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The Monitoring Review of Switzerland: Assessment and Recommendations

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MONITORING REVIEW OF SWITZERLAND: ASSESSMENT AND RECOMMENDATIONS

Regions in Switzerland are very successful...

1. Regions in Switzerland show high levels of GDP *per capita*, a variety of strong economic sectors (as measured by their exporting performance) and a highly educated population, particularly in Région Lémanique (36.1% in 2006) and Zurich (37.7%). They have high levels of knowledge-intensive employment, especially in Zurich, and high-tech manufacturing in North West Switzerland. Swiss regions score very high on patent applications, especially cantons such as Basel-Stadt. Moreover, they could be considered leaders in green growth. They are at the forefront of innovation in green technologies, such as energy efficiency and pollution abatement.

...facing fewer development challenges than many regions within the OECD...

2. The policy challenges with respect to regions in Switzerland are moderate in comparison with those in many OECD countries. The dichotomy between urban and rural areas is relatively limited: most people live in intermediate regions, cities are relatively small and rural areas are not as remote as in many other OECD countries. Although mountains impose certain geographical barriers, areas in Switzerland are not far removed from cities and towns. Inequality between regions is relatively limited and every area can be considered to have at least adequate access to public and private services. Although the GDP per capita in urban regions is higher than in rural areas, its level in all Swiss regions remains very high in comparison with most OECD regions. De-population of rural cantons (or other cantons, for that matter) is not observed, and the challenges of ageing are but less acute than in several other OECD regions. All these elements suggest that some of the policy challenges that other OECD countries face with respect to regional development are absent from Switzerland.

...but confronted with lagging productivity growth

3. Although the level of labour productivity in Swiss regions is relatively high, labour productivity growth over the last decade has been lagging. The growth in labour productivity over 1998-2005 was on average 2.2% in predominantly urban regions, against 1.7% in intermediate regions and 1.5% in predominantly rural regions, well below the growth rates of many OECD regions. A substantial part of the labour productivity growth differences in Switzerland can be explained by different regional economic specialisations: urban regions tend to be specialised in sectors that have higher labour productivity growth rates. In addition, there is a strong correlation between the share of high- and medium-high tech employment in 2006 and the labour productivity growth over 1998-2005 in the seven *Grandes Régions* in Switzerland. Despite relatively small inter-regional differences in economic and labour market performance, urban regions have higher labour productivity growth rates. These urban cantons are highly interlinked, both with each other and with other cantons in Switzerland, not least because of small distances and good connectivity. This provides an opportunity for regional policy in Switzerland to foster competitive assets of the regions that are lagging by making use of the linkages they have to other regions. Regional policy could take into account the increasing poly-centricity of Swiss regions and capitalise on urban-rural linkages.

Functional regions do not correspond to administrative regions

4. Switzerland is a federal country with many responsibilities at the level of the 26 cantons. In addition, regions are statistically defined at the level of seven *Grandes Régions*, comprising several cantons, with the exception of Zurich and Ticino. In practice, sub-cantonal territories are also referred to as regions in the regional policies developed by cantons. Yet while cantons play a key role in policy making, they cannot be considered the real functional areas. Functional regions are those areas in which most daily activities, such as economic and social activities of citizens and firms take place. They can be defined by several indicators, including: i) commuting flows, ii) overlapping specialisations, iii) knowledge spillovers, and iv) economic interlinkages. These indicators suggest that functional realities in Switzerland do not follow cantonal boundaries.

- i. **Commuting flows** confirm the existence of labour markets that exceed cantonal boundaries. Commuting forms one of the elements of the OECD definition for functional metropolitan regions: neighbouring regions that have net commuting rates of 10% or higher are in this definition considered to be one functional labour market area. In 2000, Switzerland counted 12 cantons with net commuting rates higher than 10%. They make up three different integrated labour markets, around Basel, Bern and Zurich respectively. In the remaining, mostly rural, cantons net commuting flows to other cantons are limited.
- ii. Several regions in Switzerland have **clusters in common**, most notably Zurich, Espace Mittelland and Central Switzerland. They all have at least three economic specialisations in common with each other. This suggests that these clusters spread out over a wider area than defined by the boundaries of the seven *Grandes Régions*. Considering these overlapping specialisations, it is not surprising to find that several regions in Switzerland, especially Zurich, Espace Mittelland and Central Switzerland, face the same European regional “competitors” for talented people and investment in the same sectors, which could also be considered cross-border extensions of Swiss clusters.
- iii. Several regions are highly linked through **co-patents**, which point to the existence of inter-regional knowledge spillovers. In absolute terms, the most important regional linkages through co-patents in 2007 were between North-West Switzerland and Zurich; North-West Switzerland and Espace Mittelland; and Zurich with East Switzerland. This would suggest relatively high functional relationships between the larger metropolitan areas of Zurich and Basel. Foreign co-patent data confirm the existence of a large functional metropolitan area in Northern Switzerland. The main foreign regions with which actors in three Swiss regions (Espace Mittelland, North West Switzerland and Zurich) are linked through co-patents are remarkably similar. Baden-Wuerttemberg, Bayern and Alsace are the dominant partner regions for all these three regions, making up between 30 and 60% of their foreign co-patents.
- iv. **Similarities in business cycles** suggest that Switzerland consists of three or four large functional metropolitan areas, plus a limited number of more remote areas. Data on average cantonal income per capita over 1990-2005 show that there are broadly four areas in which cantonal business cycles are highly similar: greater Geneva, greater Bern, greater Basel and greater Zurich. The functional areas of greater Basel and greater Zurich are to a large extent interrelated, as illustrated for example by the similarities between business cycles of Basel-Stadt and Zurich, St. Gallen and Argau. Basel-Stadt, however, is also interrelated with other cantons (Jura and Solothurn) that do not show similarities in business cycles with the cantons of greater Zurich. There are seven remaining cantons in which business cycles are relatively unrelated to each other.

