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ABSTRACT

Title: The Two Sides of the Same Coin: Is Fiscal Decentralization Threatening Regional Convergence? Evidence for Spain.

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Abstract: *The link between fiscal decentralization and economic growth is a work-horse field of research which has historically arrived to ambiguous conclusions. Nevertheless, less is known about the regional consequences of an asymmetric decentralized system as in the case of Spain. In this article, we provide evidence for the literature evaluating the two-extreme-cases regions (The Basque Country and The Valencian Community) in terms of how they have been benefited/harmed, after the approval of their respective more recent critical laws regarding the Spanish fiscal decentralization process: (i) the Basque Economic Agreement (BEA, hereinafter) approved in 2002 and (ii) the 2001-model within the common financing system. To undertake this analysis, we develop our empirical strategy based on diff-in-diff regression and the Synthetic Control Method for comparative case studies. The usage of these methodologies constitutes one of the main novelties in this article since the literature of fiscal decentralization has been, historically, dominated by panel methods such as: IV, GMM or Fixed effects models. We intend to demonstrate that an asymmetric fiscal decentralized system, based on cultural or political reasons rather than economic ones, is not innocuous for the economic development of a given region and it has quasi-permanent consequences in terms of convergence for the whole country. We find the BEA approved in 2002 would have increased importantly the Basque Country level of GDP per capita under diff-in-diff regression and under Synthetic Control method. Conversely, we also find that the approval of the 2001-model, within the common financing system, has implied a considerably reduction in the Valencian level of GDP per capita, also under both methods.*

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Keywords: *foral regime, common regime, difference-in-differences, synthetic control method, GDP per capita*

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