

OECD Territorial Reviews: Milan, Italy

Is Milan's economic drive at risk?

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Introduction

Milan ranks among wealthy OECD metropolitan regions and is often identified with the "Made in Italy" brand on the international arena, notably for fashion and design. Once a successful industrial city, Milan has grown into the core of a wider industrial metropolitan region that is home to more than 7 million people. Industrial activities still drive the region's periphery while the centre of Milan is veering towards becoming a service platform for a significant share of northern Italy. Milan's historical skills endowment and its advantageous geographic location could underpin its ambition to become a southern European and Mediterranean capital, supplying advanced services and new technologies while remaining an international capital of fashion and design.

However, both external and internal challenges are putting strains on Milan's aspirations. On the external front, increasing global competition has revealed the limits of Milan's historical lead and the need to support the renewal of its comparative advantages. On the internal front, public goods and services such as transportation have not kept pace with the continuous urban sprawl and the widening commuting flows across the metropolitan region. This has led to a deterioration of the region's liveability, hampering the region's buzz and capacity to attract knowledge workers.

Failure to accelerate the innovation process and to enhance the region's attractiveness could prove costly. Milan needs to capitalise on its advanced services and functions to bolster regional innovation dynamics and to fuel national growth. Rapid metropolitan governance reforms will help design and implement a competitiveness strategy for the entire metropolitan region.

This Policy Brief looks at some of these challenges and at the possible solutions put forward in a new *OECD Territorial Review of Milan*. ■

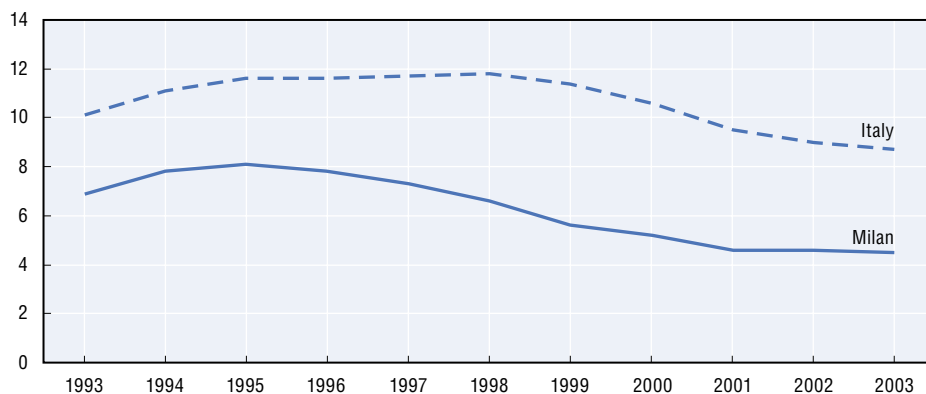
Is Milan's economic drive at risk?

Milan has long enjoyed an outstanding industrial history and the aura of a global city. Its past and present prosperity has been underpinned by a well-educated and relatively young labour market, a lively entrepreneurship pool, and networks of dynamic small firms. Milan's unemployment rate has remained consistently below national average over the 1993-2003 period (Figure 1). In the international arena, Milan stands out as a major commercial partner in the European market through particularly dense linkages with Germany and France (which accounted for almost 25% of its exports and more than 40% of its imports in 2004). Milan also took in more than 40% of the foreign direct investment (FDI) that came into Italy in 2004.

However, both external and internal challenges are putting a question mark over Milan's future competitiveness.

