# OECD Economic Surveys
# SWITZERLAND

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# OECD Economic Surveys: Switzerland 2022

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# Foreword

This Survey is published on the responsibility of the Economic and Development Review Committee of the OECD, which is charged with the examination of the economic situation of member countries.

The economic situation and policies of Switzerland were reviewed by the Committee on 28 September 2021. The draft report was then revised in the light of the discussions and given final approval as the agreed report of the whole Committee on 5 November 2021.

The Secretariat's draft report was prepared for the Committee by Urban Sila, Véronique Salins, with contributions from Alexander Hijzen and Andrea Salvatori and under the supervision of Mame Fatou Diagne. Statistical research assistance was provided by Corinne Chanteloup and editorial assistance by Emily Derry.

The previous Survey of Switzerland was issued in November 2019.

Information about the latest as well as previous Surveys and more information about how Surveys are prepared is available at http://www.oecd.org/eco/surveys.

# Table of contents

Foreword 3

Executive Summary 9

1 Key Policy Insights 14
- Introduction 15
- Policy support should target hardest-hit firms and vulnerable groups 19
  - The COVID-19 pandemic continues to raise uncertainty 19
  - Unprecedented policy support helped sustain incomes and employment through the pandemic 20
  - The economic recovery will continue, but the protracted pandemic increases uncertainty 22
  - Monetary policy remains accommodative 24
  - Fiscal policy should avoid premature tightening 27
  - Supporting hardest-hit firms and facilitating job reallocation 31
- Boosting competition to raise productivity and growth 33
  - Improving regulatory settings 36
  - Maintaining international openness to harness competitive pressures 39
- Ensuring effective use of resources to raise living standards of all and make growth more sustainable 41
  - Environmental performance is good but consumption patterns and resource use still result in environmental pressures 41
  - Boosting green investment and eco-innovation 44
  - Addressing challenges from population ageing 45
  - Making the tax mix more growth friendly 49
  - Fighting corruption and money laundering 52
- References 58

2 Fostering a strong labour market to support the recovery and sustain growth 65
- Introduction 66
- High resilience and substantial government support shielded the labour market during the crisis 67
  - Adequate policies effectively supported the labour market during the crisis 67
  - The impact of the crisis varied considerably across groups of workers and sectors 70
  - The legacy of the crisis could weigh on the labour market 75
- Exiting the crisis and facilitating job reallocation 79
  - Balancing adequate support and incentives for workers' reallocation 79
  - Seizing the opportunity to reconsider the social protection of the self-employed 84
  - Boosting active labour market policies 86
  - Fostering geographical mobility 88
- Making the labour market more inclusive 88
  - Addressing the gender income gap 88
  - Supporting the employment of older workers 92

Raising skills and lowering inequities in education 93
References 101

## Tables

Table 1. The economy has recovered to pre-crisis levels 10
Table 1.1. Macroeconomic indicators and projections 23
Table 1.2. Low-probability events that could lead to major changes in the outlook 24
Table 1.3. The fiscal position is strong 30
Table 1.4. Potential impact of structural reforms on per capita GDP 31
Table 1.5. Illustrative direct fiscal impact of selected recommended reforms 31
Table 1.6. Past recommendations on lowering barriers to competition 41
Table 1.7. Past recommendations on ensuring sustainable and inclusive growth 55

## Figures

Figure 1. The Swiss economy has been relatively resilient 10
Figure 2. The fiscal position remains strong despite the fiscal expansion during the crisis 11
Figure 3. Productivity growth has slowed 11
Figure 4. Environmental pressures remain despite decoupling of domestic emissions and material use from growth 12
Figure 1.1. Risks and challenges from the ongoing pandemic persist 15
Figure 1.2. The Swiss economy has shown its resilience in the face of a global crisis 16
Figure 1.3. The overall resilience masks high heterogeneity across sectors and groups 16
Figure 1.4. The Swiss enjoy a high standard of living and relatively low income inequality 17
Figure 1.5. The crisis has hit low-income households harder 17
Figure.1.6. Productivity growth has slowed 18
Figure 1.7. The COVID-19 pandemic has yet to be overcome 20
Figure 1.8. Economic developments 22
Figure 1.9. Monetary policy remains accommodative 26
Figure 1.10. The build-up of imbalances in the residential real estate market has continued 27
Figure 1.11. Emergency fiscal measures pushed public balance into a deficit 28
Figure 1.12. The crisis had differing impacts across sectors 32
Figure 1.13. Switzerland is a top performer in terms of labour productivity and GDP per capita 34
Figure 1.14. Productivity is very high in a number of sectors 34
Figure 1.15. The globally competitive and high value-added economy is sustained by a highly skilled workforce 35
Figure 1.16. With ageing, productivity growth will be key to sustain living standards 35
Figure 1.17. Productivity growth has slowed 36
Figure 1.18. There is room to improve regulatory settings 37
Figure 1.19. Barriers to trade in services are higher than in most other OECD countries 40
Figure 1.20. Switzerland has benefited from high inward FDI 40
Figure 1.21. Switzerland has decoupled economic growth from domestic greenhouse gas emissions and material use but environmental pressures remain 42
Figure 1.22. Population is ageing rapidly 46
Figure 1.23. Employment rates fall steeply after 65 46
Figure 1.24. Ageing creates fiscal pressures 47
Figure 1.25. The replacement rate from mandatory pension schemes is expected to fall 48
Figure 1.26. Switzerland relies heavily on direct taxation 49
Figure 1.27. The tax system contributes to high indebtedness of Swiss households, while reliance on taxing immovable property is low 50
Figure 1.28. Switzerland's VAT rate and revenues are among the lowest in the OECD 51
Figure 1.29. Switzerland performs well in control of corruption 53
Figure 1.30. Anti-money laundering measures are effective in most aspects 54
Figure 2.1. The labour market has shown resilience, helped by swift policy support 67
Figure 2.2. The number of job vacancies exceeded their pre-crisis level in the second quarter of 2021 68
Figure 2.3. The short-time working scheme significantly cushioned the impact of the pandemic on employment 69
Figure 2.4. The impact of containment measures differed across sectors 71

Figure 2.5. Skilled labour shortages temporarily eased during the pandemic 72
Figure 2.6. Short time work use differed across groups 72
Figure 2.7. Probability that an employee moves to non-employment or short-time work between consecutive quarters 74
Figure 2.8. The Swiss labour market performs well in international comparison 76
Figure 2.9. The sizeable gender wage gap and high incidence of part-time work weigh on women's labour incomes 77
Figure 2.10. Women and foreigners disproportionally work in the most affected sectors 78
Figure 2.11. Employment gaps are sizeable for some groups 79
Figure 2.12. Short-time work was massively used in the sectors most affected by restrictions 80
Figure 2.13. Several countries have recently (re)introduced or increased co-financing by firms in job retention schemes 82
Figure 2.14. Gross replacements rates in job retention schemes tend to be higher than in the unemployment benefit systems 83
Figure 2.15. Self-employment represents a sizable share of employment in Switzerland 84
Figure 2.16. Access to social protection is limited for self-employed workers 85
Figure 2.17. Enrolment in early childhood education and care is low 89
Figure 2.18. The disincentives for second-earners to move to full time employment are very large 90
Figure 2.19. Incidence of long-term unemployment increases with age 92
Figure 2.20. Performance in reading varies widely across socio-economic groups 93
Figure 2.21. The pandemic crisis led to widespread closure of schools 94
Figure 2.22. Participation in adult learning is high but should be broadened 96
Figure 2.23. Participation in life-long learning has declined during the pandemic, especially for older workers who tend to have lower digital skill 97
Figure 2.24. Swiss adults' digital skills are solid but lag the top performers 98
Figure 2.25. Immigrants have heterogeneous educational attainment 99

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## Basic statistics of Switzerland, 2020[1]

(Numbers in parentheses refer to the OECD average)[2]

| | | | | | |
|---|---|---|---|---|---|
| **LAND, PEOPLE AND ELECTORAL CYCLE** | | | | | |
| Population (million) | 8.6 | | Population density per km² | 218.6 | (38.6) |
| Under 15 (%) | 15.0 | (17.8) | Life expectancy at birth (years, 2019) | 83.7 | (80.2) |
| Over 65 (%) | 19.1 | (17.4) | Men (2019) | 81.9 | (77.6) |
| International migrant stock (% of population, 2019) | 29.9 | (13.2) | Women (2019) | 85.6 | (82.9) |
| Latest 5-year average growth (%) | 0.8 | (0.6) | Latest general election | October 2019 | |
| **ECONOMY** | | | | | |
| Gross domestic product (GDP) | | | Value added shares (%) | | |
| In current prices (billion USD) | 752.4 | | Agriculture, forestry and fishing | 0.7 | (2.8) |
| In current prices (billion CHF) | 705.9 | | Industry including construction | 25.3 | (26.3) |
| Latest 5-year average real growth (%) | 1.0 | (0.8) | Services | 74.0 | (71.0) |
| Per capita (000 USD PPP) | 71.7 | (46.4) | | | |
| **GENERAL GOVERNMENT** | | | | | |
| Per cent of GDP | | | | | |
| Expenditure | 37.8 | (49.8) | Gross financial debt (OECD: 2019) | 43.9 | (108.9) |
| Revenue | 35.0 | (38.8) | Net financial debt (OECD: 2019) | -17.2 | (68.0) |
| **EXTERNAL ACCOUNTS** | | | | | |
| Exchange rate (CHF per USD) | 0.94 | | Main exports (% of total merchandise exports) | | |
| PPP exchange rate (USA = 1) | 1.14 | | Chemicals and related products | 39.4 | |
| In per cent of GDP | | | Commodities and transactions | 22.4 | |
| Exports of goods and services | 62.3 | (50.6) | Miscellaneous manufactured articles | 16.4 | |
| Imports of goods and services | 53.6 | (47.1) | Main imports (% of total merchandise imports) | | |
| Current account balance | 1.2 | (0.0) | Commodities and transactions | 30.2 | |
| Net international investment position | 99.9 | | Chemicals and related products | 19.6 | |
| | | | Machinery and transport equipment | 18.0 | |
| **LABOUR MARKET, SKILLS AND INNOVATION** | | | | | |
| Employment rate (aged 15 and over, %) | 64.6 | (55.1) | Unemployment rate, Labour Force Survey (aged 15 and over, %) | 4.8 | (7.1) |
| Men | 70.0 | (63.0) | Youth (aged 15-24, %) | 8.6 | (15.1) |
| Women | 59.4 | (47.7) | Long-term unemployed (1 year and over, %) | 1.6 | (1.3) |
| Participation rate (aged 15 and over, %) | 67.9 | (59.5) | Tertiary educational attainment (aged 25-64, %) | 45.3 | (39.0) |
| Average hours worked per year | 1,495 | (1,687) | Gross domestic expenditure on R&D (% of GDP, 2017, OECD: 2018) | 3.4 | (2.6) |
| **ENVIRONMENT** | | | | | |
| Total primary energy supply per capita (toe) | 2.7 | (3.7) | CO2 emissions from fuel combustion per capita (tonnes, 2019) | 4.2 | (8.3) |
| Renewables (%) | 23.8 | (11.9) | Water abstractions per capita (1 000 m³, 2012) | 0.3 | |
| Exposure to air pollution (more than 10 µg/m³ of PM 2.5, % of population, 2019) | 48.5 | (61.7) | Municipal waste per capita (tonnes, 2019) | 0.7 | (0.5) |
| **SOCIETY** | | | | | |
| Income inequality (Gini coefficient, 2018, OECD: latest available) | 0.311 | (0.317) | Education outcomes (PISA score, 2018) | | |
| Relative poverty rate (%, 2018) | 10.5 | (11.7) | Reading | 484 | (485) |
| Median disposable household income (thousand USD PPP, 2018) | 38.5 | (25.4) | Mathematics | 515 | (487) |
| Public and private spending (% of GDP) | | | Science | 495 | (487) |
| Health care (2019) | 11.3 | (8.8) | Share of women in parliament (%) | 41.5 | (31.5) |
| Pensions (2018, OECD: 2017) | 12.2 | (8.6) | Net official development assistance (% of GNI, 2017) | 0.5 | (0.4) |
| Education (% of GNI, 2019) | 4.6 | (4.4) | | | |

1. The year is indicated in parenthesis if it deviates from the year in the main title of this table.
2. Where the OECD aggregate is not provided in the source database, a simple OECD average of latest available data is calculated where data exist for at least 80% of member countries.
Source: Calculations based on data extracted from databases of the following organisations: OECD, International Energy Agency, International Labour Organisation, International Monetary Fund, United Nations, World Bank.

# Executive Summary

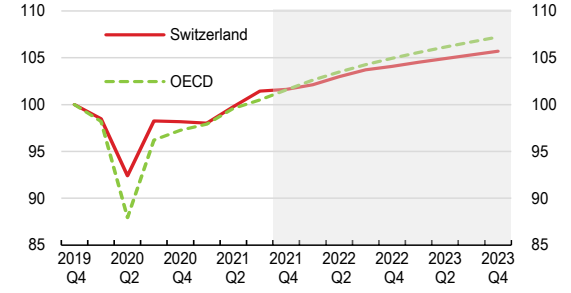
## The economy is set to recover but some sectors and groups were hard hit

**The COVID-19 pandemic continues to raise uncertainty and challenges.** Infections started rising steeply again at the end of 2021 and the emergence of a new variant has clouded prospects for a rapid exit from the pandemic. The vaccination campaign accelerated once again thanks to booster shots, but the share of vaccinated remains below many OECD peers. Major constraints on economic life were largely lifted in the course of 2021, boosting economic activity, but uncertainty remains high.

**The Swiss economy has been relatively resilient.** Globally competitive companies, a highly skilled workforce, and low reliance on hospitality and entertainment activities mitigated the adverse impact of pandemic containment measures. The authorities swiftly extended generous support to sustain incomes and liquidity, while high trust in the government and the highly effective health system enabled less strict lockdowns.

### Figure 1. The Swiss economy has been relatively resilient

Real GDP, index 2019 Q4 = 100




Source: OECD Economic Outlook database.

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**The economy recovered to pre-crisis levels in the first half of 2021.** GDP dropped by 2.5% in 2020 (calendar-adjusted) as activity in high-contact sectors was severely limited and private consumption restricted. Elevated uncertainty dampened investment. Yet, the rise in unemployment remained subdued thanks to government support, notably the expanded short-time work compensation scheme. The lifting of pandemic restrictions from spring 2021 triggered a quick rebound in activity, but global supply constraints and renewed pressures from the pandemic weighed on the recovery.

**The impact of the crisis differed significantly between different sectors, companies and workers.** Sectors less affected by distancing requirements and sectors that could adapt easily to the opportunities of increased digitalisation recovered quickly after the first wave. Other activities, more dependent on direct contacts, have faced heavy restrictions, some of them for almost a year. This has had a disproportionate impact on low-middle skilled and low-wage workers, given their high employment in these sectors. There is a risk that consumer preferences have changed and that demand for some goods and services remains depressed more permanently, requiring restructuring and employment transitions in the coming years.

### Table 1. The economy has recovered to pre-crisis levels

| Growth rates, unless specified | 2021 | 2022 | 2023 |
|---|---|---|---|
| Gross domestic product (GDP) | 3.5 | 3.0 | 1.8 |
| Unemployment rate (% of labour force) | 5.1 | 4.8 | 4.6 |
| Consumer price index | 0.6 | 1.1 | 0.8 |
| General government net lending (% of GDP) | -2.3 | 0.2 | 0.8 |

Source: Based on OECD Economic Outlook 110 database with updates to selected variables.

## Policy support should increasingly target only the hardest-hit firms and vulnerable groups

**Monetary policy has remained expansionary.** The policy interest rate stayed at -0.75% and the countercyclical capital buffer for mortgages was deactivated in early 2020 to support credit. In spring 2020, the SNB set up a refinancing facility to complement the government's guarantee programme for corporate loans (COVID-19 credits). The SNB has intervened regularly in the foreign exchange market to stave off safe-haven pressures on the Swiss franc and resulting deflationary pressures.

**Risks in the financial sector have risen.** Adequate capital and liquidity buffers in the Swiss financial system have contributed to stability. Yet, credit defaults and market corrections may materialise only with delay, once the extensive policy support at home and abroad is withdrawn. Stress tests point to overall resilience, but a number of individual institutions face a risk of capital being depleted in the event of an adverse shock. The build-up of imbalances continued in the residential real estate market,

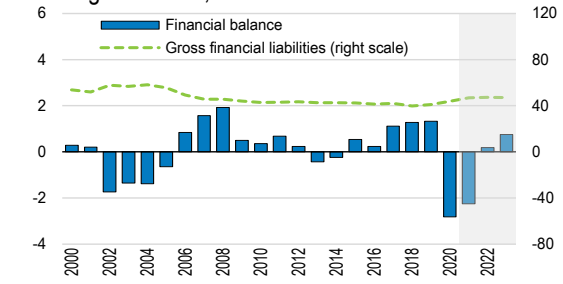
partly as a side effect of low interest rates, raising risks.

**The fiscal position remains strong.** Extensive emergency spending and a marked drop in fiscal revenues have pushed public finances into a deficit. The total cost of pandemic-related extraordinary fiscal expenditures is estimated at roughly 2.4% of GDP in 2020 and again in 2021. The fiscal position nevertheless remains very strong: gross general government debt stood at 44% of GDP in 2020 and net debt is negative. Interest rates on issuing new debt remain at very low levels.

**Fiscal policy should remain supportive until the recovery is well under way.** The strong fiscal position with low public debt has been achieved within the framework of the federal debt brake rule and cantonal fiscal rules. Nevertheless, the existing federal framework risks tightening fiscal policy too soon as it requires extraordinary COVID-19 expenditures to be compensated over a relatively short period. Premature fiscal tightening could undermine the recovery and should be avoided.

### Figure 2. The fiscal position remains strong despite the fiscal expansion during the crisis

General government, % of GDP




Source: OECD Economic Outlook database.

StatLink https://stat.link/hs132m

**For the most affected firms and vulnerable people, targeted government support will continue to be needed.** Debt financing and credit guarantees have helped to ease immediate financial constraints. Many companies may however face deteriorating balance sheets due to low profitability and rising debt. Likewise, workers in certain sectors risk unemployment in great numbers in case of premature withdrawal of support.

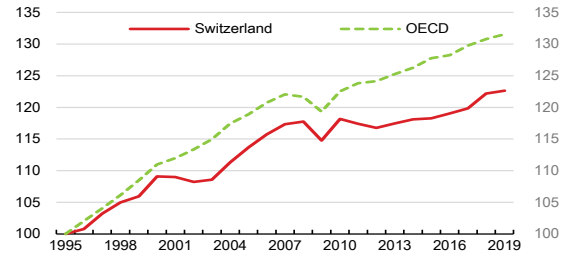
**A key challenge is to provide sufficient support for viable firms while helping displaced workers find new jobs.** Scaling back the short-time work scheme and asking firms to increasingly bear part of the cost of the scheme can be an effective way to support viable companies in need, while avoiding delaying layoffs in non-viable companies. More effective active labour market policies can help displaced workers find new jobs or gain new skills. A broader use of financial incentives for the unemployed to take up jobs would notably benefit the young, low-skilled workers and foreigners. Also, lower disincentives to hire older workers would help raise employment.