Switzerland has reformed regional policy to promote the regions' competitiveness and export capacity

5. While old regional policy in Switzerland used infrastructure investment and loans to attract firms to mountainous and rural regions, the focus of policy shifted during the 1990s towards efficiency and the creation of value added. This change, which was in line with trends in many OECD countries, was formalised with the introduction of New Regional Policy (NRP) in 2008, which largely leaves the task of reducing inter-regional financial disparities to the reformed fiscal equalisation system (introduced in 2008). The three pillars comprising the NRP offer an appropriate set of instruments to effect this change: direct support for strategic regional development programmes, complemented by mechanisms of co-ordination with other policies, and supported by policy intelligence tools. The combination of these three pillars is expected to help maximise the overall impact of the NRP.

However, the content of the NRP does not always correspond to its stated aims

6. The spirit of the NRP signals a departure from a primarily infrastructure-led approach towards a closer integration between hard and soft capital investment. At the same time, the stated goal of strengthening regional innovation capacity has coexisted with partial focus on supporting sectoral projects. A better fit between the content of the NRP and its objectives, as well as more effective implementation, could be sought along four lines of action briefly reviewed below: (i) extending NRP coverage to all regions; (ii) increasing inter-cantonal policy co-ordination; (iii) better co-ordinating the NRP with sectoral policies; and (iv) building strategic management and evaluation capacity.

(i) NRP coverage should be extended to all regions

7. In contrast to the effort of many OECD countries to tap the specific growth potential of all regions rather than subsidising the poorest, the NRP continues to apply only to rural and mountainous regions. Urban areas have been eligible for federal support through a separate agglomeration policy since 2001. Agglomeration policy covers a heterogeneous spectrum of urban areas ranging from the five main urban centres to other "agglomerations", which include towns in predominantly rural regions covered by NRP in principle. A dedicated infrastructure fund has been set up, mainly to cover transport investment, while another fund supports innovative "model projects". The separation of programmes despite the overlap between the areas covered by the NRP and agglomeration policy represents a missed opportunity to exploit the increasing interlinkages between urban, intermediate and rural areas.

8. NRP would gain in coherence if it covered all regions. The Swiss federal system guarantees substantial autonomy to the cantonal and local levels. The current split between the NRP and agglomeration policy contributes little to reducing institutional and policy fragmentation and might ignore or even hinder existing interdependencies among territories. Extended NRP coverage could help to address the challenges of polycentric regions and urban-rural interrelationships. In practice, the various instruments are sometimes brought together under a single coherent strategy at the sub-national level, where they are often being handled by the same actors.

(ii) More can be done to increase inter-cantonal policy co-ordination

9. NRP implementation programmes tend to address individual cantons, which raises issues of capacity and economies of scale. Following the elaboration of a federal multi-year programme that sets the overall strategic orientations, cantons have been invited to submit an implementation programme to apply for funding (all but three participated in 2007). Implementing the policy shift put forward by the NRP

requires skills and capabilities that vary across cantons. Some cantons responded quickly to the NRP requirements, whereas others experienced difficulties and delays, sometimes due to the legislative framework that needed to be put in place. The high level of turnover among regional policy actors in the cantons opens opportunities to cultivate a new mindset, but it also entails a risk of losing skills and institutional memory. Some rural areas do not necessarily perceive themselves as part of larger functional areas despite their geographic proximity and economic interaction. This may then translate into isolated choices favouring small-scale projects.

