere else relative to GDP (over 9%) other than in Malta (16%), it was also relatively high in Estonia and Bulgaria, countries with relatively low levels of GDP per head even within the region. At the same time, it was relatively low in Slovenia, in which GDP per head is relatively high.

Within all the countries, however, the data available indicate a relatively high degree of concentration of FDI in and around capital cities, as in the Cohesion countries. In Hungary, therefore, over two-thirds of inward investment in 2001 went to the region in which Budapest is located; in the Czech Republic, 60% went to Prague and the surrounding region (Střední Čechy) in the same year and in Slovakia, some 63% went to Bratislava (Table A2.10). In Poland, on the other hand, where there are a number of large cities apart from Warsaw, FDI inflows are less concentrated. Nevertheless, the capital city region (Mazowieckie) accounted for around a quarter of total inflows in 1998 and two other regions (Łódzkie and Wielkopolskie), both of which contain large cities (Lodz and Poznan), for another quarter.

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- 1 It should be noted, however, that in the southern countries, the provision of a minimum level of income tends to be a regional responsibility and access to this varies from one region to another.
  - 2 Moreover, the Italian figures relate to smaller NUTS 2 regions instead of larger NUTS 1 regions as in the UK, which would tend in itself to widen rather than narrow the difference.
  - 3 Unlike in Italy, there is no systematic tendency for the relative number of people above retirement age to be greater in more prosperous regions than less prosperous ones, or indeed vice versa.
  - 4 This, of course, ignores the benefits which might stem from levying taxes locally to fund local expenditure in terms of encouraging greater fiscal responsibility and more efficient deployment of spending.
  - 5 In practice, social contributions in countries in which a ceiling on the maximum amount payable is fixed are regressive above the level of earnings involved and this tends to offset the progressive schedule of income tax rates.
  - 6 At the same time, it should be noted that the widespread tendency to shift away from taxes on income to taxes on expenditure generally has the effect of reducing the progressive nature of the tax system as a whole.
  - 7 The system in Denmark is set to alter in the near future with possibly large changes in both the structure of the public sector and the division of responsibilities between different levels of government.



# Statistical annex to Part 2

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## A2.1 Public expenditure by economic category, 1995 and 2002

	Goods and services		of which: empl. comp.		Social benefits		Debt interest		Other transfers + subsidies		GDFC*		Total expenditure		Total revenue		Budget balance	
	1995	2002	1995	2002	1995	2002	1995	2002	1995	2002	1995	2002	1995	2002	1995	2002	1995**	2002
	% of GDP																	
EU15	20.7	20.6	11.1	10.4	17.2	16.4	5.4	3.4	6.7	4.2	2.6	2.2	51.3	47.4	46.1	45.5	-5.2	-1.9
BE	21.4	22.3	11.9	12.0	16.6	16.1	9.3	6.1	4.6	4.7	1.8	1.6	52.8	50.3	48.5	50.4	-4.3	0.1
DK	25.8	26.3	17.3	17.6	20.4	17.5	6.4	3.7	5.2	5.2	1.8	1.8	60.3	55.5	58.0	57.4	-2.3	1.9
DE	19.8	19.2	9.0	7.9	18.1	19.4	3.7	3.1	11.5	4.8	2.3	1.6	49.6	46.3	46.1	45.0	-3.5	-1.3
EL	15.3	15.8	11.3	11.9	15.1	16.4	11.7	5.5	3.4	3.4	3.2	3.8	49.4	46.9	39.3	45.6	-10.1	-1.3
ES	18.1	17.6	11.3	10.3	13.9	12.5	5.2	2.8	4.4	3.9	3.7	3.4	45.0	39.8	38.4	39.9	-6.6	0.1
FR	23.9	23.9	13.7	13.7	18.5	18.1	3.6	3.1	4.4	4.0	3.3	3.1	55.1	53.5	49.6	50.3	-5.5	-3.2
IE	16.4	15.1	10.2	8.3	11.8	8.3	5.4	1.4	4.7	3.9	2.3	4.4	41.5	33.3	39.4	33.1	-2.1	-0.2
IT	17.9	18.8	11.2	10.7	16.7	17.1	11.5	5.8	4.9	3.8	2.1	1.8	53.4	47.7	45.8	45.2	-7.6	-2.5
LU	18.4	18.1	9.7	8.6	16.5	15.7	0.4	0.3	6.4	6.2	4.6	4.7	45.5	44.4	47.6	46.8	2.1	2.4
NL	24.0	24.5	10.8	10.5	15.3	11.8	5.9	3.1	8.1	3.8	3.0	3.3	51.4	47.5	47.3	45.9	-4.1	-1.6
AT	20.4	18.6	12.6	9.7	19.5	18.6	4.4	3.6	7.6	8.3	3.1	1.3	57.3	51.7	52.0	51.3	-5.3	-0.4
PT	18.6	21.1	13.6	15.4	11.8	13.0	6.3	3.0	4.4	5.4	3.7	3.4	45.0	46.1	39.6	43.3	-5.4	-2.8
FI	22.8	21.7	15.2	13.5	22.1	16.8	4.0	2.2	5.2	4.0	2.8	2.9	59.6	50.0	55.7	54.2	-3.9	4.2
SE	27.3	28.0	16.7	16.3	20.6	17.6	6.6	3.2	6.4	3.9	4.0	3.2	67.7	58.5	60.3	59.5	-7.4	1.0
UK	19.6	20.0	8.3	7.6	15.4	13.5	3.7	2.1	3.8	3.8	2.0	1.3	44.6	40.7	38.9	39.4	-5.7	-1.3