## Boosting competition to raise productivity and growth

**Fostering productivity growth is crucial to maintain high living standards in the future.** Switzerland is one of the top OECD performers in terms of labour productivity, but productivity growth has slowed markedly over the last three decades. Productivity improvements are needed to counter the impact of an ageing population on GDP per capita growth.

### Figure 3. Productivity growth has slowed

Labour productivity (real GDP per person employed), 1995 = 100




Source: OECD Productivity database.

StatLink https://stat.link/p7hev4

**Barriers to free and open competition within the internal market remain**. Competition in the domestic market is still hampered across cantonal borders. The administrative burden on start-ups is higher than in top performers and resolving commercial disputes takes a long time. The merger control framework remains too permissive and civil action against cartels is rare due to high complexity and short prescriptive periods. State involvement in the economy, notably in the network sectors, and the advantageous position of numerous state-owned enterprises reduce competition.

**Lower barriers to trade and continued access to global markets are needed.** Some sectors remain shielded from international competition, notably agriculture and some services sectors, harming productivity. Switzerland also imposes

some constraints on inward foreign direct investments mainly through equity restrictions. The partnership between Switzerland and the EU is also at risk of eroding over time, in case various bilateral agreements become outdated. Ensuring a continued stable framework for the economic relationship with the EU would secure access and competitive exposure to the most important trading partner, raising productivity and growth.

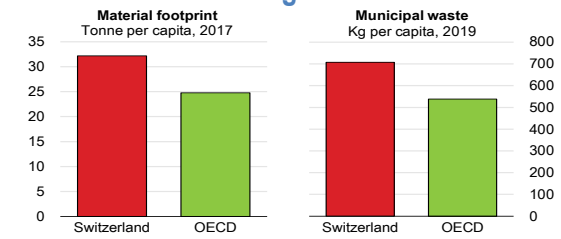
## Ensuring the effective use of resources to raise sustainability and inclusion

**Switzerland has successfully decoupled economic growth from domestic greenhouse gas emissions and material use, but environmental pressures remain.** A high standard of living together with a relative lack of domestic raw materials and energy resources necessitate high imports. As a result, the material footprint per capita is significant and a large share of the associated environmental damage occurs abroad. Municipal waste per capita is among the highest in the OECD and municipal waste generation has not been decoupled from consumption, despite a number of policy instruments.

**Switzerland has set a net-zero greenhouse gas emissions target by 2050, but sufficient measures to achieve it remain to be adopted.** Switzerland prices its $CO_2$ emissions at high rates, but various exemptions to the carbon tax reduce its effectiveness. In addition, plans to further raise the carbon tax and introduce an air-ticket levy have recently been halted. Environmentally harmful subsidies and tax exemptions in agriculture, forestry and public transportation give rise to a pricing and incentive system that distorts the link between market signals and costs of environmental damage across sectors.

**There is room to better align investment portfolios with climate goals and foster eco-innovation**. The Swiss financial sector has a global outreach, but is still heavily invested in oil and coal extraction, despite significant progress in recent years. Higher transparency on the climate compatibility of investment portfolios and exposures to climate-related risks can help in adoption of effective climate-related initiatives. Switzerland is a global leader in innovation activity, but it could further leverage its position to boost environment-related R&D and eco-innovation.

### Figure 4. Environmental pressures remain despite decoupling of domestic emissions and material use from growth




Source: OECD Environment Statistics (database).

StatLink https://stat.link/invs5u

**A substantial pension reform is overdue**. The statutory retirement age has remained at 65 years for men since its introduction in 1948. Ageing creates fiscal pressures, by lowering revenues and putting pressures on age-related costs (pension, health-care and long-term care), and weighs on employment and growth. On current policies, the ratio of retirees to employees is set to soar and pension replacement rates for the mandatory pension system are set to drop significantly over time. Yet, reforms have proven very difficult.

**A range of disincentives and barriers contribute to early retirement and low uptake of work by older workers.** After the age 65, the otherwise high employment rate shows a steeper decline than in OECD peers. Once unemployed, older workers can have difficulties in finding a job. Narrow specialisation, lack of job-search experience and rising wage costs with age, including due to rising pension contribution rates, play a role. Pension reform and targeted policies to support older workers in their job search and retraining could help bring more of them to work.

**The gender pay gap is sizable.** The interplay between the tax and benefit systems and high costs of childcare result in disincentives to work for second earners, notably mothers. Low supply of affordable and high-quality childcare exacerbates the issue, contributing to a high take up of part-time work and markedly lower working hours. Increasing the supply of childcare and lowering work disincentives for second earners would help raise labour incomes for women and promote equity. Better access to early childhood education could help children from disadvantaged backgrounds to succeed later in life.

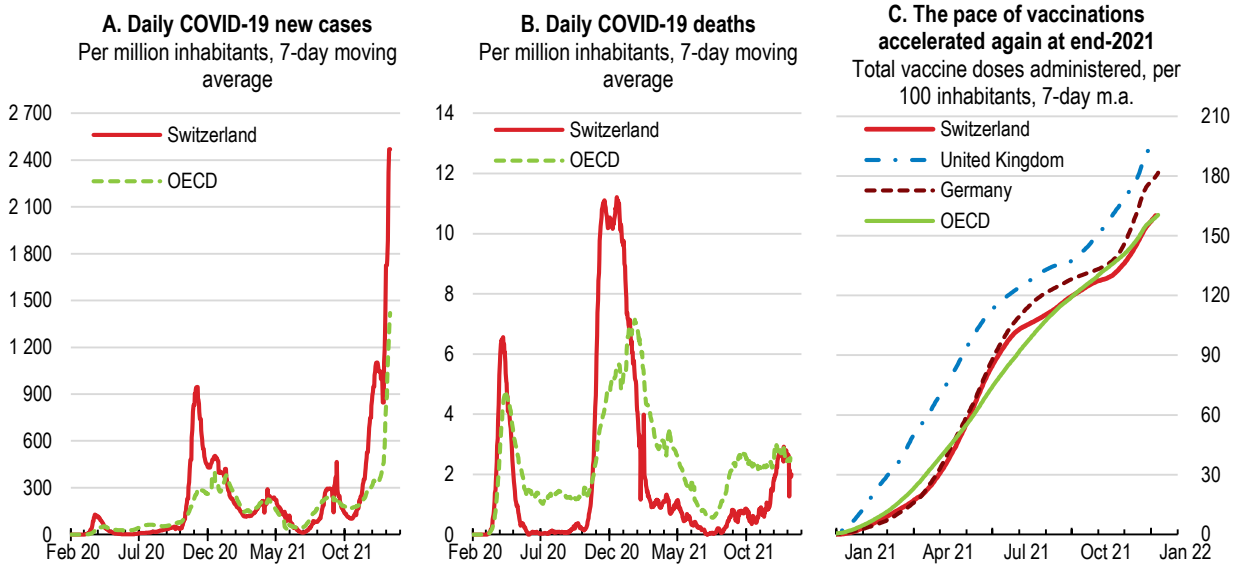
| MAIN FINDINGS | RECOMMENDATIONS |
|---|---|
| **Supporting the economy to exit the crisis** | |
| Inflation is projected to remain moderate as the economy recovers, with substantial risks and uncertainty. | Monetary policy should remain accommodative until the recovery is firmly underway. |
| The Swiss financial system enjoys adequate capital and liquidity buffers. However, credit defaults and market corrections may materialise with delay. | Consider reactivating the countercyclical capital buffer targeted at residential mortgages.<br>Progress further on managing the risks from "too-big-to-fail" banks, notably with strengthened liquidity requirements and resolution and emergency plans. |
| The deficit increased but gross general government debt remains low and net debt is negative (positive net assets). Interest rates on issuing new debt remain at historically low levels. | Use the flexibility within the fiscal framework (the debt brake rule) to apply temporary adjustments and avoid a too rapid tightening in fiscal policy. |
| The crisis had differing impacts across sectors. A premature withdrawal of support could trigger unnecessary bankruptcies and labour shedding and may result in scarring and poverty. A key challenge is to provide sufficient support for hard-hit firms and workers, while facilitating resource reallocation. | Continue to narrow policy support to hardest-hit sectors and vulnerable groups. |
| The extensions to the short-time working compensation scheme during the pandemic have adequately protected workers and firms but risk hindering job reallocation and restructuring during the recovery. | Once most pandemic restrictions are lifted, scale back the short-time working compensation scheme and reintroduce firms' financial participation to the cost of the scheme. |
| **Boosting competition to raise productivity and growth** | |
| Competition in the domestic market is still hampered by cantonal borders. The merger control framework remains too permissive and civil action against cartels is rare due to high complexity and short prescriptive periods. | Fully implement the Internal Market Act to ensure equal access to markets in all cantons.<br>Harmonise the merger control framework with that of the EU and strengthen the civil law on cartels. |
| The administrative burden on start-ups is higher than in top performers, and resolving commercial disputes takes longer and is costlier than on average in the OECD. | Reduce the administrative burden on start-ups. Introduce "Silence is consent" licensing rules.<br>Expand the government one-stop shop (EasyGov.swiss) by integrating cantonal governments' services. |
| Barriers to trade in services are higher than in most other OECD countries. Switzerland also imposes constraints on inward foreign direct investments (FDI) mainly through equity restrictions. Agriculture is heavily shielded from foreign competition and it receives high direct support payments. | Lower restrictions on trade in both goods and services, notably in agriculture. Remove the barriers to FDI where applicable and keep them low. |
| **Ensuring effective use of resources to raise sustainability** | |
| Municipal waste per capita is above the OECD average and has not decreased for the last 15 years, despite a number of policy instruments aimed at reduction. | Prepare a federal waste prevention strategy including indicative targets for municipal waste reduction. |
| The measures and targets of the proposed revised CO2 Act would have set important milestones on the way to reaching the net-zero greenhouse emissions target by 2050. However, plans to further raise the carbon tax and introduce an air-ticket levy have recently been halted (with the rejection of revised CO2 Act by a popular vote). | Continue efforts to broaden the base of the carbon tax by reassessing exemptions and align pricing of CO2 emissions with international climate cost benchmarks. |
| Switzerland could better leverage its internationally competitive financial and corporate sectors, and high saving rate to boost green investment and foster eco-innovation. The financial sector is still heavily invested in oil and coal extraction, and much less in renewable energy or electro-mobility. | Continue increasing transparency in relation to climate compatibility of financial portfolios. Strengthen the disclosure of climate-related risks for large companies and the financial sector. |
| **Raising labour market participation and inclusion** | |
| Population is ageing rapidly. First pillar funding faces serious pressures and pension replacement rates from the mandatory pension system are set to drop significantly. | Fix the retirement age at 65 for both genders and link it to life expectancy. |
| The gender income gap is high in Switzerland, in part due to high incidence of part-time employment. The interplay between the tax and benefit systems and a high cost of childcare result in lower working hours and lower labour incomes for women. | Keep expanding the supply of childcare and provide targeted measures (means-tested fee reductions, childcare benefits or tax credits) to improve affordability.<br>Reduce disincentives to work for second earners, by moving from family-based to individual-based taxation or through tax adjustments and slower withdrawal of benefits. |
| Students from a disadvantaged background are significantly more likely to underperform and less likely to graduate with a tertiary degree. | Improve access to early childhood education and care for low-income households. |

# 1 Key Policy Insights

## Introduction

Switzerland continues to face uncertainty and challenges from the ongoing pandemic (Figure 1.1). The steep rise in infections and the emergence of a new variant at the end of 2021 clouded prospects for a rapid exit from the pandemic. Meanwhile, the economy has been on the path to recovery. Containment measures and restrictions on social and economic life were largely lifted during 2021, boosting economic activity. After a 2.5% drop in GDP in 2020 (calendar-adjusted), growth has resumed in 2021 and GDP reached its pre-pandemic level already in the second quarter of 2021.

### Figure 1.1. Risks and challenges from the ongoing pandemic persist




Source: OECD calculations based on Our World in Data.

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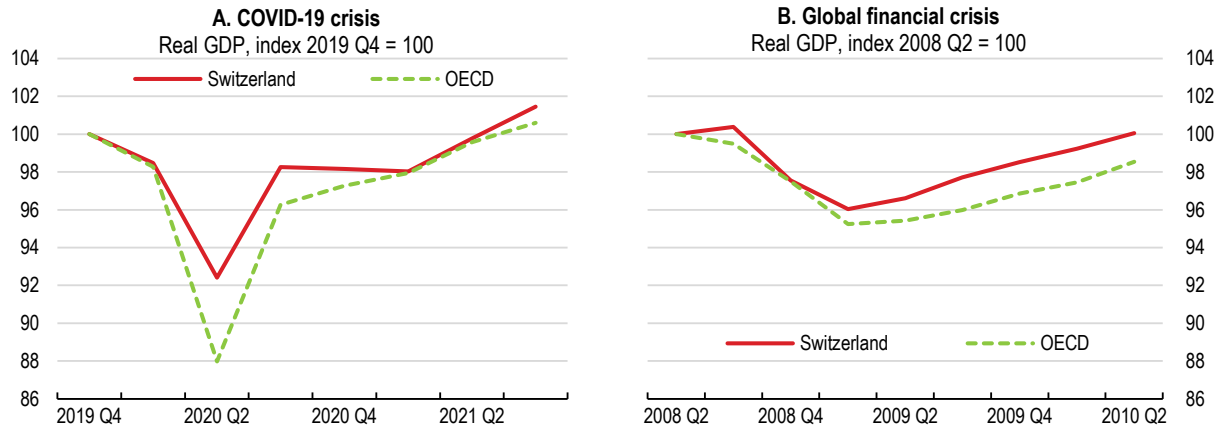
The Swiss economy has again shown its resilience in the face of a global crisis (Figure 1.2), despite its integral position in global value chains and dependence on foreign demand. The stable macroeconomic environment, high skills-based economy with globally competitive industries and companies, and well-functioning product and labour markets are all factors contributing to this resilience. In addition, national lock-downs and containment measures were less strict than in other OECD economies. A quick and targeted policy reaction to sustain jobs and incomes, and support companies and liquidity, also hindered the rise in unemployment and prevented numerous firm bankruptcies.

## Figure 1.2. The Swiss economy has shown its resilience in the face of a global crisis




Source: OECD Economic Outlook database.

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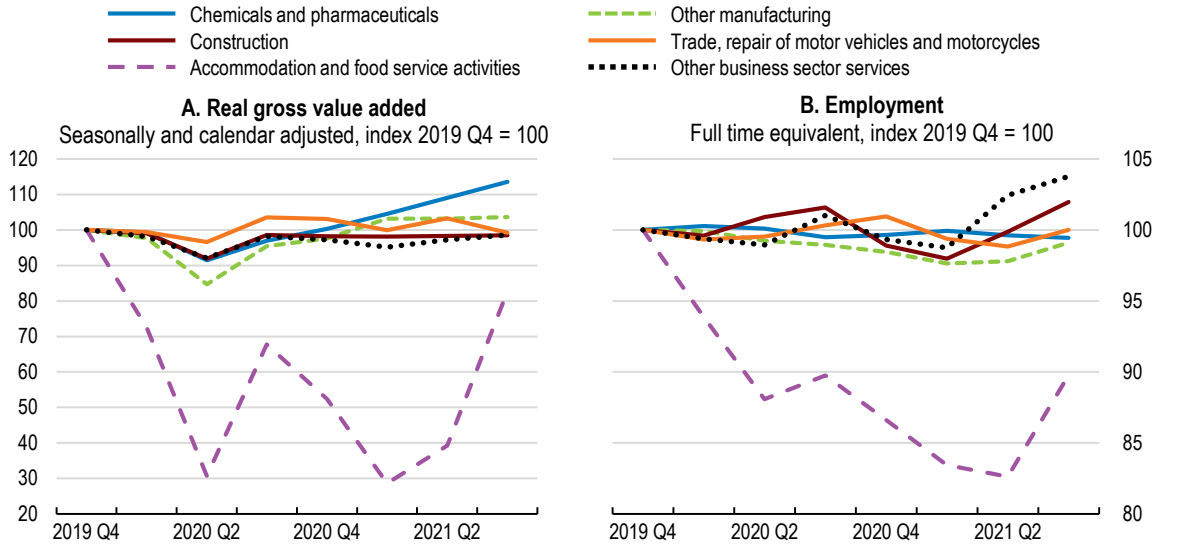
Nevertheless, the overall strength of the economy masks heterogeneity across sectors and groups (Figure 1.3). Sectors less affected by distancing requirements, such as manufacturing, or services that could adapt easily to the opportunities of increased digitalisation, recovered quickly after the first wave. Other services, more dependent on direct contact between consumers and producers faced heavy restrictions for almost a year. This has had a disproportionate impact on low-income and low-skilled workers, the self-employed and foreign workers, given the relative importance of these sectors for their employment.

## Figure 1.3. The overall resilience masks high heterogeneity across sectors and groups




Source: State Secretariat for Economic Affairs (SECO); Federal Statistical Office (FSO).

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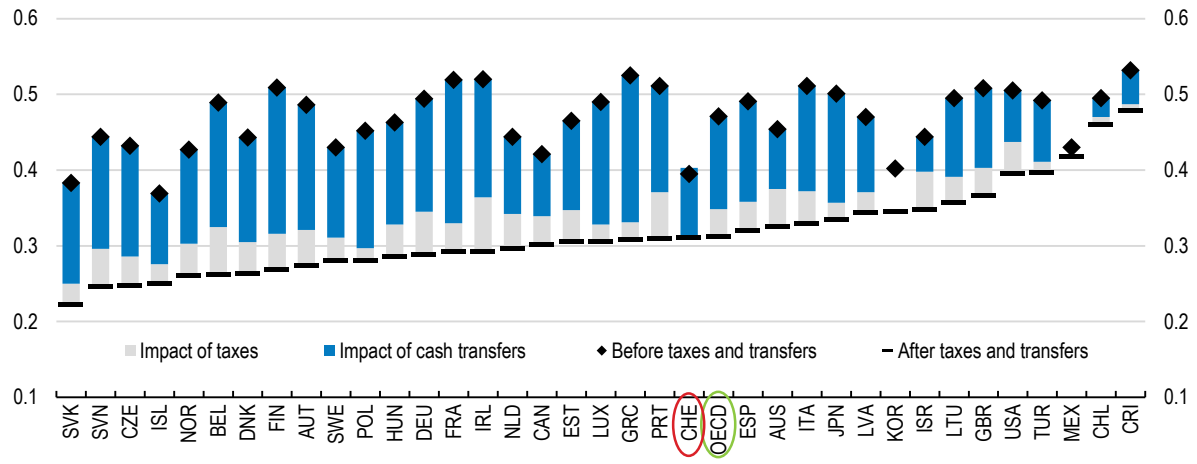
For some firms in the most affected sectors, the recovery may be difficult. Moreover, there is a chance that consumer preferences have changed and demand for some goods and services will remain depressed more permanently. With the removal of government support, the number of firm bankruptcies, which have stayed very low, is likely to rise. The challenge now is to allow labour and capital reallocation to strengthen growth, while targeting support to viable jobs and companies. Equally challenging and important is helping vulnerable workers and groups, to prevent poverty and deprivation.