- On the external front, the upsurge of countries that combine both lower labour costs and promising technological capacities increasingly demands faster and more comprehensive innovation from Milanese firms. In this respect, Milan has retained a relatively modest profile. First, Milan suffers from the lack of a well-structured and coherent innovation policy for its metropolitan area. Following the restructuring of large companies during the 1980-1990s, Milan's productive fabric has been mostly composed of SMEs (the average size of firms has dropped from a 100 index in 1981 to 73.5 in 2001), which has contributed to delaying investment in research and development (R&D) compared with European competitors. The Lombardy region where Milan is situated spent consistently less than other leading European regions such as Paris-Ile-de-France, London, Baden-Württemberg in Germany and Lyon-Rhône-Alpes in France between 1998 and 2000. Second, SMEs have seen few incentives to patent their innovations. Lombardy generated far fewer patent registrations in high-technology sectors than the above-mentioned leading European regions during the 1998-2002 period.
- On the internal front, continuous urban sprawl and widening commuting flows have generated significant gridlocks across the enlarged metropolitan region. The shortage of housing and the ensuing prohibitive costs in the core of Milan pushed hordes of workers out into the periphery. These new commuters soon turned to private vehicles to reach their workplace as the deficit of suburban public transport infrastructure aggravated road congestion. Milan is now choking under critical transport bottlenecks even though mobility determines the region's quality of life, attractiveness and competitiveness. Not only is Milan a heavily polluted city, which affects its future capacity to attract workers and visitors, but its unique potential to build a comprehensive engine for innovation with regional, national and international spillovers may fade away.

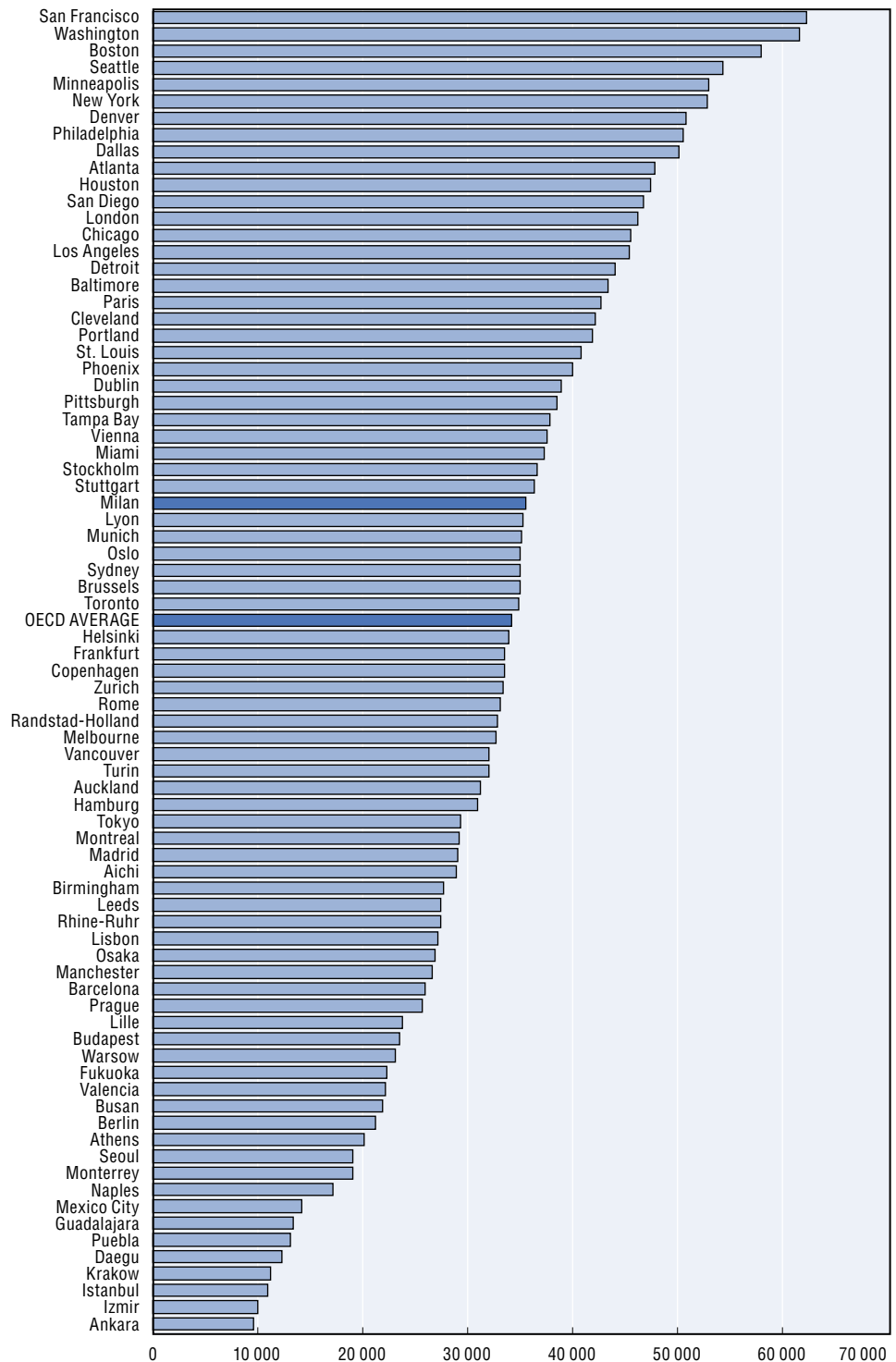
Figure 1.
UNEMPLOYMENT RATES
IN MILAN AND ITALY
1993-2003, %