\* GDFC = gross domestic fixed capital formation

\*\* DE: not including unification-related debt and asset assumptions by the Federal Government (Threuhand, eastern housing companies and Deutsche Kreditbank) equal to EUR 116.3 billion;

NL: not including a net amount of EUR 14.9 billion of exceptional expenditure related to the reform of the financing of social housing societies

Source: Eurostat, Government sector accounts

## A2.2 Public expenditure on old-age pensions and unemployment benefits, 1995 and 2000

*% of total expenditure on social benefits*

	Old age pensions*			Unemployment benefits		
	1995	2000	% point change	1995	2000	% point change
EU15	44.8	46.4	1.6	8.4	6.3	-2.1
BE	43.1	43.8	0.7	13.0	11.9	-1.1
DK	37.7	38.1	0.4	14.8	10.5	-4.2
DE	42.7	42.2	-0.4	9.0	8.4	-0.6
EL	52.1	49.4	-2.7	4.5	6.2	1.6
ES	43.9	46.3	2.4	16.5	12.2	-4.3
FR	43.5	44.1	0.5	7.9	6.9	-1.0
IE	26.5	25.4	-1.1	15.3	9.7	-5.7
IT	63.4	63.4	0.0	3.0	1.7	-1.4
LU	45.1	40.0	-5.1	3.1	3.3	0.2
NL	38.0	42.4	4.4	9.9	5.1	-4.8
AT	48.4	48.3	-0.1	5.6	4.7	-0.9
PT	41.7	45.6	3.9	5.4	3.8	-1.6
FI	32.8	35.8	3.0	14.4	10.4	-3.9
SE	37.5	39.1	1.6	10.9	6.5	-4.4
UK	43.1	47.7	4.5	5.6	3.2	-2.4