The crisis has hit low-income households harder. Overall, high employment rates and a compressed wage distribution underpin a high standard of living and relatively low income inequality (Figure 1.4). Yet, evidence shows that during the crisis, households in the higher income brackets lost a lower share of their income and their situation improved more rapidly during economic recovery (Figure 1.5). While all households reduced spending, they did it for different reasons. Poorer households spent less due to income loss and uncertain prospects. Richer households, on the other hand, cited lower opportunities to spend as the main reason for lower spending. Moreover, savings of poor households fell significantly while they rose in richer households, adversely impacting wealth inequality (Martinez et al, 2021; SRG/Sotomo, 2021). This said, government support was well-targeted and poorer households received stronger support in relative terms.

## Figure 1.4. The Swiss enjoy a high standard of living and relatively low income inequality

Household income distribution, Gini coefficient[1], 2019 or latest available year




1. Scale from 0 "perfect equality" to 1 "perfect inequality".
Source: OECD Income Distribution database (IDD).

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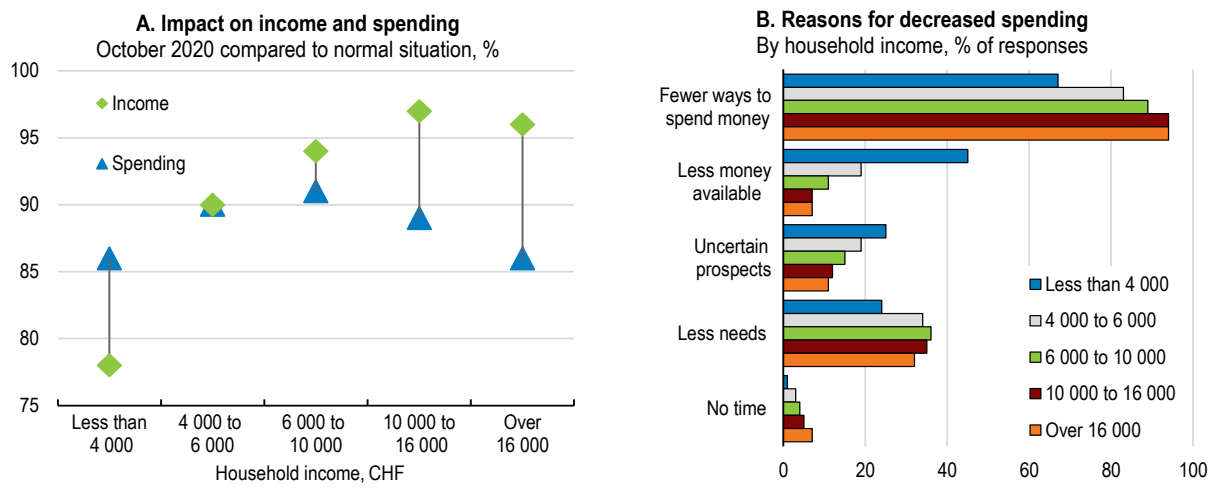
## Figure 1.5. The crisis has hit low-income households harder




Source: SRG/Sotomo, 2021, https://sotomo.ch/site/wp-content/uploads/2021/03/7.-SRG-Corona-Monitor.pdf

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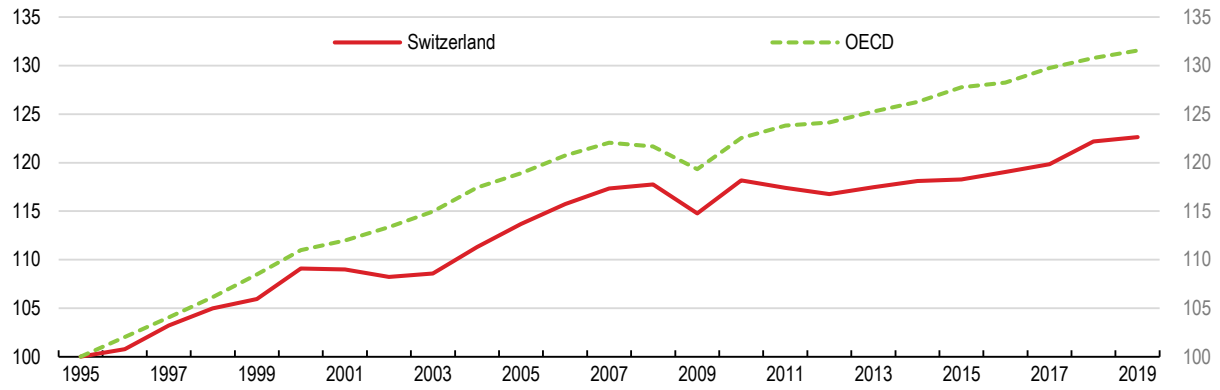
A revival in productivity growth is crucial to maintain high living standards in the future. Employment rates face pressures from rapid population ageing, weighing on future economic growth. Switzerland is one of

the top OECD performers in terms of labour productivity, but productivity growth has been low over the last three decades (Figure 1.6). There still exist barriers to competition within the internal market, including due to the advantageous position of numerous state-owned enterprises. Also, some sectors remain shielded from international competition, notably agriculture and some services sectors, harming productivity. Lower barriers to trade and competition and an improved business environment can spur competition and foster investments that will help revive productivity.

### Figure.1.6. Productivity growth has slowed

Labour productivity (real GDP per person employed), 1995 = 100




Source: OECD Productivity database.

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Effective and sustainable use of resources can sustain a stronger and more inclusive growth. Switzerland has successfully decoupled economic growth from domestic greenhouse gas emissions and material use. Yet, environmental pressures remain, notably due to high levels of consumption and resulting high levels of emissions and resource use embodied in imports. The pension system has not been sufficiently reformed in decades, and older workers should be better equipped to work longer. Taxes and benefits provide low work incentives for second-earners and together with the high cost of childcare, contribute to a high gender gap in working hours and labour incomes. Targeting skills provision – including of digital skills – to older workers and low-income workers would aid the post-crisis recovery and help better prepare the Swiss economy to the challenges of technological change.

Against this background, the main messages of this Survey are:

- Fiscal and monetary policy should continue to support the economy until the recovery is well under way. Yet, support should increasingly focus on people, rather than jobs, by facilitating job search, upskilling and preventing poverty. It should also be channelled towards hardest-hit but viable firms and aim to alleviate debt overhang. Enhancing insolvency procedures would facilitate capital reallocation.
- A more dynamic economy with fewer barriers to firm exit and entry and a lower administrative burden on start-ups can spur competition and productivity growth. Stability in international agreements and openness to trade and investment will sustain access to export markets and exposure to valuable competitive pressures.
- High labour market participation by all groups and environment-friendly policies will make growth more inclusive and sustainable. A reformed pension system and higher incentives to work for mothers and older workers will help in this regard. Better targeting of skills training to low-income workers will allow them to benefit from the digital transformation. Policies to improve the environmental sustainability of consumption and investment as well as consistent pricing of environmental externalities will also boost well-being in the long-term.

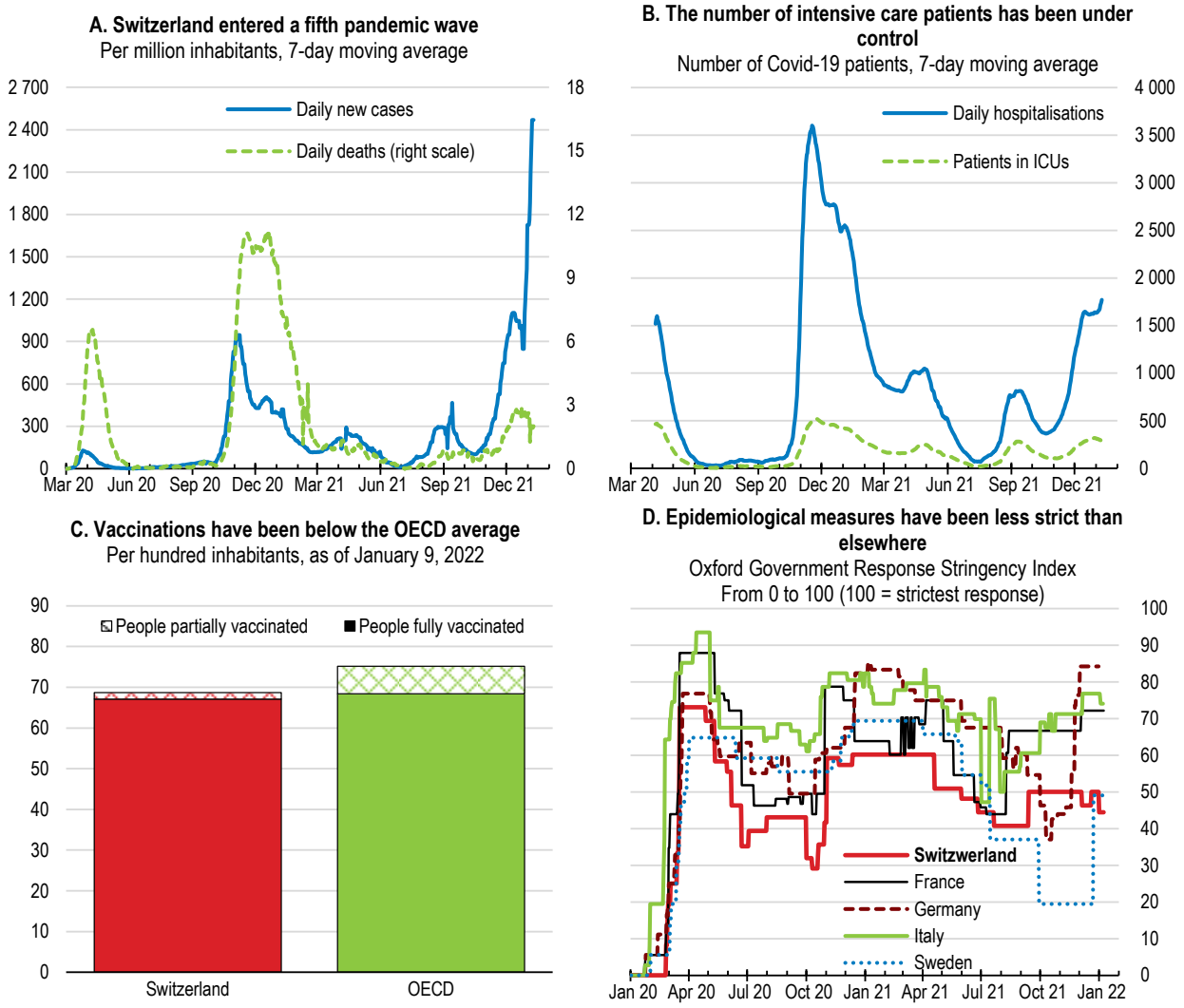
## Policy support should target hardest-hit firms and vulnerable groups

### *The COVID-19 pandemic continues to raise uncertainty*

The virus started to spread in February 2020 and the government quickly introduced strict epidemiological measures. Containment measures have been in place ever since, but to varying degrees of strictness, depending on the intensity of subsequent infection waves (Figure 1.7). In March 2021, in the wake of the second wave, the government gradually started lifting the most restrictive containment measures, once the vaccination campaign gathered pace and the number of infections and hospitalisations fell significantly. Yet, in November 2021, Switzerland entered a fifth pandemic wave, with a steep rise in infections and hospitalisations and an increased uncertainty from a new Omicron virus variant. The latter prompted the authorities to reintroduce targeted temporary travel bans and further tighten health barrier measures, such as broadening the use of the sanitary pass. The risk of stricter measures impacting economic activity also rose considerably. The pace of vaccinations, which slowed markedly over the summer, accelerated towards the end of 2021 thanks to booster shots, but the share of vaccinated persons remains below many OECD peers.

The main epidemiological objective in Switzerland has been to avoid lack of capacity in the health system. The number of patients in intensive care has remained under control throughout the pandemic (Figure 1.7). Supported by high trust in the domestic health system, the Swiss authorities chose to implement epidemiological measures that were less stringent than in many other OECD peers (Figure 1.7), avoiding prolonged full lock-downs. This contributed to the less severe economic downturn. A policy priority now should be to ensure that all resources necessary are used to fully deploy vaccinations – including booster shots - as quickly as possible to protect lives and limit the need for economically harmful containment measures.

## Figure 1.7. The COVID-19 pandemic has yet to be overcome




Source: OECD calculations based on Our World in Data; Federal Office of Public Health; Oxford COVID-19 Government Response Tracker, Blavatnik School of Government, University of Oxford.

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### *Unprecedented policy support helped sustain incomes and employment through the pandemic*

As the first wave of the pandemic hit, strict containment measures led to severe restrictions on activity in various sectors, notably services relying on close contact (hospitality and entertainment). Private consumption collapsed while high uncertainty dampened private investment.

The federal government rapidly extended generous policy support to sustain incomes and employment. It vastly expanded the short-time work compensation (STWC) scheme, offered income support to the self-employed and parents who stayed at home to look after children, and made unemployment insurance more generous. Cantons also quickly started offering financial support to affected sectors and firms. Monetary policy remained accommodative and the government issued guarantees for commercial loans to companies to sustain access to liquidity. As the second pandemic wave undermined the recovery from the third quarter of 2020, the authorities prolonged most of the emergency support measures into 2021 and introduced new grants, loans and guarantees. These included the “hardship” support for companies that had a 40% drop in sales due to the containment measures, and targeted support measures for firms

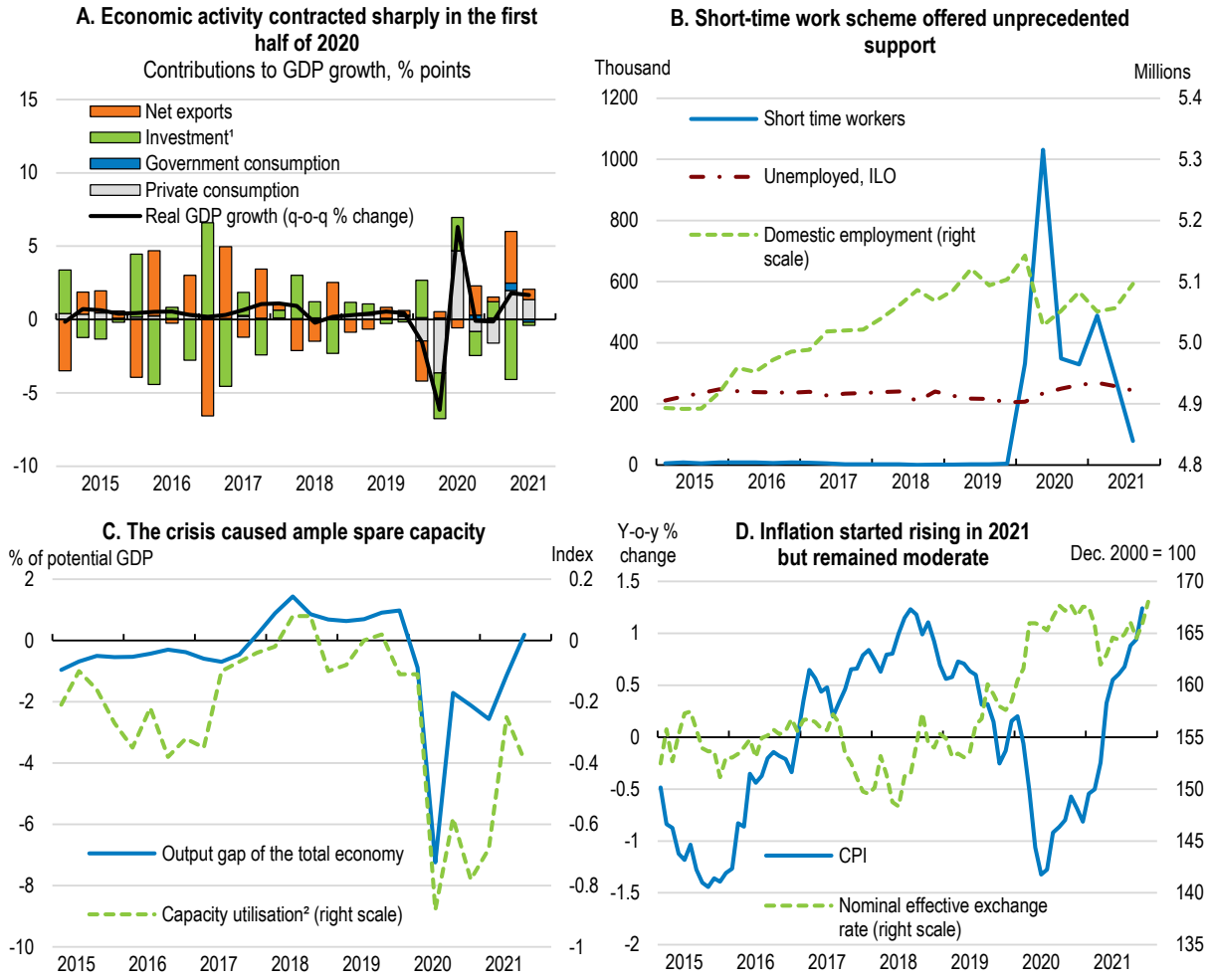
in sports, culture, tourism and transport. In December 2021, the legal basis of most extraordinary measures was extended until end-2022.

Overall, in 2020, Swiss GDP fell by 2.5% (in real terms, calendar-adjusted), one of the smallest contractions in the OECD. Less strict lock-downs and lower reliance on the hospitality sector in the economy played a role. The extensive fiscal and monetary support helped keep the business sector afloat and contributed to the strong rebound in economic activity in the third quarter of 2020, following a partial lifting of pandemic restrictions. Similarly, in the second and third quarters of 2021, after pandemic restrictions from subsequent waves were largely lifted, the economy recorded a broad-based recovery. Notably, parts of the services sector - hospitality and entertainment - that faced particularly severe restrictions for a prolonged period, recorded large increases. Private consumption also saw a large upturn. In contrast, in Q3 2021, global supply chain disruptions started to have an adverse impact on segments of the manufacturing sector and private investment.

The labour market has been recovering. During the crisis, the unemployment rate rose to 5.2% in 2020 Q4, up by roughly one percentage point from 2019 Q4. Thanks to public support measures, this rise was much lower than suggested by the extensive spare capacity in the economy (Figure 1.8) (see Chapter 2 of this Survey). The number of registered unemployed and the number of workers on short-time work schemes have steadily declined since early 2021.

Inflation remained negative during 2020 on the back of safe-haven pressures on the Swiss franc and low core inflation. In early 2021, headline inflation edged up due to rising commodity prices and currency depreciation. Headline inflation turned positive in April 2021, for the first time in more than a year.

## Figure 1.8. Economic developments




1. Including stock building.
2. Current utilisation of technical capacity / business infrastructure compared to a normal level. A positive (negative) index value signals utilisation is higher (lower) than normal.
Source: OECD Economic Outlook databases; SECO; KOF Swiss Economic Institute; OFS; SNB.