Source: Istat.

Amid an already sluggish economic background, the Milan metropolitan region, home to more than 7 million people, displays disappointing international performances: it ranked only 30th out of 78 OECD metropolitan regions in terms of gross domestic product (GDP) per capita in 2002 (Figure 2). Moreover, the

Figure 2.
GDP PER CAPITA IN
78 OECD METROPOLITAN
REGIONS (2002)
 Unit: USD PPP



Source: OECD Metropolitan Database.

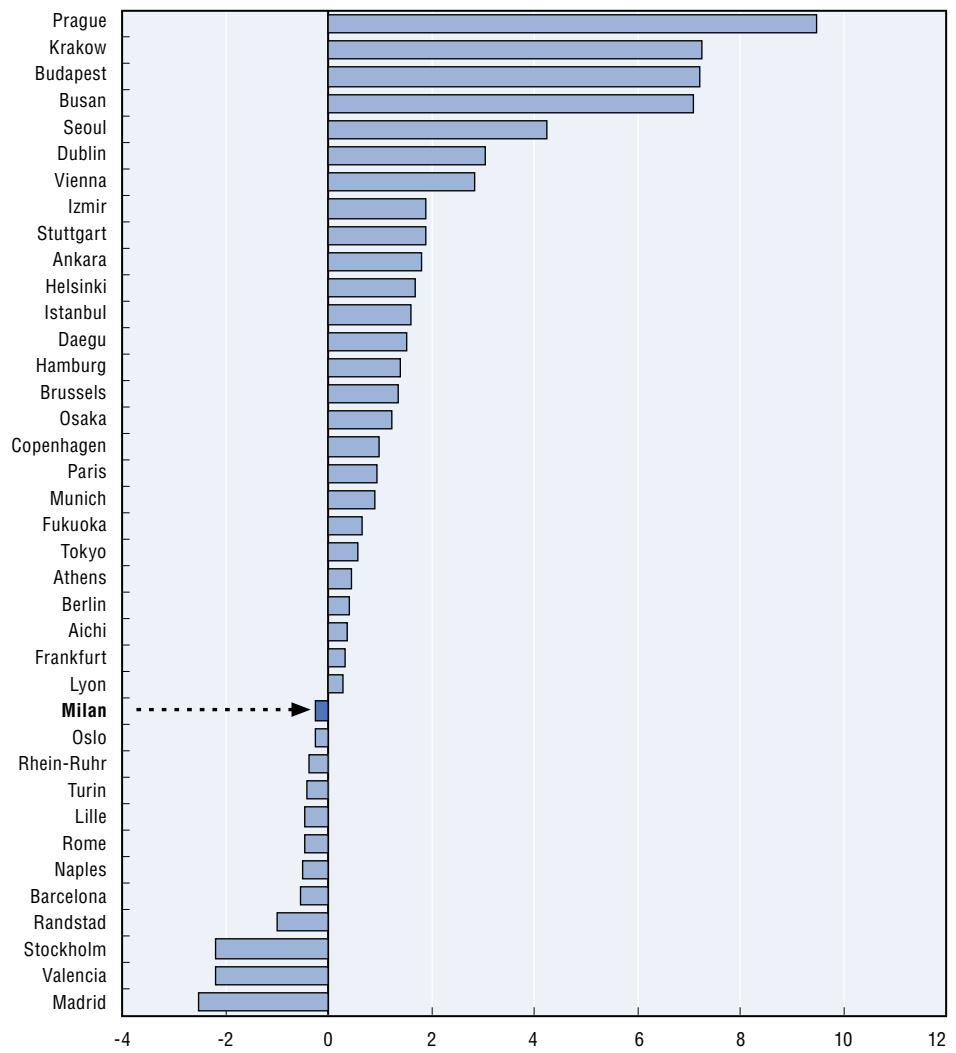
region's capacity to step up the pace appears unclear as its labour productivity growth has been negative over the 1999-2002 period, in contrast with many European regions including Helsinki, Copenhagen, Frankfurt and Lyon (Figure 3).