\* Old-age pensions include survivors' benefits

Note: Except for DK, IE, LU, AT, all 2000 data are provisional or estimated

Source: Eurostat, ESSPROS

## A2.3 Public expenditure by function, 1995 and 2001

	% of GDP													
	Total		General services		Environment		Health		Education		Social protection		Other	
	1995	2001	1995	2001	1995	2001	1995	2001	1995	2001	1995	2001	1995	2001
EU15	52.9	46.9	8.2	6.8	0.8	0.7	6.2	6.3	5.2	5.0	20.0	18.8	12.5	9.3
BE	52.8	49.5	12.1	10.2	0.7	0.8	6.2	6.6	6.4	6.2	18.6	17.2	8.8	8.5
DK	60.3	55.3	10.8	8.6	0.0	:	5.1	5.4	7.7	8.3	26.8	24.0	9.6	9.0
DE	56.1	48.3	6.7	6.3	1.0	0.6	6.4	6.4	4.5	4.2	21.3	21.8	16.2	9.0
EL	51.0	47.8	16.8	10.9	0.5	0.6	3.4	3.7	3.3	3.1	18.3	19.4	8.7	10.1
ES	:	39.4	:	5.5	:	0.9	:	5.3	:	4.3	:	13.4	:	10.0
FR	55.1	52.5	6.3	6.4	1.1	1.3	7.9	7.9	6.3	6.0	21.5	20.4	12.0	10.5
IE	41.5	33.9	7.3	3.8	0.0	:	6.2	6.3	5.1	4.3	13.6	9.5	9.1	10.1
IT	53.4	48.5	14.1	9.6	0.7	0.9	5.5	6.4	4.9	5.0	18.7	17.8	9.5	8.8
LU	45.5	39.1	4.6	4.7	1.5	1.3	5.6	4.9	5.0	4.7	19.2	17.1	9.6	6.4
NL	56.4	46.6	10.0	8.2	0.8	0.7	3.9	4.1	5.1	4.8	20.7	17.5	15.9	11.3
AT	57.3	51.8	9.3	8.5	1.4	0.4	7.6	6.1	6.5	5.7	22.6	21.5	9.9	9.6
PT	45.0	46.2	8.7	6.7	0.4	0.7	5.3	6.8	6.5	7.0	12.5	13.6	11.6	11.4
FI	59.6	49.1	7.0	6.4	0.3	0.3	6.2	6.0	7.3	6.5	26.0	20.6	12.8	9.3
SE	67.7	57.1	11.9	8.8	0.2	0.3	6.4	6.8	7.1	7.3	27.2	23.8	14.9	10.1
UK	43.5	39.2	5.7	4.3	0.3	0.5	5.6	6.1	4.5	4.6	17.3	16.0	10.1	7.7

Note: For 1995, no data are available for ES; EU15 includes an estimate for ES

Source: Eurostat, Government sector accounts

## A2.4 Public expenditure by region in the UK, 2000-01\*

	North	N West	Yorks	E Midlands	W Mids	S West	East	London	S East	England	Scotland	Wales	N Ireland	UK
	<i>Expenditure per head (EUR)</i>													
<b>Social security</b>	3472	3212	2891	2706	2870	2732	2502	2712	2384	2781	3150	3303	3408	2856
<b>Education</b>	1218	1225	1216	1149	1217	1112	1148	1270	1097	1183	1523	1203	1695	1227
<b>Health</b>	1953	1950	1866	1682	1762	1781	1672	2293	1695	1861	2210	2138	2105	1911
<b>Roads+transport</b>	281	210	193	232	208	245	262	314	240	243	304	248	222	248
<b>Environment</b>	324	299	253	232	235	225	196	284	214	249	328	424	272	265
<b>Other</b>	1157	1117	1233	1028	1054	1013	1049	1524	944	1130	1606	1383	2837	1232
<b>Total</b>	8406	8012	7653	7028	7346	7108	6829	8397	6575	7446	9120	8698	10539	7740
	<i>% of regional GDP</i>													
<b>Social security</b>	17.2	14.1	12.6	11.1	12.0	11.5	9.2	7.1	8.3	10.4	12.4	15.7	16.8	10.9
<b>Education</b>	6.0	5.4	5.3	4.7	5.1	4.7	4.2	3.3	3.8	4.4	6.0	5.7	8.4	4.7
<b>Health</b>	9.7	8.6	8.1	6.9	7.4	7.5	6.2	6.0	5.9	7.0	8.7	10.2	10.4	7.3
<b>Roads+transport</b>	1.4	0.9	0.8	0.9	0.9	1.0	1.0	0.8	0.8	0.9	1.2	1.2	1.1	0.9
<b>Environment</b>	1.6	1.3	1.1	0.9	1.0	0.9	0.7	0.7	0.7	0.9	1.3	2.0	1.3	1.0
<b>Other</b>	5.7	4.9	5.4	4.2	4.4	4.3	3.9	4.0	3.3	4.2	6.3	6.6	14.0	4.7
<b>Total</b>	41.6	35.3	33.3	28.7	30.6	30.0	25.2	21.9	22.8	27.9	36.0	41.3	52.1	29.6
<b>GDP per head (EUR 000)</b>	20.2	22.7	23.0	24.5	24.0	23.7	27.1	38.3	28.8	26.7	25.3	21.0	20.2	26.1