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### *The economic recovery will continue, but the protracted pandemic increases uncertainty*

The gradual lifting of pandemic restrictions along with the rollout of vaccines has triggered a rebound in activity, starting in the second quarter of 2021. The global supply chain disruptions and the fifth pandemic wave will slow the recovery at the end of 2021 and in early 2022, but no new major containment measures are assumed. Thereafter, improving prospects and the low cost of capital will underpin a recovery in investment. Recovering external demand should foster exports. Improvements in labour market conditions and consumer confidence, and the normalisation of households' high savings will support consumption. However, further decline in unemployment is projected to be gradual, reflecting the eventual removal of policy support and an expected pick-up in bankruptcies. Inflation will remain moderate. In particular, temporary pressures on annual inflation from high prices of energy and materials are assumed to subside in the course of 2022. The Swiss real GDP has caught up with the pre-crisis levels in Q2 2021, but will remain markedly below what was forecast in late 2019.

## Table 1.1. Macroeconomic indicators and projections

Annual percentage change, volume (2015 prices)

| | 2018 | 2019 | 2020 | Projections | | |
|---|---|---|---|---|---|---|
| | Current prices (billion CHF) | | | 2021 | 2022 | 2023 |
| **Gross domestic product (GDP)** | 719.8 | 1.2 | -2.5 | 3.5 | 3.0 | 1.8 |
| Private consumption | 372.2 | 1.4 | -3.7 | 2.4 | 3.8 | 2.1 |
| Government consumption | 79.9 | 0.7 | 3.5 | 6.0 | 0.4 | -2.2 |
| Gross fixed capital formation | 184.0 | 0.6 | -1.7 | 2.9 | 3.0 | 1.9 |
| Housing | 22.7 | -3.9 | -6.5 | 0.0 | -0.6 | 0.5 |
| Business | 139.9 | 0.7 | -2.0 | 3.2 | 3.9 | 2.3 |
| Government | 21.4 | 4.3 | 4.7 | 3.7 | 0.7 | 0.9 |
| Final domestic demand | 636.1 | 1.1 | -2.3 | 3.0 | 3.1 | 1.5 |
| Stockbuilding[1] | -6.0 | 0.7 | 1.3 | -3.7 | -0.9 | 0.0 |
| Total domestic demand | 630.1 | 1.9 | -0.8 | -1.1 | 2.1 | 1.5 |
| Exports of goods and services | 476.6 | -0.8 | -6.4 | 9.5 | 4.6 | 5.0 |
| Imports of goods and services | 387.0 | -0.2 | -4.4 | 2.5 | 3.5 | 5.4 |
| Net exports[1] | 89.6 | -0.4 | -1.8 | 4.6 | 1.2 | 0.6 |
| **Other indicators** (growth rates, unless specified) | | | | | | |
| Potential GDP | . . | 1.4 | 1.3 | 1.3 | 1.3 | 1.3 |
| Output gap[2] | . . | 0.8 | -3.0 | -0.9 | 0.8 | 1.3 |
| Employment | . . | 0.7 | -0.2 | -0.2 | 1.0 | 0.4 |
| Unemployment rate (% of labour force) | . . | 4.4 | 4.8 | 5.1 | 4.8 | 4.6 |
| GDP deflator | . . | -0.1 | -0.5 | 1.4 | 1.4 | 1.0 |
| Consumer price index | . . | 0.4 | -0.7 | 0.6 | 1.1 | 0.8 |
| Core consumer price index[3] | . . | 0.4 | -0.3 | 0.3 | 0.7 | 0.8 |
| Household saving ratio, net (% of disposable income) | . . | 17.4 | 23.1 | 23.0 | 20.1 | 18.7 |
| Current account balance (% of GDP) | . . | 4.9 | 1.2 | 7.0 | 7.7 | 7.4 |
| General government financial balance (% of GDP) | . . | 1.3 | -2.8 | -2.3 | 0.2 | 0.8 |
| Underlying government primary financial balance[2] (% of GDP) | . . | 1.0 | -1.3 | -1.8 | -0.1 | 0.3 |
| General government gross debt (% of GDP) | . . | 41.0 | 43.9 | 46.9 | 47.3 | 47.0 |
| General government net debt (% of GDP) | . . | -16.3 | -17.2 | -14.1 | -13.7 | -14.1 |
| Three-month money market rate, average | . . | -0.7 | -0.7 | -0.8 | -0.8 | -0.8 |
| Ten-year government bond yield, average | . . | -0.5 | -0.5 | -0.2 | -0.2 | -0.2 |

Note: This set of projections has been prepared by the OECD desk, following the latest update of GDP numbers, without the OECD-wide update in projections. The table is therefore based on the OECD Economic Outlook 110 database with updates to selected variables.
1. Contribution to changes in real GDP.
2. Percentage of potential GDP.
3. Consumer price index excluding food and energy.
Source: OECD Economic Outlook database.

Uncertainty is high. The renewed fast-paced surge in infections could require drastic measures and weigh on the economy. Potential lower efficacy of vaccines on new variants would have a similar effect. The willingness of the population to be vaccinated is becoming an increasingly important factor. On the upside, further progress in vaccination could be more rapid than assumed or the pandemic could retreat more quickly than expected. Also, a faster rundown of accumulated savings could result in higher consumption and activity. As a very open economy, Switzerland is at risk of being significantly affected by potential trade disruptions due to renewed pandemic waves, geopolitical tensions or new trade barriers, including in the trade with the EU. The continued rise in imbalances in the domestic real estate market raises vulnerabilities.

## Table 1.2. Low-probability events that could lead to major changes in the outlook

| Shock | Possible Impact |
|---|---|
| Renewed major global pandemic wave with a virus variant resistant to existing vaccines | This would trigger renewed containment measures, with adverse impact on incomes and employment. Pressures on public finances could lead to defaults abroad and result in tightened financing conditions in Switzerland, due to safe haven pressures on the franc and rising risk premia. |
| International corporate debt crisis | Amid high and rising levels of corporate indebtedness globally, a downturn could lead to debt-servicing problems for highly leveraged companies and repricing of risk with reverberations through international financial markets. Safe-haven flows could push up the exchange rate, reducing Swiss exports, hurting confidence and raising deflation risks. Internationally active banks could also be exposed. |
| Intensification of global trade tensions | As a small open economy, Switzerland would be severely affected by a major increase in barriers to trade and capital flows. |
| Major house price correction and sudden rises in interest rates | A large correction in housing prices coinciding with a further economic downturn could expose vulnerabilities in the financial system, causing a crisis in the financial sector that could feed back to the real economy. In addition, sudden rises in interest rates would sharply increase debt-servicing costs for highly leveraged households and investors, raising the risk of defaults. |

### *Monetary policy remains accommodative*

Monetary policy has been expansionary since the global financial crisis. The policy interest rate has been stable at -0.75% since 2015, the lowest in the OECD (Figure 1.9). However, the negative interest rates put pressures on interest margins and weigh on bank profitability. In order to ease pressures on banks, in March 2020, the Swiss National Bank (SNB) raised the exemption ratio (i.e. raised the threshold factor from 25 to 30), thereby reducing the share of reserves on which banks earn negative interest. With this, the SNB can still successfully steer money market rates close to the targeted policy rate without unnecessarily penalising banks (Maechler and Moser, 2020), strengthening their role as credit providers during the crisis. In addition, to facilitate further credit activity by banks, the Federal Council deactivated in March 2020 the countercyclical capital buffer targeted at mortgage loans financing residential real estate (previously 2%).

To help companies bridge liquidity shortages during the COVID-19 crisis, the government introduced a guarantee programme for corporate loans (COVID-19 credits), available between end-March and end-July 2020. As a complement, the Swiss National Bank (SNB) set up the SNB COVID-19 refinancing facility, enabling banks to access the required liquidity at the SNB policy rate. The programme is estimated to have reached 20% of all Swiss firms (Fuhrer et al., 2020) with a total size of the programme at 2.4% of GDP. Moreover, the programme successfully reached young and small firms that tend to be more financially vulnerable during crises.

The SNB intervened heavily in the foreign exchange market in the first half of 2020 to stave off appreciation pressures on the Swiss franc caused by safe-haven capital inflows and resulting deflationary pressures. The pressures on the franc subsequently eased and interventions subsided, but overall, the Swiss franc gained roughly 6% between December 2019 and November 2021 (Figure 1.9).

The SNB remains committed to foreign exchange interventions if needed. Due to negative interest rates and a relatively small domestic bond market (reducing scope for asset purchases) the exchange rate is one instrument that helps steer monetary conditions and fulfil the mandate of price stability. However, high accumulated foreign reserves expose the central bank balance sheet to the risk of sizable valuation losses.

### Box 1.1. Monetary policy framework

According to article 99 of the Federal Constitution and the National Bank Act (art.5 para.1), the mandate of the Swiss National Bank (SNB) is to ensure price stability, its primary objective, while taking due account of economic developments.

The SNB's monetary policy strategy, in place since 2000, sets out how the SNB implements its mandate. Price stability is stated as the CPI inflation standing below 2% annually, while remaining positive. Deflation, i.e. a protracted decline in the price level, is regarded as a breach of the objective of price stability. The SNB does not react mechanically to temporary deviations from the price stability objective. For example, if inflation temporarily exceeds the 2% ceiling as a result of one-off factors, monetary policy does not necessarily need to be adjusted. The same applies for short-lived deflationary pressures.

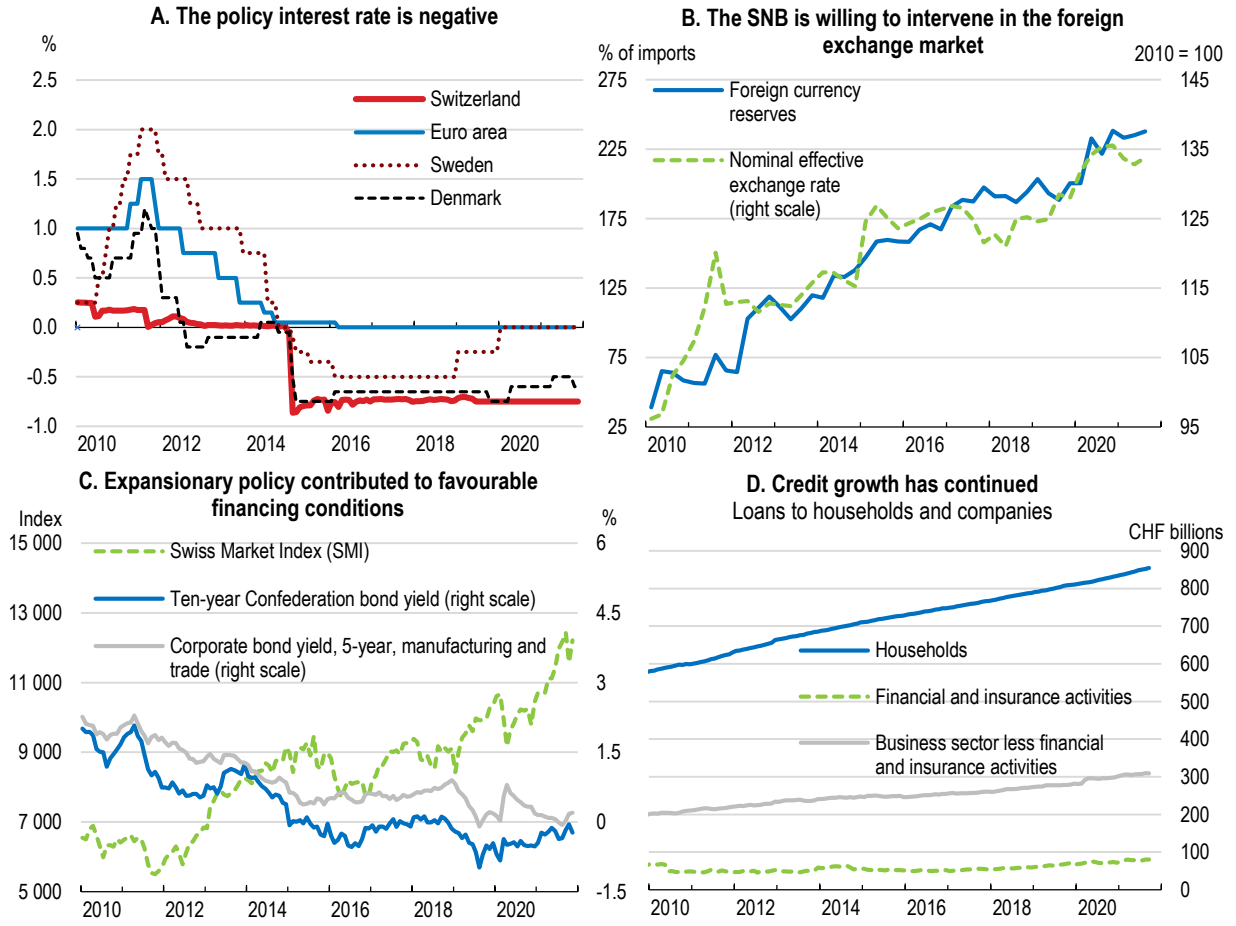
Conditional inflation forecasts for the next three years serve as the main indicator for monetary policy decisions. The SNB considers also a range of indicators on domestic and international economic and financial developments.

The SNB implements its monetary policy by setting the SNB policy rate. The SNB seeks to keep the secured short-term Swiss franc money market rates close to the SNB policy rate. In the current negative-rate environment, it does so by charging banks and other financial institutions interest on part of their sight deposits with the SNB. Given that the policy rate cannot be lowered indefinitely, the SNB also intervenes in the foreign exchange market as necessary to influence monetary conditions. Besides the negative rate on sight deposits and the FX interventions, policy is implemented with traditional open market operations (e.g. repos) and standing facilities.

The monetary policy stance is reviewed quarterly, and monetary policy decisions are taken quarterly by the SNB Governing Board (or more frequently if necessary). The decisions are announced in press releases. In June and December, the members of the Governing Board also explain the monetary policy decision at a press conference.

The SNB's expansionary monetary policy provided favourable financing conditions and contributed to ample supply of credit and liquidity to the economy. Despite a steep drop in GDP in the first half of 2020, liquidity was maintained and annual growth in bank lending remained robust, even after the COVID-19 credit guarantee programme ended (Figure 1.9). Private sector companies surveyed in Q1 and Q2 2021 reported that there had been hardly any delays in payments on the part of their customers and practically no bad debt losses (SNB, 2021a and 2021b). This said, prospects for inflation remain moderate and long-term inflation expectations remain well-anchored (SNB, 2021b), while risks and uncertainty are still elevated. Monetary policy should therefore remain accommodative, until the domestic economy is firmly on a sustainable recovery path.

## Figure 1.9. Monetary policy remains accommodative




Note: On 13 June 2019 a new monetary policy rate was introduced and the reference rate became the SARON. Prior to this, the SNB set a target range for the three-month Swiss franc LIBOR with the latter used as the policy reference rate (shown in Panel A).
Source: Refinitiv; OECD Economic Outlook; SNB.

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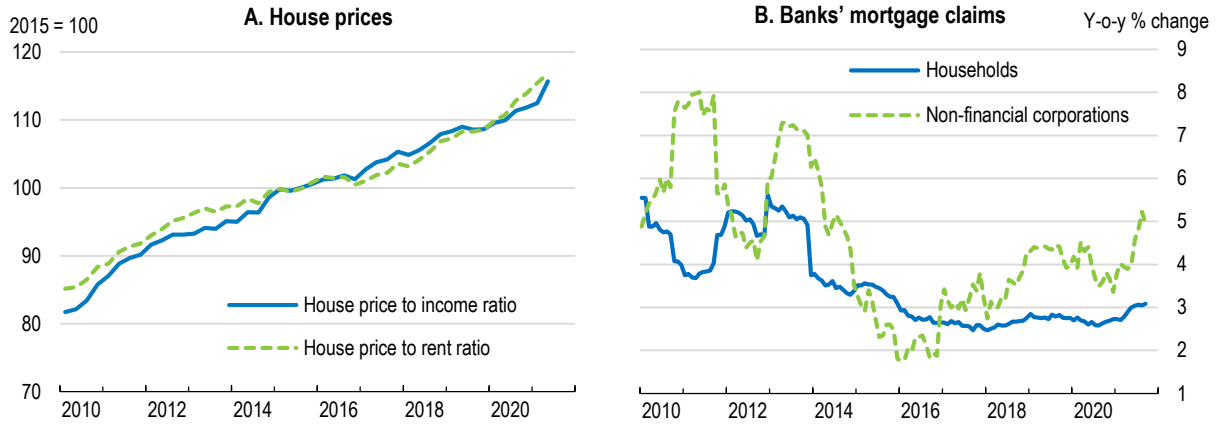
Risks in the financial sector have risen during the crisis, as also recognised by the financial sector supervisor FINMA in its publication the Risk Monitor (FINMA, 2021 and 2020a). Thanks to adequate capital and liquidity buffers the Swiss financial system was able to withstand the challenges. The share of non-performing loans and the level of impaired claims have increased slightly, but remain low by historical standards (SNB, 2021c). However, credit defaults and market corrections may materialise only with delay once the extensive policy support at home and abroad is withdrawn. Stress tests by the SNB (2020a and 2021c) and FINMA (2020b) show that most institutions would be able to cope with a further deterioration in economic conditions without seriously impairing their lending capacity. Nevertheless, a number of individual institutions face a risk of their capital being more seriously depleted in adverse circumstances (SNB, 2020a and 2021c).

Close monitoring of risks and adequate buffers should be maintained. The authorities should consider reactivating the countercyclical capital buffer targeted at residential mortgage loans. There is also further progress to be made on managing risks from “too-big-to-fail” banks. Big losses incurred by Credit Suisse (more than USD 5 billion) and UBS (several hundred million) from exposures to a US hedge fund (Archegos Capital Management) highlighted how significant shocks can occur even without a macroeconomic or system-wide financial shock. The three domestic systemically-important banks are yet to prepare effective emergency plans, with the two global banks (Credit Suisse and UBS) having done so successfully in 2019.

However, the latter two still need to become fully resolvable, so that in the event of a crisis they can be restructured or liquidated without endangering financial stability (FINMA, 2020c). A recent review has also found that there is room to strengthen liquidity requirements of the systemically-important banks to cover liquidity needs in an emergency (Federal Council, 2021a). Continued vigilance, effective regulation and risk oversight are also needed in the fintech sector.

The build-up of imbalances in the residential real estate market has also continued, partly as a side effect of low interest rates. Growth in real estate prices and in mortgage loans has remained largely unabated (Figure 1.10), despite the economic slowdown. The mortgage-to-GDP ratio is already very high by international standards and has continued growing, indicating growing vulnerabilities. In the residential investment property segment, price rises continued in spite of high vacancies (SNB, 2020a and 2021c). These imbalances expose debtors and creditors to shocks to the interest rate or further economic deterioration that could adversely affect mortgage repayments and rents. According to an assessment by FINMA (2021), a real estate crisis involving sharp price corrections could lead to large losses, and capital in a number of banks would be significantly depleted. This would have adverse consequences for financial stability.

**Figure 1.10. The build-up of imbalances in the residential real estate market has continued**




Source: OECD, Analytical House Price Indicators database; SNB.