Milan seems to have lost part of the historical drive it had built on past investments. Therefore, it may fall behind other European regional capitals in the long term if it fails to meet its challenges fully and rapidly enough. If Milan is to be upgraded into a creative service hub interwoven with a vibrant industrial fabric, rapid action will be required to: (i) bolster its innovation dynamics and attractiveness; and (ii) support the reform process via more inclusive governance mechanisms. ■

How can Milan capitalise on its high value-added functions?

Policies to better exploit and diffuse Milan's advanced functions could give a fresh impetus to the regional innovation dynamics and generate important spillovers at the national level. Few areas in OECD countries are able to replicate Milan's well-balanced production framework, for example. The Milan metropolitan region's industrial fabric is both specialised and diversified, which has helped to compensate for the negative effect of sectoral crises. Several networks of specialised and complementary SMEs excel in light industries such

Figure 3.
AVERAGE ANNUAL LABOUR PRODUCTIVITY GROWTH IN 38 OECD METROPOLITAN REGIONS (1999-2002)
Unit: %



Source: OECD Metropolitan Database.

as furniture, metal engineering and electric equipment, as well as mechanics. At the same time, the core area of Milan hosts clusters of knowledge-intensive activities such as ICT and biotechnology and fulfils high value-added functions that shape various phases of a product's life cycle and generate spillovers into multiple supply chains. Milan could renew itself as a strategic powerhouse for a large part of Italy and beyond by permanently upgrading and refining its creative brainpower. This challenge is illustrated below along three axes: business services, breakthrough innovation activities, and internationally visible assets.