10. Inter-cantonal co-operation is essential to tackle regional growth challenges but current mechanisms are not fully effective. Key determinants of regional economic growth such as inter-firm linkages, transport connections and education spillovers tend to go beyond the cantons' administrative boundaries. A variety of inter-cantonal platforms for information exchange and harmonised solutions in public service delivery have been established, but co-ordination mechanisms have often remained sectorally focused and the large number of such mechanisms has raised concerns about the transaction costs involved. At the same time, the democratic legitimacy of inter-cantonal bodies has sometimes been questioned. NRP funding set aside for inter-cantonal co-ordination has also remained underused. The NRP could have a clearer and stronger focus on promoting inter-cantonal projects. For example, increased (or even exclusive) funding of inter-cantonal projects within the NRP could be considered. The federal government, through Regiosuisse, could also finance evaluations to assess which co-ordination mechanisms appear to work best for specific economic development activities and encourage cantons to use them via financial incentives.

(iii) Regional and sectoral policies can be better co-ordinated

11. Increasing the impact of the NRP does not necessarily require additional funding so much as more effective co-ordination with (and leveraging effect on) other policies. The Conference of the Confederation for Territorial Organisation (COT) was created in 1998 to bring together all federal actors that implement policies with a territorial impact; it currently meets four times a year under the joint authority of the State Secretariat of the Economy SECO and the Federal Office for Spatial Planning ARE. Pillar 2 of the NRP specifically aims to co-ordinate the NRP with different sectors. Agreements have been established recently in areas such as innovation, environment and tourism to foster exchanges of information and the development of common projects. While such measures represent a necessary step in the direction of reducing programmatic redundancy and enhancing co-ordination across federal activities, the differences in the actors targeted and the nature of the instruments leave important gaps to be bridged.

12. Greater alignment of the NRP, agglomeration policy and agricultural policy could help realise policy complementarities. Despite efforts to prevent any duplication between model projects under agglomeration policy and NRP projects, some "blind spots" remain. For example, economic promotion for four important clusters in Berne – ICT, medical technology, precision engineering, and services – is not included in the NRP as they tend to be located in urban areas, whereas NRP focuses on agriculture and tourism. There is also a disconnection between income support to farmers via direct payments, which account for over 70% of the agricultural policy budget, and innovation-oriented NRP projects at the cantonal level as well as other federal programmes. Such concerns have been partly addressed by the creation of the Federal Network for Rural Development in 2006. Cross-sectoral co-ordination could be further improved by linking formally or merging the NRP and agglomeration policy, expanding joint agreements and projects between the NRP and agricultural policy, and further using spatial planning instruments in the service of sustainable economic development strategies.

(iv) Strategic management and evaluation capacity needs to be strengthened

13. The monitoring and evaluation system needs to be strengthened in a way that does not inflate federal control at the expense of cantonal autonomy but allows for more strategic guidance. The federal criteria for evaluating implementation programmes should be public and clear prior to submission by cantons. The programme agreements established between levels of government should be seen both as a way to specify the responsibilities of the parties to ensure that sub-national programmes are consistent with NRP logic, as well as a learning tool for diffusing best practices. Finally, the education and training activities of Regiosuisse could be further developed based on an assessment of stakeholders' needs.

14. Given the difficulties that the Confederation already faces in gathering information from cantons for monitoring purposes, introducing sanctions may exacerbate cantons' reluctance to provide data and encourage gaming. Instead, attention could be given to refining the indicator system to better enable the Confederation to provide strategic assistance to cantons and regions. The limited knowledge regarding the "right indicators" to monitor and the need for flexibility have been rightly acknowledged by the federal government. Information produced through the first round (2008-2011) should therefore be used to refine the monitoring system and establish a core set of indicators with clear definitions linked to annual reports.

Switzerland is a leading country in science, technology and innovation, but there are signs of stagnation

15. Switzerland is a leading country in innovation, especially on the high-tech side. Many large Swiss companies are world leaders in pharmaceuticals, biotechnology, medical technology, machinery and equipment, and other high-tech goods. The framework conditions for innovation are excellent, but there is a tendency for R&D investments and innovation outputs to stagnate. Moreover, innovation is more than science and technology. Data collected in Switzerland through innovation surveys underscore the importance of "innovation without R&D", and the fact that innovation is a multi-faceted phenomenon, involving many other investments and capacities at the firm level. Untapped potential exists in traditional sectors, in intermediate and rural regions: small firms with lower absorptive capacities could further develop into innovative ventures and contribute both to sustained national growth and to balanced territorial development.

Reinforcing innovation promotion at regional level could help improve overall economic performance.