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To prevent a further build-up of imbalances in the housing market, the Swiss Bankers Association, with effect from January 1st 2020, tightened self-regulation for mortgage loans on the investment property market, by requiring higher down-payments and faster mortgage repayment. These changes were recognised by FINMA as binding minimum standards (FINMA, 2019). Switzerland would however benefit from a broader toolkit of macroprudential measures that take into account affordability, for instance debt-to-income and debt-service-to-income limits on mortgage loans. In addition, as recommended in previous Surveys (OECD 2017a and 2019a), the framework for setting macroprudential rules should be strengthened, with SNB and FINMA given clear and strong mandates to propose and calibrate the tools. Currently, the rules are set in agreement with the Swiss Bankers Association, which may impact timeliness and stringency (IMF, 2019).

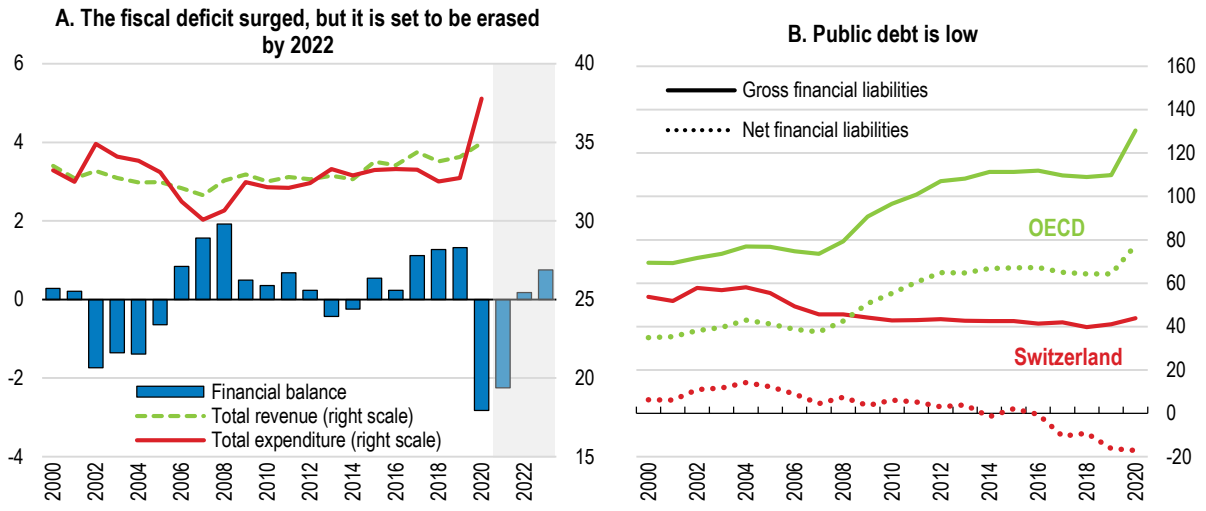
### *Fiscal policy should avoid premature tightening*

Extensive emergency spending and markedly lower fiscal revenues pushed public finances into a deficit. After five consecutive years of surpluses, the general government deficit reached 2.8% of GDP in 2020. A slightly smaller deficit is expected in 2021, at 2.3% of GDP, and a surplus in 2022, at 0.2% of GDP (Figure 1.11). The total cost of pandemic-related extraordinary fiscal measures is estimated at CHF 17 billion in 2020, and just slightly more in 2021, about 2.4% of GDP each year (FFA, 2021a). The federal

government also provided guarantees to companies, in the amount of CHF 17.5 billion outstanding at the end of 2020 (FFA, 2021b).

### Figure 1.11. Emergency fiscal measures pushed public balance into a deficit

General government, % of GDP




Source: OECD Economic Outlook database.

StatLink https://stat.link/i7tdbs

The fiscal loosening was appropriate given the severity of the crisis and available fiscal space. Gross general government debt at 44% of GDP in 2020 remains low in international comparison (Figure 1.11). Moreover, net debt is negative (i.e. positive net financial assets, at 17% of GDP) and interest rates on issuing new debt remain at historically low levels. Between mid-2000s and 2019, a frugal fiscal policy led to a marked decrease in Swiss public debt, in contrast to many other OECD economies (Figure 1.11). This was achieved within the framework of the federal debt brake rule (and cantonal fiscal rules) that aims to use fiscal policy as a stabilisation tool over the economic cycle as well as pursue fiscal sustainability by keeping nominal debt stable (i.e. a declining debt-to-GDP ratio) (Box 1.2).

However, the existing federal debt brake framework risks tightening fiscal policy too soon. The debt brake sets an annual expenditure ceiling based on expected ordinary fiscal revenues adjusted for cyclical factors, ensuring the counter-cyclicality of fiscal policy. Ex-post, over- or under-spending within the “ordinary” budget is either debited or credited to a compensation account, but positive balances from underspending can only be used to reduce debt. Additional flexibility is possible in exceptional circumstances via extraordinary expenditures that are not bound by the limits on the “ordinary” expenditure ceiling. Extraordinary spending is accounted for on the so-called “amortisation” account, whose deficit then needs to be eliminated within 6 years after the end of exceptional circumstances. However, Parliament can extend this period. The authorities estimate that the negative balance on the amortisation account resulting from COVID-19-related extraordinary expenditures could rise to CHF 25 billion (3.5% of GDP) by the end of 2021 (FFA, 2021c). Closing this gap in 6 years would entail a structural consolidation of 0.6 percentage points of GDP per year over the 2022-2027 period. This would come on top of the limits on ordinary spending growth prescribed within the debt brake framework due to the gradual cyclical improvement of the economy.

### Box 1.2. The debt brake rule

The debt brake rule is a central element of the Swiss fiscal framework at the federal level. It subjects the Confederation's fiscal policy to a binding rule. Its principles have been accepted by popular vote on December 2001 and its core provisions are enshrined in the Federal Constitution (article 126). Details are set out in the Financial Budget Act.

The debt brake is designed to ensure that fiscal policy remains sustainable over the long term by aiming to keep nominal debt stable (i.e. a declining debt-to-GDP ratio). The rule also takes into account the economic cycle in order to help smooth growth fluctuations. It is a structural deficit rule that limits expenditures to the amount of structural (i.e. cyclically adjusted) revenues. Thus, the debt brake does not require budgets to be balanced on an annual basis, but only over an entire economic cycle. Within this mechanism, total federal government expenditures are kept relatively independent from the cycle whereas tax revenues act as automatic stabilizers. Actual deviations from the limit set by the rule result in a credit or debit to the so-called "compensation account". Deficits in this account must be considered when setting the new expenditures ceiling for the following year and eliminated in the subsequent years. Moreover, in principle, positive balances from underspending can only be used to reduce debt.

In extraordinary circumstances (such as severe recessions or natural disasters), the rule's expenditures ceiling can be raised by a qualified majority of both chambers of parliament, whereby a binding rule also applies for the extraordinary budget. Extraordinary receipts and expenditures are recorded on an amortisation account and any deficits on the amortisation account due to extraordinary expenditures have to be covered over the course of six years by means of surpluses in the ordinary budget. In special situations, the parliament has the power to extend the six-year deadline.

Rapid fiscal tightening in the aftermath of the crisis could undermine the recovery and should be avoided. One option is to exceptionally use the positive balances on the compensation account (from previous underspending) to reduce part of the amortisation account deficit. A longer payback period for the amortisation account could also be considered, to ease immediate pressures towards fiscal tightening. In view of the challenges related to fiscal policy in the medium run, the Parliament has tasked the Federal Council to propose an amendment that would allow the debt associated with the coronavirus crisis to be managed without resorting to budget cuts and tax increases.

Over the summer 2021, the Federal Council decided on a balanced (federal) ordinary budget for 2022, and an additional CHF 1.2 billion in extraordinary expenditure in 2022 linked to the aftermath of the COVID-19 crisis. However, these are planned to be compensated by the supplementary distribution of SNB profits in the maximum amount of CHF 1.3 billion, accounted under extraordinary receipts (FFA, 2021c). Subject to the conditions defined in the agreement between the Federal Department of Finance and the SNB (i.e. availability of sufficient reserves for distribution), a supplementary distribution in similar amounts (roughly 0.2% of GDP) will also take place over 2023-2025, helping reduce the COVID-19 debt (Federal Council, 2021b).

Furthermore, in the summer 2021, the Federal Council opened the consultation process for a temporary amendment to the Financial Budget Act in order to help offset the COVID-19 debt. Options include using future surpluses in the ordinary budget (that historically have occurred regularly due to slight underspending) to reduce the debt over the medium term, or, alternatively, using past accumulated surpluses to reduce part of the debt. In early 2022, once the real financial impact on the federal budget will be better known, the Federal Council will decide which solution will be submitted to Parliament and the amendment could thus enter into force at the beginning of 2023.

Reviewing the debt brake also provides an opportunity to improve its implementation in the future. As reported in the previous Survey (OECD, 2019a), revenue forecasts tend to be on the conservative side and persistent underspending (compared to the approved spending ceilings) is the norm. A case in point,

in the exceptional circumstances of the coronavirus pandemic a cyclical/ordinary deficit of CHF 2.9 billion would have been permitted in 2020 at the federal level, but in reality the ordinary deficit amounted to 1.2 billion, leading to a 1.6 billion (0.2% of GDP) "structural surplus" (FFA, 2021b). This resulted in a credit to the compensation account that in principle cannot be transferred to cover extraordinary expenditures (unless budgeted ex-ante). In the current juncture, moving to fuller use of available fiscal space would support economic recovery as well as lower the burden on monetary policy. Moreover, the government would have more leeway to pursue structural reform, for instance by further expanding affordable childcare, reducing inequities in education and training and pursuing a more ambitious investment agenda in green technology and green R&D.

### Table 1.3. The fiscal position is strong

General government, % of GDP

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|---|---|---|
| **Total revenues** | **32.7** | **32.9** | **32.7** | **33.8** | **33.5** | **34.4** | **33.8** | **34.1** | **35.0** |
| Taxes | 19.6 | 19.7 | 19.6 | 20.3 | 20.3 | 21.0 | 20.6 | 20.9 | 20.8 |
| Social contributions | 6.5 | 6.6 | 6.5 | 6.6 | 6.6 | 6.6 | 6.4 | 6.5 | 7.0 |
| Other revenues | 6.5 | 6.6 | 6.5 | 6.9 | 6.7 | 6.8 | 6.8 | 6.6 | 7.1 |
| **Total expenditures** | **32.4** | **33.3** | **32.9** | **33.2** | **33.3** | **33.3** | **32.5** | **32.8** | **37.8** |
| Social protection | 12.5 | 13.3 | 13.0 | 13.1 | 13.3 | 13.2 | 12.9 | 12.9 | .. |
| Education and health | 7.3 | 7.4 | 7.4 | 7.5 | 7.6 | 7.5 | 7.4 | 7.6 | .. |
| General public services | 4.4 | 4.4 | 4.4 | 4.5 | 4.4 | 4.4 | 4.3 | 4.2 | .. |
| Economic affairs | 4.0 | 4.0 | 3.9 | 4.0 | 3.9 | 3.9 | 3.9 | 3.9 | .. |
| Other[1] | 4.1 | 4.2 | 4.1 | 4.2 | 4.2 | 4.2 | 4.1 | 4.2 | .. |
| **Net lending** | **0.2** | **-0.4** | **-0.2** | **0.5** | **0.2** | **1.1** | **1.3** | **1.3** | **-2.8** |
| Primary balance | 0.6 | -0.2 | 0.0 | 0.8 | 0.4 | 1.3 | 1.4 | 1.4 | -2.8 |
| **Gross debt** | **43.4** | **42.6** | **42.6** | **42.5** | **41.3** | **42.0** | **39.8** | **41.0** | **43.9** |
| Net debt | 3.1 | 3.9 | -1.6 | 2.2 | -0.6 | -10.5 | -9.1 | -16.3 | -17.2 |

1. Defence; public order and safety; housing and community amenities; recreation, culture and religion; environment protection.
Source: OECD National Accounts database; Economic Outlook database.

### Box 1.3. Potential impact of reforms

Structural reforms can boost economic growth and incomes. Table 1.4 quantifies the impact on growth of some of the reforms recommended in this Survey (quantification is not feasible for all of them) based on the OECD long-term model and OECD estimates of relationships between reforms and total factor productivity, capital deepening and the employment (Égert, 2017). The analysis suggests that if Switzerland implemented the selected set of reforms (see below), per capita income could increase by about 3% in 10 years. The estimates are illustrative.

### Table 1.4. Potential impact of structural reforms on per capita GDP

| | 10 years |
|---|---|
| Improve the business environment (less state involvement, lower barriers to trade and investment). | 1.7% |
| Boost active labour market policies. | 0.9% |
| Keep expanding the supply of affordable and high-quality childcare facilities. | 0.3% |
| Reform the pension system (lifting the retirement age). | 0.3% |
| **Package of reforms** | **3.3%** |

Note: Simulations based on the OECD Economics Department Long-term Model. A no policy change scenario is used as the baseline. The following changes in policy/outcomes are assumed. The Product Market Regulation (PMR) components where Switzerland underperforms are reduced to OECD average (reduced state ownership of the economy, less regulation in network sectors and lower barriers to trade and investment). Active labour market policies are boosted to reach the average of five top performers in the OECD (as % of GDP per capita per unemployed person). Family benefits in kind (% of GDP) are increased to OECD average. Pension reform: first equalising retirement age for men and women at 65, then retirement age gradually rises to 67 in 2034, and by half of the expected gain in life expectancy thereafter (to reach 68 in 2058).
Source: OECD calculations.

The following estimates quantify the direct fiscal impact of selected recommendations included in the Survey. The estimates are illustrative.

### Table 1.5. Illustrative direct fiscal impact of selected recommended reforms

| Reform | Fiscal impact (savings (+)/ costs (-)) (% of GDP) |
|---|---|
| Improve the business environment (less state involvement, lower barriers to trade and investment). | Negligible |
| Boost active labour market policies. | -0.2% |
| Keep expanding the supply of affordable and high-quality childcare facilities. | -0.4% |
| Improve the implementation of the debt-brake rule (reduce underspending). | *-0.4% (other reforms listed here can be financed from this)* |
| Make the tax mix more growth friendly. | Fiscally neutral reform |
| Reform the pension system (lifting the retirement age). | +1.1% (by 2060) |

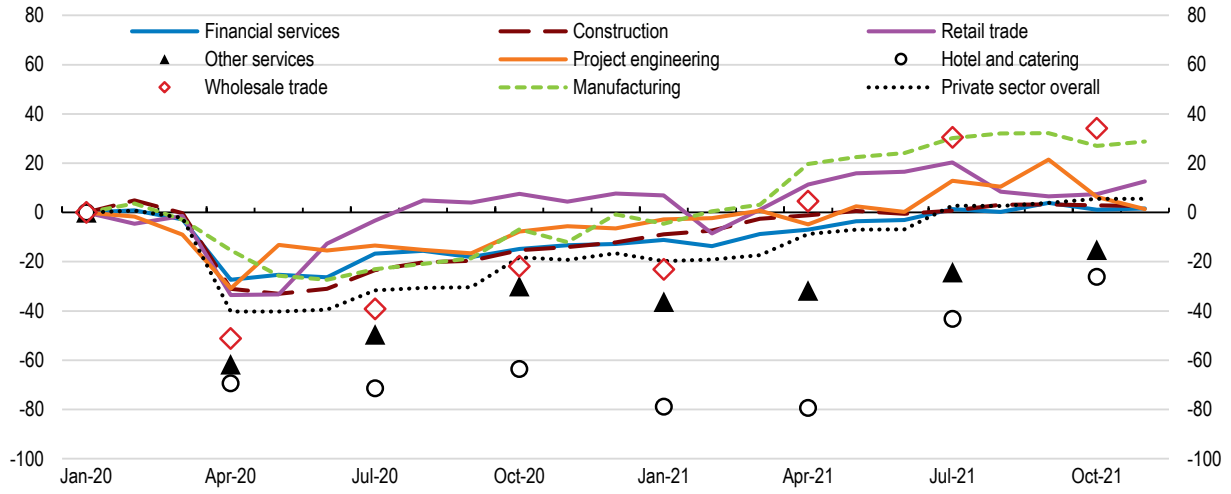
Note: Fiscal room of 0.4% of GDP under the debt-brake rule was estimated in the previous OECD Switzerland Survey (OECD, 2019a). Tax reform includes: reducing personal income taxes (for second earners), financed by raising VAT and taxes on immovable property; phasing out environmentally harmful tax exemptions and subsides; phasing out interest deductibility in personal income tax and broadening the base for taxing capital gains. The fiscal dividend of the pension reform is computed by taking a difference between the required increase in government revenues to keep debt-to-GDP ratio stable in "baseline" and "pension reform" scenarios. See also Figure 1.24 below. Based on simulations of the OECD Economics Department Long-term Model.
Source: OECD calculations.

### *Supporting hardest-hit firms and facilitating job reallocation*

The crisis had differing impacts across sectors and groups. In the first quarter of 2021, while close to 70% of companies reported that the crisis had a negative impact on their business, about 15% reported a positive impact (SNB, 2021a). Some sectors experienced a boost to their activities and were hiring new staff. The health care and social services sectors and the IT sector displayed more job postings in November 2020 than a year earlier (X28-Novalytica). Also, as reflected in the KOF Business indicator (Figure 1.12), sectors such as manufacturing and construction-related activities steadily recovered towards pre-crisis levels by the end of 2020, as they were able to adapt to changes in working arrangements and sanitary restrictions. The business situation in the retail sector quite closely followed the strictness of lockdowns and recovered relatively quickly after spring 2020 and again after winter 2020-21. In contrast, sectors such as hotels and catering, passenger airlines and wholesale trade remained severely affected for more than a year. For the hardest-hit sectors there is a risk that consumer preferences may have changed and that demand will not recover to pre-crisis level even in the longer term.

## Figure 1.12. The crisis had differing impacts across sectors

KOF Business Situation indicator, seasonally adjusted balances, cumulative from January 2020




Source: KOF Swiss Economic Institute.

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Debt financing and credit guarantees have helped to ease immediate financial constraints on companies and contain financial stress. As in several other OECD economies, the number of corporate bankruptcies actually decreased in 2020, by 6.6% year-on-year (FSO, 2021). This can be attributed to public support as well as the easing of bankruptcy regulations for COVID-19 affected companies. It is, however, likely that many companies, especially SMEs, face deteriorating balance sheets due to low profitability and rising debt (OECD, 2021a, Chetty et al., 2020, Gourinchas et al., 2020, Diez et al., 2021). In June 2021, the KOF Swiss Economic Institute (2021) reported that corporate bankruptcies were on the rise in some industries, such as hospitality and transportation, but they have not reached high levels.

Too early withdrawal of support could trigger unnecessary bankruptcies and labour shedding and may result in labour scarring and poverty. Ending crisis-related support measures should be contingent on removing confinement measures that limit doing business in high-contact sectors. Continued support for households and companies therefore remains warranted in certain sectors, but needs to be carefully targeted (OECD, 2021a and 2021b).

Finding a balance between supporting viable firms and phasing out support for other businesses is a challenge. Company financial distress may increase once support is withdrawn. The rapid debt build-up due to the crisis – including as a result of liquidity-support measures - could pose risks to financial stability and result in debt overhang, adversely affecting private investment and growth (OECD, 2021a). On the other hand, too generous public support for too long risks keeping unviable firms artificially alive ("zombie" firms), stripping viable firms of valuable resources, hindering productivity growth and recovery.