\* 2000-01 financial year

Source: DG REGIO calculations based on Public Expenditure Statistical Analysis (PESA) 2002-03 and Eurostat, Regional accounts

## A2.5 Public expenditure by region in Italy, 2000

	Piemonte	Valle d'Aosta	Lom- bardia	Trentino Alto Adige	Veneto	Friuli Venezia Giulia	Liguria	Emilia Romagna	Toscana	Umbria	Marche	Lazio	Abruzzo	Molise	Campania	Puglia	Basilicata	Calabria	Sicilia	Sardegna	Italy
	<i>Expenditure per head (EUR)</i>																				
<b>Social security</b>	4302	4413	4070	3265	3530	4678	4976	4546	4216	4327	4009	4550	3601	3420	2713	3054	3200	3100	2920	3276	3769
<b>Education</b>	743	1103	725	1455	730	1009	933	804	939	920	777	1321	802	784	805	751	803	766	743	888	848
<b>Health</b>	1553	2224	1947	2121	1531	1680	1556	1742	1623	1785	1517	1586	1190	1395	1375	1359	1426	1354	1426	1548	1589
<b>Roads+transport</b>	558	1056	377	720	399	591	801	414	503	610	423	774	470	631	414	404	538	560	408	469	489
<b>Environment</b>	267	631	258	526	207	301	340	229	312	529	294	287	266	376	254	221	302	244	256	436	275
<b>Other</b>	4646	7964	6922	6766	3998	5564	5391	4705	4198	4302	4028	7341	3581	3489	3119	3278	4271	3243	3635	5125	4827
<b>Total</b>	12070	17391	14299	14854	10395	13823	13997	12440	11791	12473	11049	15858	9910	10096	8680	9067	10540	9267	9389	11742	11797
	<i>% of regional GDP</i>																				
<b>Social security</b>	18.2	18.1	15.2	12.1	14.9	20.7	23.4	17.7	18.8	21.7	19.8	20.3	21.8	22.0	21.0	23.0	22.1	25.4	22.7	22.0	18.7
<b>Education</b>	3.1	4.5	2.7	5.4	3.1	4.5	4.4	3.1	4.2	4.6	3.8	5.9	4.8	5.1	6.2	5.7	5.6	6.3	5.8	6.0	4.2
<b>Health</b>	6.6	9.1	7.3	7.8	6.5	7.4	7.3	6.8	7.2	8.9	7.5	7.1	7.2	9.0	10.7	10.3	9.9	11.1	11.1	10.4	7.9
<b>Roads+transport</b>	2.4	4.3	1.4	2.7	1.7	2.6	3.8	1.6	2.2	3.1	2.1	3.4	2.8	4.1	3.2	3.0	3.7	4.6	3.2	3.2	2.4
<b>Environment</b>	1.1	2.6	1.0	1.9	0.9	1.3	1.6	0.9	1.4	2.6	1.5	1.3	1.6	2.4	2.0	1.7	2.1	2.0	2.0	2.9	1.4
<b>Other</b>	19.7	32.7	25.9	25.0	16.9	24.6	25.4	18.3	18.7	21.5	19.9	32.7	21.6	22.5	24.2	24.7	29.5	26.5	28.2	34.5	23.9
<b>Total</b>	51.1	71.4	53.5	54.8	44.0	61.2	65.8	48.5	52.4	62.5	54.5	70.7	59.9	65.1	67.3	68.4	72.9	75.8	72.8	79.0	58.4
<b>GDP per head (EUR 000)</b>	23.6	24.4	26.7	27.1	23.6	22.6	21.3	25.7	22.5	20.0	20.3	22.4	16.5	15.5	12.9	13.3	14.5	12.2	12.9	14.9	20.2

Note: Public expenditure includes spending by public corporations as well as by General Government; figures in bold relate to Objective 1 regions.  
Source: DG REGIO calculations based on MEF-DPS (2002), TPA database and Eurostat, Regional accounts