16. The NRP introduces innovation promotion as an important component of regional policy, an evolution from the previous focus on infrastructure provision. This orientation is highly relevant to ensure widespread growth throughout the whole country, through an expansion of innovative activities beyond the sectors and companies currently involved in innovation. The polycentric territorial development model adopted by Switzerland functions well and provides good framework conditions for a policy aiming at wider innovation diffusion, in contrast with the situation in very centralised countries, where resources tend to be overly concentrated in the capital. The rich potential for cross-border cooperation beyond the country's borders adds to the possibilities for regions to become actors in innovation promotion. Several Swiss cantons are engaged in cross-border partnerships, and could develop their collaboration further in the domain of innovation, through, e.g. the establishment of innovation advisory services that tap into resources across the borders, or the encouragement of technology transfer practices implemented at the level of these border regions.

Since federal policy supports science-driven innovation, the regions could support other types of innovation

17. The Confederation has adopted a robust and effective science and technology policy, based on a market failures rationale. This policy is largely (and justifiably) spatially blind. Federal innovation policy, and in particular the instruments deployed by the Swiss Innovation Promotion Agency (CTI), address very well the needs of the science- and technology-based innovators. Companies with lower absorptive capacities, innovating without R&D, or involved in other forms of innovation (e.g. organisational innovation) are not a target of federal policy. To serve their needs, proximity matters: they should become the target of regional innovation policies and supported under the NRP. In other words, within the “innovation triangle” of knowledge creation-diffusion-absorption, federal policy addresses the first two elements: knowledge creation and diffusion. This points towards a potential role for sub-national authorities in addressing knowledge absorption bottlenecks.

18. A clearer division of labour for a multi-level innovation policy needs to be defined along these lines. The federal level would maintain its country-wide policy focused on knowledge creation and technology transfer for technology-driven innovation, while the sub-national level would take up an active role in knowledge absorption and diffusion. In this framework, the federal level would concentrate its role on the core activities of CTI, which have proven effective: supporting technology transfer and joint public-private R&D projects, on the basis of excellence and relevance, across the whole country, relying on strong technology transfer networks when they exist. The Knowledge and Technology Transfer Networks (KTT) would in this view acquire a national dimension and their specialisation be reinforced. The role of the federal level would remain concentrated on knowledge creation and diffusion. Functional regions would be in charge of innovation promotion in the wider sense and address knowledge absorption needs: this would be done by establishing networks of innovation promotion agencies and advisors, covering the local and cantonal dimensions, coordinated and quality-controlled at the level of the functional region. This mission includes linking with KTT when technology needs are at stake. The target groups for the federal level should be innovative, technology-advanced companies, while the target groups for the regions should be the companies innovating in a learning-by-doing and learning-by-interacting mode.

Existing cantonal initiatives need to be better coordinated and more efficiently implemented...

19. There are no explicit regional innovation policies in Switzerland. A large number of uncoordinated and very diverse innovation-promotion initiatives are developed and implemented by the cantons, as part of their economic development mission. The NRP helps to reveal and provides a boost to those initiatives. The type of innovation support developed at cantonal level is complementary to federal instruments, as it involves advice and support for start-ups, small companies, networks and technology transfer activities on a sub-national scale, based on proximity relationships. There is a lack of visibility and quality assessment of those dispersed initiatives. There are also cases where unnecessary competition and lack of coordination take place between federal and cantonal initiatives, e.g. in start-up support.

...and can form the basis for inter-cantonal initiatives, especially in cross-border areas

20. The inter-cantonal level emerges as the most relevant for innovation promotion on a sub-national scale: only few initiatives are implemented at this level, but they demonstrate the possibility to overcome barriers for inter-cantonal cooperation in innovation. The NRP should use its leverage potential on inter-cantonal cooperation by increasing the share of funding dedicated to inter-cantonal projects. The launch of RIS-like exercises could help move towards this target. The cross-border dimension of regional innovation policies should be given more prominence in regional actions, taking examples from successful cases and

introducing indicators of results and outcomes to demonstrate the value-added of the initiatives. The territorial definition for regional innovation policy under the NRP should be extended to cover agglomerations, since these play a key role in innovation. This would facilitate the establishment of integrated regional innovation policy initiatives.

Strategic management capacities for innovation policy need to be built

21. Capacity gaps are present, at both federal and cantonal levels, when it comes to the conduct of innovation policies with a regional dimension. There is a need to develop a more strategic view of regional innovation-promotion activities. The system would benefit from a clarification on where the best local competences in innovation promotion lie and from more visibility of available services in given territories and throughout the country. This would help address the limits of small-scale, disconnected initiatives, and support the selection process for NRP funding. Evaluation practices should be reinforced and linked to funding. Evaluation of funded regional innovation projects would need to take place in order to increase their impact and ensure that the stated objectives are met at project and programme levels. Companies' views should be integrated in the strategic approaches to innovation promotion. In the midst of the efforts to establish a multi-level innovation policy where regions, cantons, functional regions and the federal state play complementary roles, the views of companies, who are the key actors for innovation, are almost absent. Opportunities for learning and exchange across cantons and functional regions should also be exploited further.