In the short term, policy makers could continue to provide liquidity to hardest-hit firms and to SMEs that may not directly benefit from the international recovery. Meanwhile, loan guarantee schemes could be fine-tuned to reduce the risk of moral hazard and adverse selection by reducing the portion of the loan backed by the government guarantee or increasing the fee to access the programmes. To avoid over-indebtedness and debt overhang, policy makers could consider the use of non-debt instruments to support the corporate sector, for example by linking loan repayment to businesses' returns or converting government loans into grants (up to a ceiling and for specific operational costs). Establishing appropriate conditions for early and orderly debt restructuring would also help (Demmou and Franco, 2021; OECD, 2021a).

Effective insolvency procedures will also be crucial to minimise the loss of resources and spur productivity-enhancing capital reallocation (Adalet McGowan et al., 2017). Switzerland scores above the OECD

average on the strength of the insolvency framework index with low personal cost to failed entrepreneurs, effective provisions for prevention and low barriers to restructuring (Adalet McGowan and Andrews, 2018). However, according to the World Bank's Doing Business indicators based on a stylised case of corporate insolvency, there is ample room for improvement in practice. The recovery rate for creditors, at less than 50%, is markedly below the OECD mean of 70% (World Bank, 2020). Moreover, the procedure takes 3 years on average, while it takes less than two years in the OECD on average and less than six months in best performers (Ireland). As the number of insolvency cases will likely rise in the near future, adequate resources will be needed for the system to work effectively, including for recruiting and training staff.

The impact of the crisis on income and employment also differed greatly between households and groups of workers. Many households experienced a drop in incomes, either because they lost their jobs or because for most workers the compensation on short-time work stood below previous salaries. Survey data shows that short-time work schemes were used more by low to middle skilled and low-wage workers, suggesting that the crisis had a significantly stronger impact at the lower end of the wage distribution (see Chapter 2). Certainly, however, without the short-time working scheme and other protective measures, the adverse impact on employment and incomes would have been much more pronounced.

A key challenge is to provide sufficient support for viable jobs while helping displaced workers find new jobs in other sectors or locations (OECD, 2021b). Chapter 2 of this Survey discusses options to make the short-time work better targeted to hard-hit firms, for instance by asking firms not subject to restrictions to increasingly bear part of the cost of the scheme. Moreover, active labour market policies should be adapted across cantons, to offer displaced workers help in finding new jobs or gain new skills, and a stronger emphasis could be put on employment incentives for the most vulnerable workers. In the medium-term, boosting labour market participation by mothers and older workers would also boost growth.

### Box 1.4. Planned economic policy to aid the recovery after the crisis

In May 2021, the Federal Council discussed the way forward for economic policy once the majority of pandemic restrictions are lifted and the economic situation normalises. Speedy economic recovery is expected, but some companies and sectors will continue to face limited demand. The Federal Council has decided to follow a transition strategy around three policy principles: normalisation, support for structural change and boosting growth through structural reform.

*Normalisation*: the Federal Council intends to gradually abandon extraordinary stabilisation measures. Short-time work compensation will continue in 2022, but gradual scaling back of the crisis-related extensions to the scheme started in July 2021. Compensation for the loss of earnings linked to COVID-19 and public support to organisers of large events will be maintained until the end of 2022.

*Support for structural change*: use of standard tools to help workers and firms adapt to structural change, including unemployment insurance, promotion of innovation, tourism policy or regional policy. The current instruments will be reviewed and strengthened if necessary.

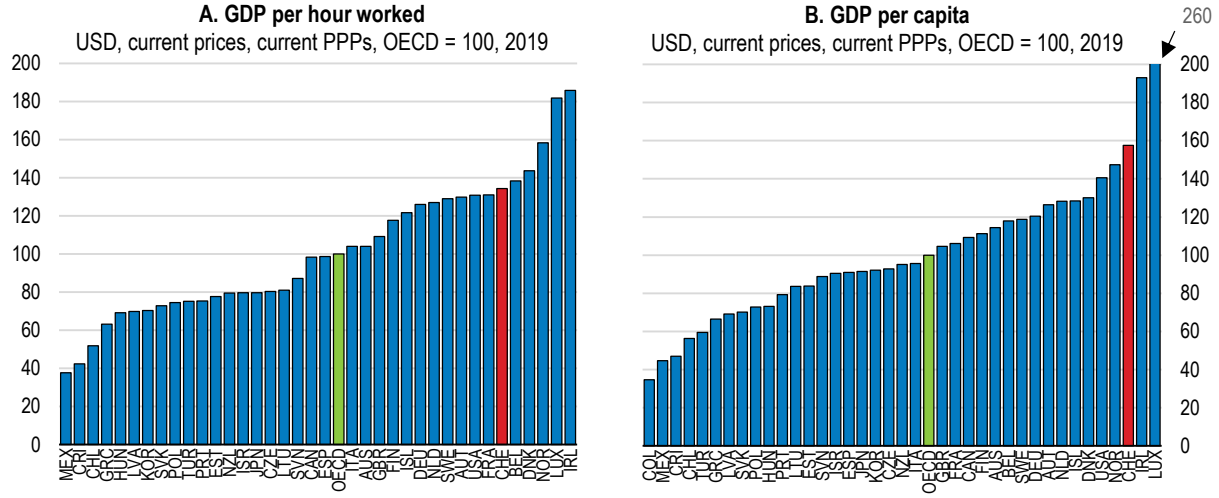
*Boosting growth*: various targeted measures to strengthen framework conditions and improve growth prospects, including for example, the "digital Switzerland" strategy, promoting decarbonisation, continued funding for investments in infrastructure (rail infrastructure, roads, electricity transmission), and lower administrative barriers to trade and entrepreneurship.

## Boosting competition to raise productivity and growth

Switzerland is one of the top OECD performers in terms of labour productivity. Together with high employment rates, this results in very high income levels (Figure 1.13). The stable macroeconomic environment, highly skilled workforce and openness to trade help sustain a globally competitive, high value-added economy. Labour productivity is particularly high in the food industry and manufacturing of

pharmaceuticals, and in a number of service sectors, including wholesale and retail trade, finance and public services (public administration, education and health) (Figure 1.14). The share of high-tech manufacturing in total manufacturing value-added is the highest in the OECD and the share of workers employed in elementary occupations one of the lowest (Figure 1.15). A profitable corporate sector and high human capital contribute to high business investment in R&D and top innovation performance.

## Figure 1.13. Switzerland is a top performer in terms of labour productivity and GDP per capita




Source: OECD Productivity database.

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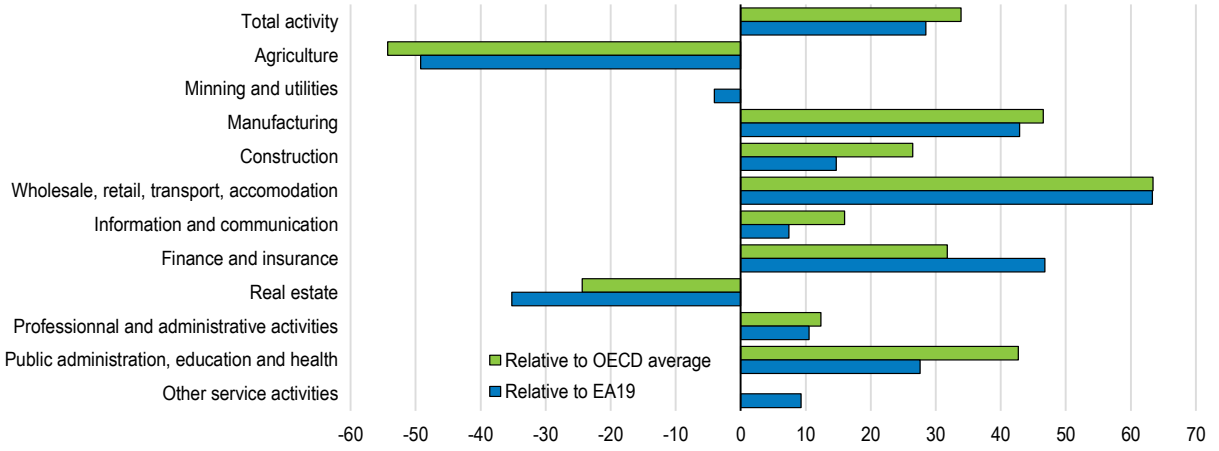
With population ageing weighing on potential GDP per capita growth and limits to employment growth, improving productivity and boosting capital investments are key to sustain living standards. Still, productivity growth has slowed down markedly (Figure 1.16). While this tendency has been observed across the OECD, the slowdown began earlier in Switzerland and productivity growth has been mostly below peers over the last two decades (Figure 1.17). Lower barriers to trade and competition and an improved business environment can generate investments that will foster productivity improvements as well as help revive economic growth. As discussed in the previous survey (OECD, 2019a), promoting a more dynamic business environment can also spur faster adoption of digital technologies.

## Figure 1.14. Productivity is very high in a number of sectors

Percentage point difference in labour productivity (GVA per person employed), 2016




Note: Gross Value Added (GVA) is GVA in current prices, current USD PPPs. OECD average include 30 OECD countries.
Source: OECD calculations based on OECD National Accounts Statistics.

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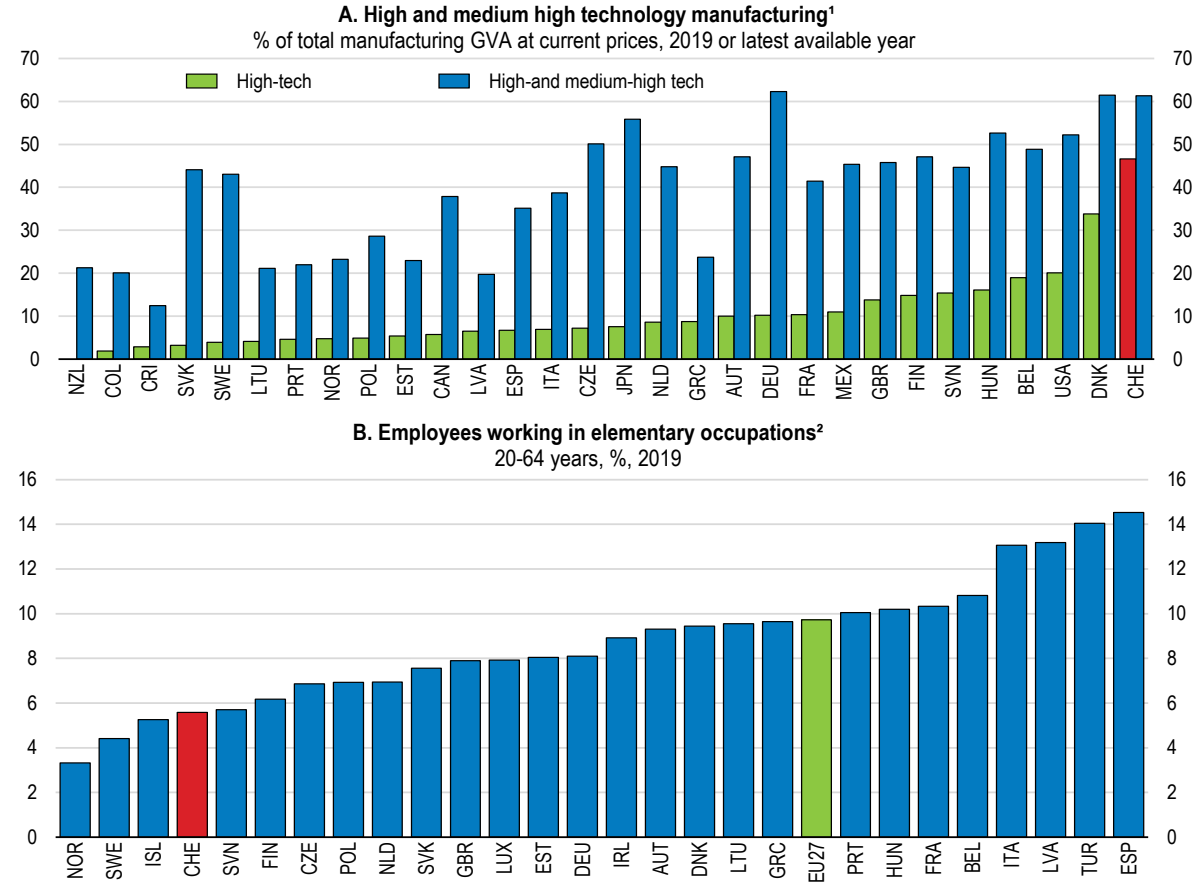
## Figure 1.15. The globally competitive and high value-added economy is sustained by a highly skilled workforce




1. Based on Eurostat aggregation of the manufacturing industry according to technological intensity, based on NACE Rev.2, 2 digit level.
2. Elementary occupations are defined in the ILO's International Standard of Classification of Occupations (ISCO). The occupations consist of simple and routine tasks which mainly require the use of hand-held tools and often some physical effort. The skills required correspond to primary education (around five years).
Source: OECD National Accounts Statistics; Eurostat database [lfsa_eegais].

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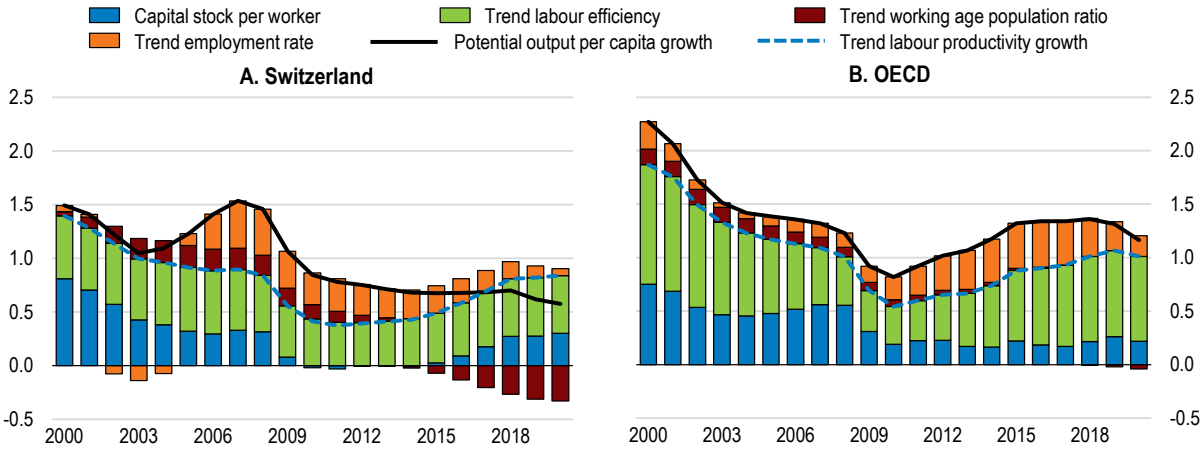
## Figure 1.16. With ageing, productivity growth will be key to sustain living standards

Contribution to potential output per capita growth, in % points




Source: OECD Economic Outlook 110 database.

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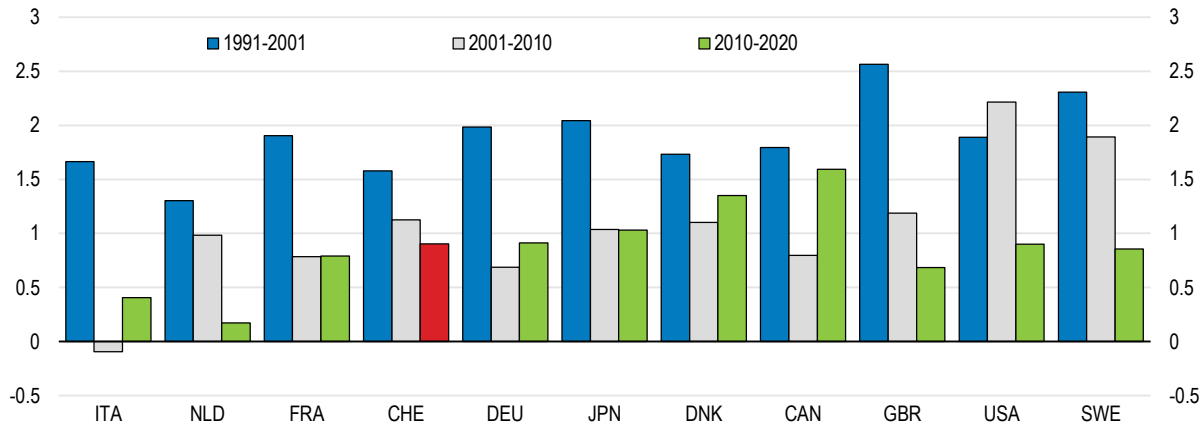
## Figure 1.17. Productivity growth has slowed

GDP per hour worked, USD, constant prices, constant PPPs, annual average % change




Note: Country ranking is based on the whole period.
Source: OECD Productivity database.

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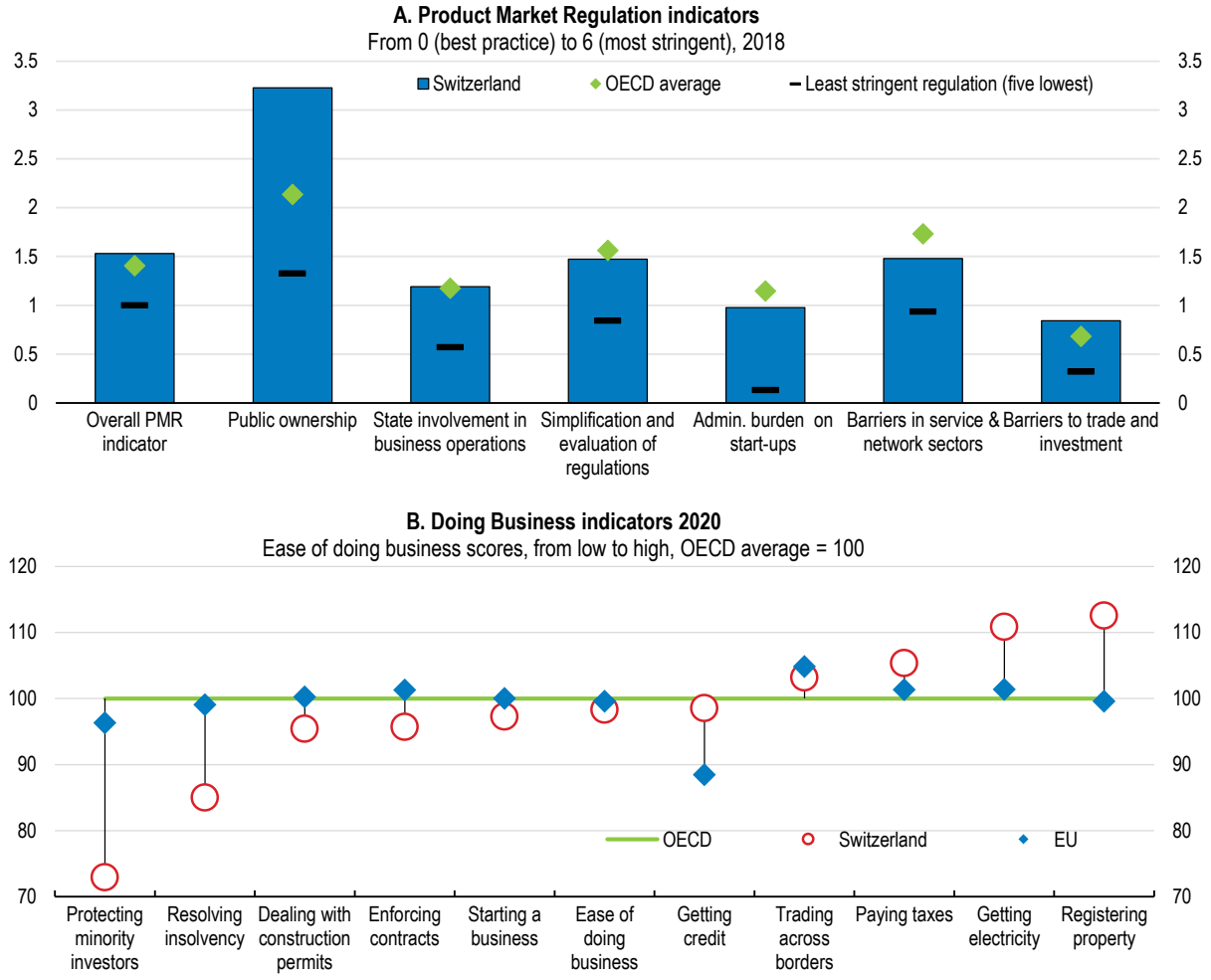
### *Improving regulatory settings*

There is room to improve regulatory settings, as suggested by Product Market Regulation (PMR) indicators (Figure 1.18). The administrative burden on start-ups is around the OECD average, but higher than in best performing OECD members. The number of procedures to open a company and the monetary cost to complete them are higher than in OECD best performers and the amount of required minimum capital for limited liability companies is also relatively high.