- **Business services** could be better exploited and upgraded, as innovation not only implies product and process advancement but also organisational improvements. This task is particularly relevant in Italy where SMEs produce quality items but may lack the capacity to enhance sophisticated skills. The core area of Milan already generates services that may help improve the abilities of SMEs: industrial design thanks to the agglomeration of highly skilled designers; financial services with the headquarters of the largest Italian banks; communication services using marketing and advertising companies, as well as the high concentration of the media industry; promotion and sales services based on one of the world's most competitive exhibition and fair systems with the Rho-Pero new fair built in 2005. However, such services often remain under-diffused. For example, although Milan has the largest academic system after Rome and some of the most specialised universities in Italy, the impact on the regional economy has remained disappointing. Universities perceive very few incentives to collaborate, they generate modest spin-offs and they barely interact with SMEs even though the latter constitute the bulk of Milan's production framework. The lack of interaction between firms, service providers and training agencies calls for the creation of brokering institutions between suppliers and users of knowledge, not only to help match complementary actors but also to induct mechanisms to trigger knowledge spillovers. Further, mechanisms to ensure permanent connections among these brokering institutions and constant upgrades of available services could help Milan progress into a strategic pole.
- Measures to build a market for **breakthrough innovation** could pave the way for future sources of growth. Breakthrough innovation, which is mostly generated in public and private research centres as well as in universities, needs to be diffused with public support in order to fuel the regional economy and to address a market failure. On the one hand, some firms are unable to express solvable demand for innovation because they are often simply not aware of available innovation. On the other hand, research institutions and universities lack incentives to collaborate with small firms, either due to their prevailing interests in research activities rather than in the diffusion of technology, or due to the higher transaction costs in dealing with small (and often micro) firms. Therefore, innovation policy should not only support R&D investment but also the diffusion of innovation throughout the economy and closer linkages between firms, research institutions and universities. Existing structures, notably the Province's Polo di Via Soderini, the Chamber of Commerce's Palazzo dell'Innovazione, and the existing technological centres, offer promising potential as innovation brokers if they can be connected with each other through a comprehensive strategy. A decisive test for Milan's innovation system will come in high-tech activities such as biotechnology, which is supported by a well-developed local healthcare sector but must contend with powerful European competitors.
- Milan's advanced activities that enjoy the highest **international visibility** should remain a safe "brand" on the volatile global market. Some of the most salient examples of such activities are fashion (Milan accounted for more than half

of Italian turnover in 2003 and the Milano Collezioni fashion fair has enjoyed constant success) and design (Milan breeds top-class designers and architects). Regarding fashion, the gap between world-renowned brands and less eminent talents should be addressed carefully. Public policies could also reinforce the synergy effects across the fashion supply chain by further facilitating inspiring linkages between stylists and manufacturing SMEs. As for design, Milan has a historical advantage thanks to strong linkages between design and manufacturing firms, but this effect could run out and needs to be rebuilt. ■

How to maintain adequate public goods?

In the long run, Milan's innovation capacity could be further depleted as the metropolitan area could become less attractive to qualified human capital because of its relatively modest wage levels. Milan offers slightly higher wages than the Italian average, but the Italian average is below that of the EU15. Milan also has a higher cost of living than other major EU cities, such as Paris, Berlin and Madrid. Milan's prestigious universities already fail to attract foreign students compared with other European universities (the most attractive, Bocconi University, only counts about 4% of foreign students), which could presage further drags in the regional innovation dynamics.

Developing Milan into a high value-added, conception-oriented and knowledge-intensive service hub requires immediate action to restore the region's connectivity and liveability. Such factors constitute key sources of growth, both exogenous (by attracting knowledge workers) and endogenous (by enhancing internal exchanges of knowledge). Exploiting synergies and complementarities between the manufacturing area and the service-oriented core requires adequate services for mobility to facilitate interaction and thus the production and diffusion of innovation, as well as to meet demand from an extended market for services.

A close scrutiny of the erratic transport framework indicates that little can be solved without reforming governance mechanisms. Infrastructure has converged in the core of the city while suburban connections and suburb-to-suburb connections have remained limited or saturated. Blurred responsibilities across levels of government, financial limits and political divergence have aggravated the investment deadlocks. Experiments have been carried out on co-operative arrangements to introduce an integrated fare system, such as the Milan Area Integrated Fare System between the municipal Milan Transport Authority and a few other municipal authorities, but they have covered only part of the mobility needs in the region. Intergovernmental agreements that could have helped resolve the transport challenge via joint planning and financing of infrastructure have rarely materialised, although other policy issues have met promising bottom-up collaboration responses. For example, the province, four municipalities in the north of the province and various economic actors established a local development agency in charge of brownfield restoration, which was renamed Milano Metropoli in 2005 with an enlarged mandate.