## A2.6 Public expenditure by region in Spain, average 1992-1999

	Galicia	Asturias	Cantabria	Pais Vasco	Navarra	La Rioja	Aragón	Madrid	Castilla y León	Castilla-La Mancha	Extremadura	Cataluña	Valencia	Illes Balears	Andalucía	Murcia	Ceuta y Melilla	Canarias	Spain	
	1637	1703	1695	2298	2221	1635	1741	1545	1755	1656	1816	1546	1458	1365	1592	1560	1499	1850	1648	
Health, social services, basic territorial financing	172	272	323	183	189	144	267	158	232	287	247	133	187	220	209	240	358	201	196	
Law+order, housing, transport	187	218	207	358	303	332	278	314	286	242	235	250	193	249	204	171	489	244	246	
EU+other regional aid	95	442	48	51	60	36	53	9	95	88	204	24	46	16	164	52	67	611	105	
Total	2091	2635	2274	2890	2773	2147	2339	2026	2367	2273	2502	1953	1883	1850	2169	2024	2413	2907	2195	
																				% of regional GDP
Health, social services, basic territorial financing	17.0	15.8	14.8	15.8	14.6	11.8	13.1	9.8	15.6	16.5	22.7	10.4	12.5	9.0	17.7	15.0	14.6	15.8	13.6	
Infrastructure	1.8	2.5	2.8	1.3	1.2	1.0	2.0	1.0	2.1	2.9	3.1	0.9	1.6	1.4	2.3	2.3	3.5	1.7	1.6	
Law+order, housing, transport	1.9	2.0	1.8	2.5	2.0	2.4	2.1	2.0	2.5	2.4	2.9	1.7	1.7	1.6	2.3	1.6	4.7	2.1	2.0	
EU+other regional aid	1.0	4.1	0.4	0.4	0.4	0.3	0.4	0.1	0.8	0.9	2.5	0.2	0.4	0.1	1.8	0.5	0.7	5.2	0.9	
Total	21.7	24.4	19.8	19.9	18.2	15.5	17.6	12.8	21.0	22.6	31.2	13.2	16.1	12.2	24.1	19.4	23.4	24.8	18.1	
GDP per head (EUR 000)	14.6	16.0	18.1	22.9	23.8	20.6	19.9	24.9	17.2	15.1	12.0	22.5	17.9	22.2	13.8	15.5	15.4	17.5	18.6	

Note: Figures in bold relate to Objective 1 regions

Source: DG REGIO calculations based on Intervención General de la Administración del Estado (IGAE) and Eurostat, Regional accounts

## A2.7 Receipts from taxes and social contributions by level of government, 1995 and 2001

*% of total receipts*

	Central govt		Social security		Regional+local govt	
	1995	2001	1995	2001	1995	2001
<b>EU15</b>	49	52	36	34	15	15
<b>BE</b>	60	60	34	33	7	7
<b>DK</b>	66	62	3	4	31	34
<b>DE</b>	30	29	43	42	27	28
<b>EL</b>	66	67	33	32	1	1
<b>ES</b>	51	48	36	36	13	16
<b>FR</b>	43	42	46	48	10	9
<b>IE</b>	83	84	15	14	3	2
<b>IT</b>	60	56	32	29	8	15
<b>LU</b>	67	67	27	27	6	6
<b>NL</b>	57	61	40	36	3	4
<b>AT</b>	45	49	35	32	20	19
<b>PT</b>	64	63	31	31	5	6
<b>FI</b>	46	51	32	27	22	22
<b>SE</b>	43	43	27	27	30	29
<b>UK</b>	79	79	17	17	4	4

*Note: Data for Portugal for 2001 relate to 2000. Central government includes EU taxes.*