The World Bank Doing Business indicators (World Bank, 2020) also show a number of weaknesses (Figure 1.18), including relatively more burdensome and time-consuming procedures for starting a business than in most other OECD members. Furthermore, resolving commercial disputes ("enforcing contracts") takes longer than on average in the OECD, and is more costly to businesses. The process for obtaining construction permits is also relatively slow and cumbersome. To build a warehouse, 13 different procedures are required and the process takes a bit above five months, almost a month longer than in the OECD on average (World Bank, 2020). Such delays in planning and issuing permits have repercussions for the wider economy, as they slow down investment and impair entrepreneurship.

Since 2017, a one-stop shop (EasyGov.swiss) has eased markedly the administrative burden on companies. It has been constantly expanding and it should be expanded further, as planned, notably by ensuring the integration of cantonal government services. "Silence is consent" licensing rules, whereby licenses are automatically issued if the competent authority has not acted in a given timeframe, could also ease procedures, as in several other OECD countries.

## Figure 1.18. There is room to improve regulatory settings




Note: EU is an unweighted average of EU countries that are members of the OECD.
Source: OECD 2018 PMR database; World Bank Doing Business indicators 2020.

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Despite continuous improvements, competition in the domestic market is still hampered by cantonal borders (Competition Commission, 2018). According to the Internal Market Act, all businesses or professions that can successfully operate in one canton must be allowed to operate in all other cantons. To name a few recent examples of potentially hampered internal competition (Competition Commission, 2020), cantons need to recognise professional licences from other cantons without further examination, but there have been barriers in the health sector, for instance. Also, some cantons have imposed "protection charges" (to protect business secrets) in connection with public invitations to tender. The Competition Commission watches over the implementation of the Internal Market Act and works continuously to ensure that new national or cantonal regulations and public procurement processes are in line with the Act and that they do not raise unwarranted barriers. The Competition Commission is also increasingly involved in awareness raising and issuing advisory notes (Competition Commission, 2018, 2019 and 2020).

The merger control framework remains more permissive than in EU countries, but reform efforts have been stalled. Over the last four years, fewer than 10% of merger notifications were investigated after preliminary examination (Competition Commission, 2018, 2019 and 2020), which potentially indicates overly lenient regulation. As recommended in past Surveys (OECD, 2017a and 2019a) and as called for by the

Competition Commission (2018), harmonisation with the European Union's merger control system would be beneficial. In particular, Switzerland should adopt the "significant impediment of effective competition" (SIEC) test of market dominance, which focuses on the changes to effective competition in a market following a merger rather than narrowly on the absolute level of market power (Röller and De La Mano, 2006; Jaag et al., 2017). Studies have shown that introducing the SIEC test would result in a strengthened competitive environment and could facilitate interventions against anticompetitive mergers by the Competition Commission (Jaag et al., 2017; Vaterlaus et al., 2020). In addition, harmonisation with the EU would simplify the examination of cross-border mergers.

Competition in Switzerland could also be boosted by strengthening the Cartel Act in a way that would further deter illegal practices of price collusion and bid rigging. As assessed by the Competition Commission (2019), while the current law provides that victims of unlawful restraints of competition are entitled to claim damages, in practice, such civil action is rare. This is because the hurdles that must be cleared in order to enforce civil claims related to cartels are excessively high (Competition Commission, 2019). Proving a violation of the competition law and quantifying damages is very complex and obtaining required evidence is difficult. The Competition Commission, under administrative law proceedings, can use more powerful investigation instruments (e.g. the power to search houses and business premises) than the civil courts. Moreover, civil claims related to cartels are subject to short prescriptive periods, making it difficult for victims to file a properly substantiated claim in time.

The scope of the civil law on cartels could be expanded so that the option of taking action in the civil courts, currently limited to competitors, would include all those affected by cartels. This would allow all end customers and public contractors, notably the cantons and municipalities, to enforce their rights in civil courts. In addition, the prescriptive period under the private law on cartels should be suspended for the time until the competition authority issues a legally binding decision. Such reforms were proposed by the Federal Council in 2012, but were never passed. In early 2020, the Federal Council announced that it would present to parliament a revised Cartel Act, including with the intention to modernise merger control (introduction of the SIEC test) and to strengthen the civil antitrust law.

State involvement in the economy, according to the PMR indicators, is among the highest in OECD, particularly in network sectors (telecommunications and energy) (Figure 1.18), distorting competition. Services typically provided by private companies in many OECD countries such as distribution of mail and packages, banks and financial services, transport and media, are largely provided by companies belonging to the Swiss Confederation, cantons or municipalities. The most notable examples are a major telecommunications provider (Swisscom, 51% owned by the state), the majority of cantonal banks, as well as energy producing or providing companies (Adler, 2017).

When state-owned enterprises (SOEs) are present in competitive markets, their special position can give them unfair advantages. For instance, implicit government guarantees can result in easier access to funding. Also, monopoly rents from regulated activities can be used to cross-subsidise the competitive part of business operations, giving SOEs room for more aggressive market tactics (OECD, 2015a). Furthermore, bailing out SOEs can be costly, as was experienced by several cantons during the 1990s real estate crisis, when a number of cantonal banks had to be rescued (Jäggi, 2018).

Equal treatment in regulatory matters has largely been achieved for SOEs of the Swiss Confederation. Systematic cross-subsidisation between monopoly services and competitive activities is prohibited and public enterprises with a dominant position need to allow non-discriminatory access to network infrastructure (Federal Council, 2017; Jäggi, 2018). Switzerland has also taken on board a number of OECD guidelines on corporate governance of SOEs (OECD, 2015b) and it now ensures that SOEs are managed based on strategic objectives and transparent corporate governance (OECD, 2020a). A recent review (Lienhard et al., 2019) concluded that the system functions well, but recommended further improvements, mostly on transparency. Ensuring regulatory and competitive neutrality however is an ongoing task, as markets and technology are constantly evolving. Regulatory agencies and competition

authorities should be empowered enough to enforce safeguards against market distortions and ensure the full and impartial implementation of all relevant laws and regulation. In addition, the possibility for private action against such distortions of competition could further deter abuse of advantageous position.

The situation with the SOEs at the cantonal level is less clear, in contrast with good progress at the federal level. Even the scope of SOEs at the cantonal level is not straightforward to determine. A report by the Federal Council (2017) finds that for many cantonal SOEs, the separation of ownership, management, regulatory and market watchdog function is not guaranteed. Several cantonal SOEs have politicians sitting on supervisory boards and there are others directly controlled by the executive. Moreover, some regulations, notably in the hospital sector, favour public enterprises and cross-subsidisation cannot be ruled out. Bringing the standards of corporate governance, transparency and regulatory and competitive neutrality for cantonal SOEs to the same level as for federal SOEs would further improve competition and reduce risks from implicit public guarantees.

### *Maintaining international openness to harness competitive pressures*

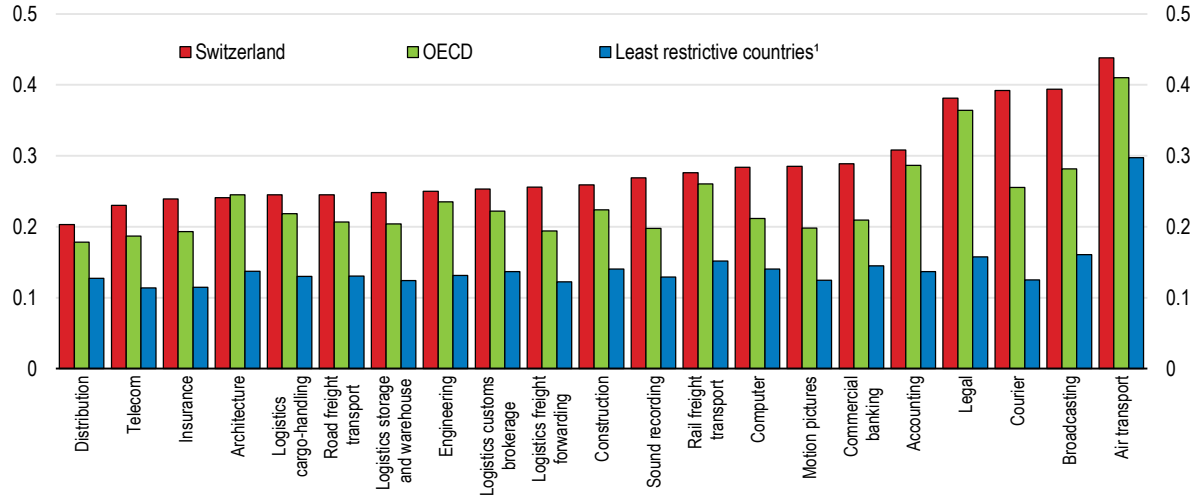
International openness and exposure to foreign competition are essential for productivity growth and innovation activity. For economies with a relatively small domestic market, such as Switzerland, international openness lets the export sector achieve economies of scale while import competition strengthens competition in the domestic market. Evidence (SECO, 2019) shows that the level of sectoral productivity is highly associated with the rate of exports in a given sector, in particular in the manufacturing industries. Productivity growth in domestically-oriented sectors has been weak or even negative, unlike that in export sectors exposed to international competition. It is therefore crucial that Switzerland remains an open economy.

Notably, Switzerland should ensure continued trade and economic partnership with the EU. This will maintain its access and exposure to its most important trading partner. As of now, the bilateral relationship between Switzerland and the EU is governed by a collection of treaties that have been signed over the years. However, some of them may become outdated in the coming years and the EU has shown reluctance to update them individually. In 2014, negotiations began on the Institutional framework agreement with the EU that aimed to provide a unified legal foundation for the future, but in May 2021 the Federal Council officially ended the negotiations without an agreement. Failing to find an adequate alternative raises risks and uncertainties related to the erosion of the Switzerland-EU partnership that could be harmful for Switzerland's external trade and competition.

There is also room to reduce further barriers to trade and to foreign direct investment. In September 2021, Switzerland unilaterally eliminated import tariffs on all industrial products. In contrast, barriers to trade in services – as indicated by the OECD Services Trade Restrictiveness Index – remain higher than the OECD average (Figure 1.19) and should be lowered to spur competitive pressures. Despite some progress on trade liberalisation efforts, restrictions on movement of people remain for independent services suppliers. Relatively high restrictiveness also stems from economy-wide regulatory burdens, as described above, due to relatively cumbersome procedures to register a company and acquire land and the prominent role of the state in the economy. Room for improvement is highest in courier services, broadcasting, motion pictures and sound recording, where relative restrictiveness is the highest (OECD, 2020c).

## Figure 1.19. Barriers to trade in services are higher than in most other OECD countries

Services trade restrictiveness index (STRI), from 0 to 1 (most restrictive), 2020




1. "Least restrictive countries" is the average of the 5 countries with the lowest score in each category.
Source: OECD STRI Regulatory database.

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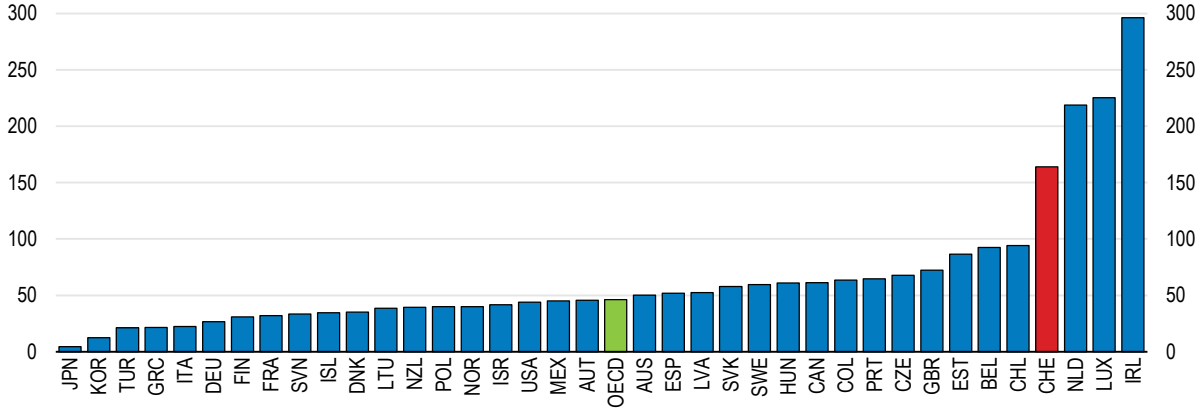
According to the OECD FDI Regulatory Restrictiveness Index, Switzerland also imposes some constraints on inward foreign direct investments (FDI), mainly through equity restrictions. Reducing the regulatory burden on FDI has a positive impact on technology transfer, knowledge spillover and eventually on productivity growth. Indeed, Switzerland has benefited substantially from such spillovers as the stock of inward FDI as a share of GDP is one of the highest in the OECD (Figure 1.20). High barriers to foreign investment are present in a few protected sectors, notably electricity, broadcasting and real estate, while barriers in other sectors are mostly below the OECD average. In 2020, under the initiative “Protection of the Swiss economy through investment controls" the Swiss Parliament tasked the government to draw up a legal framework for controlling foreign investments. The stated objective is to have a targeted, effective and administratively lean investment control system, but the purpose and scope of this measure are not yet clear. Unwarranted barriers to FDI can be damaging for investment and productivity growth.

## Figure 1.20. Switzerland has benefited from high inward FDI

Foreign Direct Investment, inward position, % of GDP, 2019




Source: OECD International Direct Investment Statistics database.

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Agriculture is still heavily shielded from foreign competition by high import tariffs and other trade barriers. Swiss agriculture also receives high direct support payments, resulting in the total support to agriculture at 150% of sectoral value added, the highest in the OECD (OECD, 2020b). As a result, labour productivity of Swiss agriculture is 50% below the OECD average (Figure 1.14). As recommended in the past (OECD, 2017a, 2019a and 2020b), lower trade barriers and less direct support would raise productivity in agriculture and could also enhance its environmental sustainability (see below).

### Table 1.6. Past recommendations on lowering barriers to competition

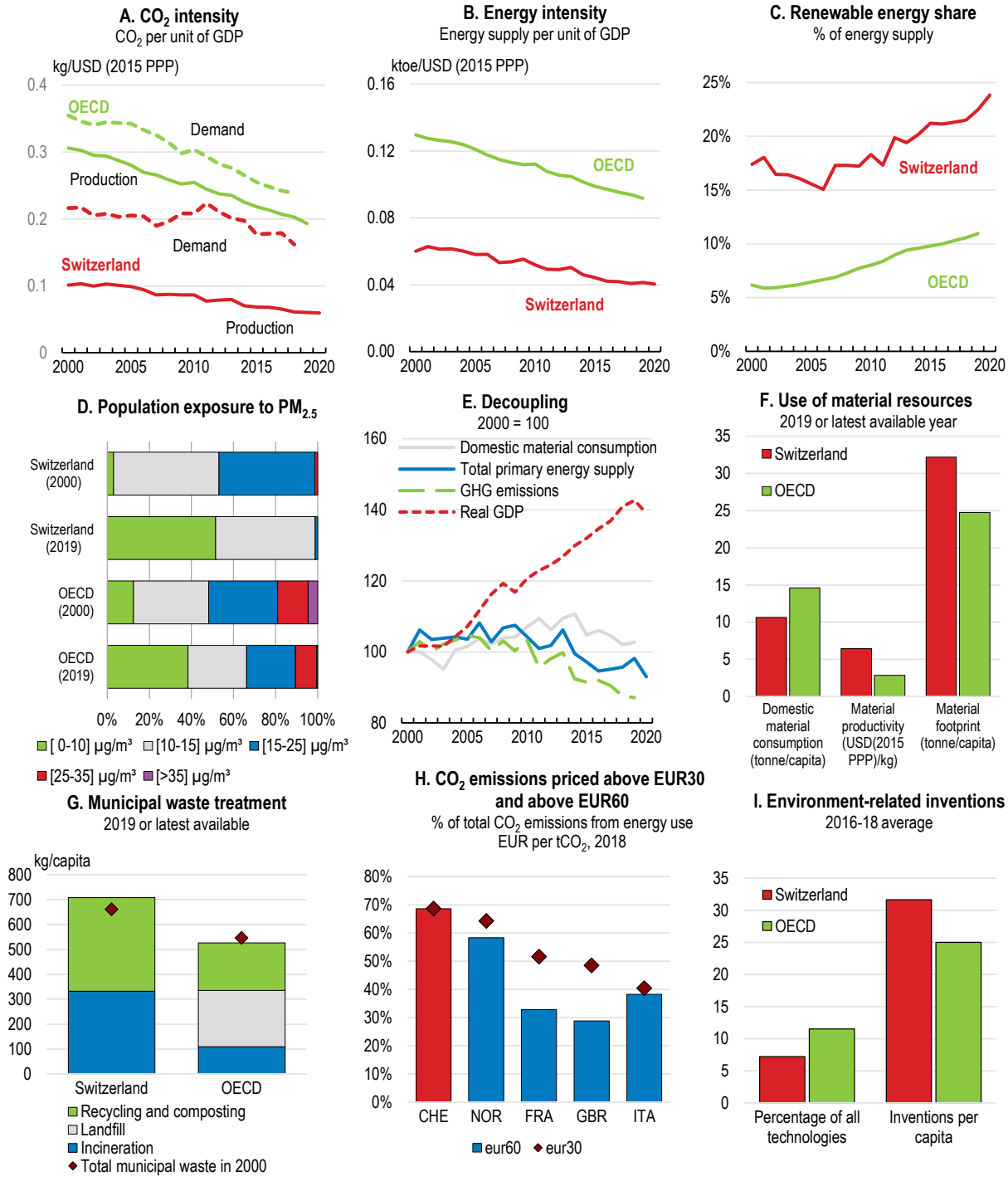
| Recommendations in previous Surveys | Action taken |
|---|---|
| Lower restrictions on trade in both goods and services, notably in highly protected agricultural products. | Regarding industrial goods, the Federal Council has sent a draft law on the unilateral abolition of all import tariffs on industrial goods to parliament. In October 2021, both chambers passed the law in principle.<br>On 1 May 2019, the Federal Council decided to renew a temporary suspension of customs duties on textile input and intermediary materials from 1 January 2016 and extend its scope. It is expected to stay in force until 31 December 2023, and now covers 522 tariff numbers and is set to reduce import duties by around CHF 3 million per year.<br>By engaging in negotiations on free trade agreements, Switzerland is contributing in lowering restrictions also on trade in agricultural products. On 1 November 2020, the EFTA-Ecuador CEPA entered into force. New agricultural concessions will enter into force on 1 August 2021 pursuant to an updated EFTA-Israel FTA and a new Agreement on Agricultural Products between Israel and Switzerland. For the new EFTA-Indonesia CEPA, as for the updated EFTA-Turkey FTA and new Switzerland-Turkey Agreement on Agricultural Products, the ratification procedures are currently ongoing and entry into force is pending. The agreements entered into force on November 1st and October 1st 2021, respectively.<br>The amendments to the Swiss Federal Law on Processed Agricultural Products, abolishing export contributions for processed agricultural products in accordance with the relevant decision at WTO's 10th Ministerial Conference from 2015, have entered into force on 1 January 2019. |
| Reduce public ownership and remove barriers to entry, including restrictions on the number of competitors, in energy, telecommunications and transport.<br>Remove remaining explicit cantonal government guarantees to their public banks. | The Federal Council is preparing a revision of the Electricity Supply and the Energy Act, including the complete liberalisation of the electricity market. Parliamentary debate is set to start in autumn 2021.<br>No Action taken. |
| Modernise merger controls and strengthen sector regulators' powers. | The Federal Council is preparing a revision of the Cartel Act, including a modernization of merger control (introduction of the SIEC test). |
| Remove representatives of economic associations from the board of the competition authority. | No action taken. |