Since the mid-1960s, Milan has reflected on possible governance arrangements aimed at keeping pace with and lending support to its economic expansion. The debate culminated in a proposal to convert the province into a *città metropolitana* ("metropolitan city"), under a 1990 law which offered regions the possibility to create a new subnational layer of government accumulating provincial and supramunicipal responsibilities. But this proposal was never put in place due to intergovernmental dissension and lack of incentives. An alternative option would be to create an autonomous transport authority, which could be coupled with or merged into a multi-purpose metropolitan co-ordinating body if one were later established. Considering that the Italian Constitution already recognises "metropolitan cities" as a subnational level, further progress could be achieved through a national policy for metropolitan areas. ■

Towards a Milan “metropolitan community”?

Overall, Milan needs to produce a new vision for its future. This vision should be able to catalyse the region’s key actors, for example through a branding strategy promoting Milan both internally and externally. Flagship projects are an essential factor in building such a strategy. Although the region nurtures a wide variety of highly-skilled creative experts, their mutual disconnection dribbles their talent away while other cities have understood how to renew themselves (like Turin with the 2006 Winter Olympic Games or Bilbao with the Guggenheim cultural project). Gathering the region’s existing brainpower into a “think tank” could help Milan design a facelift strategy and catalyst projects to build a creative and stimulating environment. The province’s ongoing “Strategic Project” called “Città di Città” has launched a call for innovative proposals and actions. Building on this momentum, Milan could perpetuate a brainstorming dynamics by establishing a top quality incubator of ideas bringing together its best professionals and thinkers. Inspiration could be drawn from other OECD cities such as Barcelona that revamped their area through ambitious modernisation projects.

Milan’s outstanding projects could hardly materialise without political backup. Milan’s proposed vision (an innovative and attractive service hub) and the practical tools to implement this vision (e.g., transportation and housing) both require intergovernmental collaboration mechanisms and adequate financial resources. Milan could exploit the new latitude and additional fiscal resources offered by the recent decentralisation reforms to support its competitiveness roadmap. Based on the educative process initiated by a co-operative experience over transport issues for example, the region could build a Milan “metropolitan community”. Its biggest merit would be to bring together isolated actors and incrementally instil a culture of trust while developing a sense of collective ownership and the desire to join forces in order to accomplish common aspirations. However, considering the institutional fragmentation and the particular struggle in reaching a consensus in the Milan area, the national government will need to play a proactive role by helping to enforce appropriate mechanisms and ensuring adequate financial resources for the governance of metropolitan areas.

Milan remains one of the top-ranked OECD metropolitan regions but could well run out of steam. In the face of emerging economies with a durable supply of low-cost labour and aggressive potential in light industries, investors and consumers will expect Milan to measure up to its historic image of industrial forerunner and creative vanguard. Failure to uphold the innovation process and to reverse the deterioration of its attractiveness could prove costly. With a strong impetus from the national government, co-operative governance arrangements could support deeper synergies and the region’s conversion into the powerful pulse of a circuit with regional and national spillovers. Milan’s assets could then be fully exploited to reinvigorate Italy’s economy in the international arena. The current constraint is that metropolitan governance reforms cannot afford to be further delayed. ■

For further information

For further information on the *OECD Territorial Review of Milan* and the series of OECD Territorial Reviews on metropolitan regions, please contact Soo-Jin Kim, e-mail: soo-jin.kim@oecd.org or Raffaele Trapasso, e-mail: raffaele.trapasso@oecd.org.



For further reading

OECD (2001), **OECD Territorial Reviews: Italy**, ISBN 92-64-19342-1, € 37, 180 p.
OECD (2005), **OECD Economic Surveys: Italy**, ISBN 92-64-01032-7, € 29, 196 p.
OECD (2005), **OECD Regions at a Glance**, ISBN 92-64-01863-8, € 40, 249 p.
OECD (2006), **Competitive Cities in a Global Economy**, ISBN 92-64-02709-2, € 47, 307 p.
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