*Source: Eurostat, Government sector accounts*

## A2.8 Distribution of inward FDI by region in selected EU countries

	% of country totals				
Germany	1998-2000	Spain	1999-2001	Italy	2000
Nordrhein-Westfalen	37.5	Madrid	69.5	Lombardia	43.5
Hessen	21.6	Cataluña	13.6	Piemonte	14.9
Baden-Württemberg	11.7	País Vasco	5.5	Lazio	8.4
Bayern	9.0	Other regions	3.0	Emilia-Romagna	7.8
Hamburg	7.7	Com. Valenciana	2.7	Veneto	4.7
Niedersachsen	3.3	Canarias	2.7	Toscana	4.3
Berlin	2.8	Andalucía	1.2	Friuli-Venezia-Giulia	4.0
Rheinland-Pfalz	1.9	Galicia	0.5	Abruzzo	3.3
Schleswig-Holstein	1.6	Baleares	0.4	Liguria	1.9
Sachsen-Anhalt	1.0	Aragón	0.3	Trentino Alto Adige	1.5
Bremen	0.5	Navarra	0.3	Umbria	1.2
Brandenburg	0.3	Asturias	0.1	Campania	1.2
Sachsen	0.3	Castilla-La Mancha	0.1	Puglia	0.8
Saarland	0.3	Castilla y León	0.1	Sicilia	0.8
Thüringen	0.3	Murcia	0.1	Marche	0.7
Mecklenburg-Vorpommern	0.2	Extremadura	0.0	Sardegna	0.4
		Rioja	0.0	Valle d'Aosta	0.4
		Cantabria	0.0	Basilicata	0.2
		Ceuta y Melilla	0.0	Molise	0.0
				Calabria	0.0

Notes: Figures for Italy refer to the number of employees in foreign-owned manufacturing subsidiaries; it should be emphasised that employment is attributed to regions according to the location of headquarters and not branches. They are, therefore, only indicative of the actual regional distribution.

Figures relate to average 1998-2000 for Germany and average 1999-2001 for Spain.

Source: DE — Bankgesellschaft Berlin based on Deutsche Bundesbank; ES — Foreign Investment Register; IT — CNEL, FDI database (R&P — Politecnico di Milano)

**A2.9 Inward FDI into the EU15 and the accession countries, average 1999-2001**

	% of GDP		% of GDP
<b>EU15</b>	6.9	<b>BG</b>	5.4
<b>BE/LU</b>	8.5	<b>CY</b>	5.8
<b>DK</b>	14.6	<b>CZ*</b>	9.2
<b>DE</b>	4.9	<b>EE</b>	7.8
<b>EL</b>	0.9	<b>HU</b>	4.2
<b>ES</b>	1.5	<b>LT</b>	3.9
<b>FR</b>	3.5	<b>LV</b>	4.4
<b>IE</b>	20.7	<b>MT</b>	15.8
<b>IT</b>	1.1	<b>PL*</b>	4.4
<b>NL</b>	13.2	<b>RO</b>	3.8
<b>AT</b>	3.1	<b>SI</b>	1.7
<b>PT</b>	4.3	<b>SK</b>	8.8
<b>FI</b>	4.6		
<b>SE</b>	13.0		
<b>UK</b>	5.9		

*BE/LU: data are for 1998; DK: data are for 1999-2000;*

*ES: data for 1998-1999; RO: data are for 1997-1999;*

*HU, SK: data are for 2000-2001*

*\*CZ and PL account for 23% and 35%, respectively, of all FDI in the accession countries.*

*Source: Eurostat, Balance of payments statistics; UNCTAD for Greece*

## A2.10 Distribution of inward FDI by NUTS 2 region in selected new Member States

Czech Republic	2001	Hungary	2001	Poland	1998	% of country totals	
						Slovakia	2001
Praha	49.3	Közép-Magyarország	67.7	Mazowieckie	24.3	Bratislavský	63.2
Střední Čechy	10.7	Közép-Dunántúl	9.4	Śląskie	13.5	Východné Slovensko	18.8
Jihozápad	7.6	Nyugat-Dunántúl	7.5	Wielkopolskie	11.6	Západné Slovensko	10.3
Severozápad	8.2	Észak-Magyarország	6.2	Dolnośląskie	8.4	Stredné Slovensko	7.7
Severovýchod	6.6	Dél-Alföld	4.0	Pomorskie	7.3		
Jihovýchod	8.4	Észak-Alföld	3.5	Łódzkie	5.9		
Střední Morava	5.2	Dél-Dunántúl	1.8	Małopolskie	5.6		
Moravskoslezsko	4.0			Kujawsko-Pomorskie	4.1		
				Zachodniopomorskie	3.9		
				Lubelskie	2.8		
				Podkarpackie	2.5		
				Świętokrzyskie	2.3		
				Warmińsko-Mazurskie	2.3		
				Lubuskie	2.2		
				Opolskie	1.8		
				Podlaskie	1.6		

Source: National statistical sources