## Ensuring effective use of resources to raise living standards of all and make growth more sustainable

### *Environmental performance is good but consumption patterns and resource use still result in environmental pressures*

Switzerland is one of the top OECD performers in terms of greenhouse gas (GHG) emissions per unit of GDP, energy supply per unit of GDP (Figure 1.21), and GDP per unit of domestic material consumption. Over the past two decades, Switzerland has achieved the goal of decoupling economic growth from domestic GHG emissions, energy use (Figure 1.21) and from all major air pollutants. The economy's low carbon intensity stems from high shares of renewable energy resources, nuclear energy in the energy mix (to be gradually phased out) and an economy dominated by services (OECD, 2017b, 2020d). Fossil fuels account for less than half of total primary energy supply, well below the OECD share of 79% (IEA, World energy balances 2020).

## Figure 1.21. Switzerland has decoupled economic growth from domestic greenhouse gas emissions and material use but environmental pressures remain




Source: OECD (2020), Green Growth Indicators, OECD Environment Statistics (database); OECD National Accounts (database); IEA (2020), IEA World Energy Statistics and Balances (database); OECD (2020), Exposure to air pollution, OECD Environment Statistics (database); OECD (2021), Effective Carbon Rates 2021; Municipal waste, OECD Environment Statistics (database); OECD (2020), Environmental policy: Environmental policy instruments, OECD Environment Statistics (database); OECD (2020), Greenhouse gas emissions, OECD Environment Statistics (database); Material Resources, OECD Environment Statistics (database).

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Nevertheless, environmental pressures are significant, due to the high standard of living and correspondingly high consumption and resource use. Compared to production based indicators, demand-(consumption-) based indicators point to higher environmental pressures (Figure 1.21) and slower progress in tackling environmental challenges. Furthermore, as an Alpine country, Switzerland is impacted by climate change more strongly than other countries. For instance, annual mean temperatures have risen by about 2 °C since monitoring began in 1864, twice as much as the global mean (Federal Council, 2018). The snowline is expected to rise, while winter snow reserves and glacier volumes will decline further with implications for tourism, water management and agriculture.

The negative environmental effects of Swiss consumption largely occur abroad. According to footprint indicators, in areas such as biodiversity and water consumption, the Swiss footprint is actually worsening, despite progress domestically (Federal council, 2018). A relative lack of domestic raw materials and energy resources necessitate high imports. Domestic material consumption per capita is well below the OECD average, but material footprint per capita that includes materials used in the production of imported products, is above the OECD average (Figure 1.21). It is estimated that between half and three-quarters of the Swiss environmental impact is embodied in the import of goods and services, in particular in relation to food consumption, housing and mobility (Frischknecht et al., 2014, OECD, 2017b). The latest OECD Environmental Performance Review of Switzerland (OECD, 2017b), recommended to promote more sustainable patterns of consumption to further improve Switzerland's resource efficiency in the context of global value chains, as also envisioned by the 2030 Sustainable Development Strategy (Federal Council, 2021c). In addition, Switzerland should better align its trade and environmental policies, including requiring an environmental impact assessment of new trade agreements. For instance, the Swiss administration already conducted the environmental impact assessment of the EFTA-MERCOSUR Free Trade Agreement. Environmental impact assessments are now quite common practice in the US, Canada and the EU (Moise and Rubinova, 2021).

Switzerland's consumption patterns are reflected in high municipal waste. At 705 kg per capita (in 2018) it is among the highest in the OECD and remains higher than 15 years ago, contrary to a number of OECD members, such as the UK, Spain and the Netherlands, that managed to reduce it significantly. Switzerland sends no household waste to landfill and recycles most of it (Figure 1.21), but municipal waste generation has not been decoupled from private final consumption, despite waste disposal fees and other policy instruments. There is considerable room for reducing residual municipal waste and biodegradable municipal waste (OECD, 2017b). A federal waste prevention strategy could help reduce municipal waste and decouple waste generation from rises in consumption.

The Federal Council set the net-zero greenhouse emissions target by 2050 and adopted an ambitious "Long-Term Climate Strategy for Switzerland". The strategy set out climate policy guidelines and established strategic targets for key sectors. In addition, within the Paris agreement, Switzerland has committed to reducing greenhouse gas emissions by 50% by 2030 (compared to 1990). Policy to achieve the 2030 target has been built on the measures and targets of a revised CO2 Act. The latter was passed in parliament in 2020, but was rejected by a popular vote in June 2021. The Federal Office for the Environment estimates that in 2020 the target 20% reduction in greenhouse gas emissions with respect to 1990 was not met (FOEN, 2021). Stronger measures are therefore needed in order not to miss the next set of targets.

Switzerland prices its CO2 emissions at high rates (Figure 1.21) and among OECD countries, it gets closest in aligning its pricing of CO2 emissions to international climate cost benchmarks (OECD, 2018a, 2019b and 2021c). The share of CO2 emissions priced above EUR 60, a midpoint estimate of the carbon cost in 2020, has been on the rise, notably in the housing sector (OECD, 2021c and 2019a). Moreover, the failure to reach the reduction target triggers a rise in the carbon tax from CHF 96 to CHF 120 per tonne of emissions in 2022. Road transport fuels are exempt from the carbon tax, but face high effective rates from fuel taxes and ever stricter CO2 emission target values for new passenger cars and new light commercial vehicles. Since January 2020, Switzerland's emissions trading scheme has been linked to the

EU's Emissions Trading System (ETS), and the emission allocation price has since jumped closer to the EU levels (Hintermann and Zarkovic, 2020). Plans to further raise the carbon tax and introduce a levy on the purchase of air tickets have recently been halted (with the rejection of revised CO2 Act by a popular vote). Going forward, Switzerland should continue its efforts to effectively reduce GHG emissions.

Exemptions to the carbon tax reduce its effectiveness. GHG-intensive companies (not under the ETS) can be exempted from the tax – on competitiveness grounds - if they commit to uninterrupted emission reductions. Still, the previous OECD Environmental Performance Review (OECD, 2017b) assessed that eligibility criteria were lax, as applicants proposed targets themselves based on "economically viable reduction potential". In addition, until 2021, companies that significantly over-performed the agreed targets were eligible to certificates that they could sell to a government fund (subsidies, effectively). The amount of the foregone carbon tax, the "subsidies" and monitoring by the Federal Office for the Environment make this a costly programme and it is questionable whether the benefits outweigh the costs. Evidence shows that emission reduction by companies exempt from the carbon tax have not been larger than of firms paying the carbon tax or being part of the ETS (Hintermann and Zarkovic, 2020). A thorough assessment of the scheme (Swiss Federal Office of Energy, 2016) showed that it did not contribute to significant emission reductions in large companies compared to already planned reductions, while it contributed somehow in small companies. This demonstrates the need to adjust the mechanism in order to help reduce emissions more effectively without introducing a heavy administrative burden. From a climate policy perspective, exemptions to the carbon tax should be gradually scrapped over time as the CO2 levies rise internationally.

Reassessing and eventually removing various environmentally harmful subsidies and exemptions would result in a more coherent pricing and incentive system across sectors and provide a clearer market signal as to the societal costs of different activities. Subsidies and tax exemptions have historically benefited particular sectors such as agriculture, forestry and public transport (OECD, 2017b) and removing them has proved politically difficult. Agriculture policy support, in particular, remains one of the highest in the OECD, and aligning agriculture policy objectives with environmental ones has been slow. As recommended by the OECD Environmental Performance Review of Switzerland (OECD, 2017b) agriculture policy support should be explicitly put at the service of achieving agri-environmental objectives, including by removing remaining sector-specific fossil fuel-related tax exemptions and reductions, e.g. on oil use and on methane emissions.

### *Boosting green investment and eco-innovation*

Switzerland should continue to leverage its internationally competitive financial and corporate sectors, and high saving rate to boost green investment and foster eco-innovation. Taking further steps to promote mainstreaming of environmental and climate-related considerations into business and investment decisions as well as to mobilise private participation in green investment could yield significant environmental benefits domestically and internationally. It could also help revive economic growth.

A voluntary climate compatibility test on a large and representative sample of the Swiss financial sector showed that in 2020, the sector's large investment portfolio was not compatible with Switzerland's climate goals and the aim to become a leading centre for sustainable finance. Using an internationally comparable methodology, the Federal Office for the Environment (FOEN) and the State Secretariat for International Financial Affairs (SIF) conducted climate compatibility tests on 179 financial institutions, including banks, pension funds and asset managers. The results showed that the sector was still heavily invested in oil and coal extraction, and much less in renewable energy or electro-mobility (Spuler et al., 2020). Moreover, while many institutions adopted climate-related investment strategies, implementation was lacking. However, progress had been made and data show that sustainable investment is rising steeply in Switzerland (Swiss Sustainable Finance, 2020). Comparison with a similar climate compatibility testing done in 2017 showed that higher transparency and awareness proved valuable for the institutions involved and many adopted effective climate-related initiatives following the first testing round.

Investment portfolios and corporations are also exposed to climate-related risks that arise from the transition to a sustainable low-carbon economy and from increased frequency and severity of climate-related natural catastrophes. Information on climate-related risks is crucial for ensuring that investors and policy makers understand the exposures. The authorities are preparing the binding implementation of the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) by large Swiss companies in all sectors of the economy. This will introduce an obligation by companies to indicate how they deal with climate risks in the areas of governance, strategy and risk management, as well as show the indicators and targets they use. From July 2021 onwards, FINMA requires large banks and insurance companies to do so. The Federal Council recommends to financial institutions to publish their methods and strategies for taking account of climate and environmental risks in performing their asset management roles. The Federal Council has also tasked the Federal Department of Finance to prepare a proposal by summer 2022, whereby big companies, banks and insurers will be obliged to report on the climate risks and climate impact of their operations. Strengthening the disclosure of climate-related risks should be stepped up, as has been done in other OECD countries.

More ambitious support for green technology and green R&D could yield benefits in terms of the environment as well as economic growth. Switzerland ranks low among OECD countries in the share of environment-related activities in its overall direct government support for research and development (R&D). However, the total expenditures that would include indirect funding via research and innovation programmes of publicly-funded agencies (e.g. the Swiss National Science Foundation and Innosuisse), and the expenditures of research and innovation institutions linked to Swiss universities, are much higher. While the share of environment-related patents is low, in per capita terms the number of environment-related patents is above the OECD average as innovation activity is high overall. It is estimated that energy-related private R&D spending is about four times the size of public spending (IEA, 2015) going mainly to pilot and demonstration projects on energy efficiency.

The revised CO2 Act set the framework for a climate fund with boosted public resources to support environmental technologies. The climate fund aimed to incorporate already existing energy-efficiency buildings programme and the technology fund that provides loan guarantees to companies that develop innovative green products and processes. With planned increased revenues from revised CO2 tax, new aviation levies and other revenues (auctioned emission allowances and sanctions) there was an expected 50% increase in funds for the buildings programme, and more than a doubling of funds for green technology and innovation. With the rejection of the revised CO2 Act, plans in this form have been halted, but efforts to support investment to boost energy efficiency and increase public funds for environmentally-related R&D should continue.

### *Addressing challenges from population ageing*

A substantial pension reform is long overdue, as already argued in the previous OECD Economic Survey, which had an in-depth chapter on population ageing (OECD, 2019a). The statutory retirement age has remained at 65 years for men since its introduction in 1948 despite dramatically changed demographics and bleaker future growth prospects. In addition, Switzerland is among the four remaining OECD members that have not yet equalised the male and female statutory retirement age, which remains at 64 for women. In December 2021, the parliament passed a reform of the first pillar of the pension system, envisaging the statutory age of retirement for women at 65, but the law will likely be challenged at a referendum.

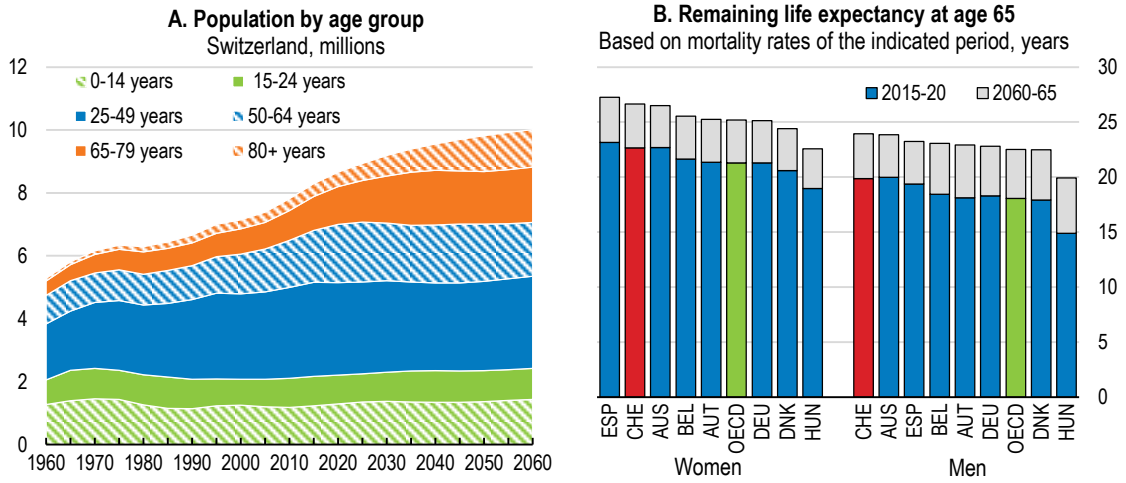
Most workers retire around age 65 and the time in retirement is increasing (Figure 1.22). Remaining life expectancy at age 65 is now close to 23 years for women and 20 years for men, and it is projected to increase by another four years by 2060-65 (Figure 1.22, OECD, 2019c). The number of people aged 80 or over will more than double by 2045. With current policies, the ratio of retirees to employees is set to soar.

Changed demographics can adversely affect growth, productivity and the labour market, where a range of disincentives and barriers contribute to early retirement and low uptake of work by older workers. After the

age 65, the otherwise high employment rate shows a steep decline – to below the OECD average (Figure 1.23). The *Chapter 2* of this *Survey* reviews the labour market aspects of the ageing population.

Ageing also creates fiscal pressures, by lowering revenues and raising costs related to pensions, health-care and long-term care. A significant increase in revenues would be required to counter the rise in expenditures, given the constraints under the debt brake rule. The main driver of rising expenditures is the increase in the size of the older population. Long-term scenarios based on Guillemette and Turner (2018, 2021) show that the ratio of revenue to GDP would need to rise by around 3 percentage points by 2060 to hold the debt-to-GDP ratio steady (Figure 1.24), assuming real spending per capita on non-ageing-related services is maintained. Pension reform can offset a significant part of the increase. Another option would be to crowd out other spending programmes with potentially adverse effects on productivity and equity.

## Figure 1.22. Population is ageing rapidly




Note: In Panel A, youth are shown in green, 25-64 year-olds in blue and seniors in orange. After 2020 data are from the "medium variant" of UN scenarios.
Source: United Nations (2019), World Population Prospects: The 2019 Revision, Online Edition.

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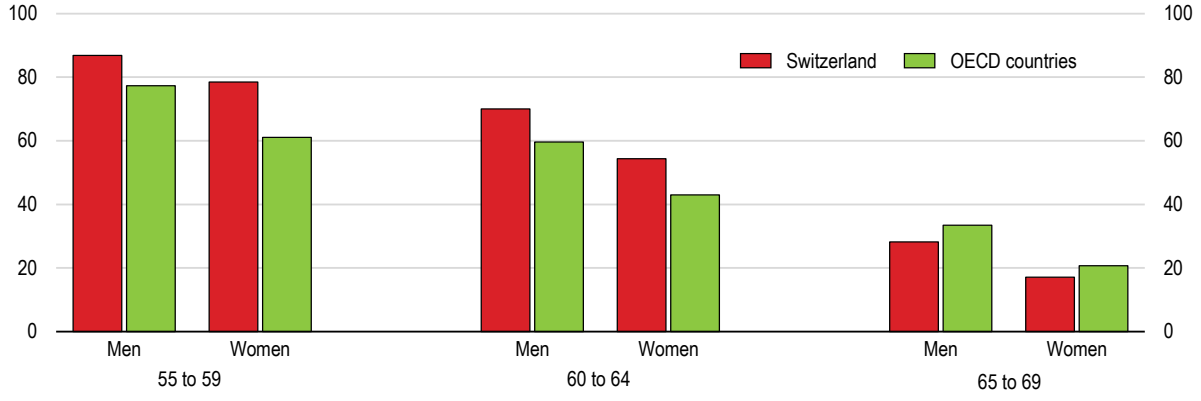
## Figure 1.23. Employment rates fall steeply after 65

Employment rate, % of respective population, 2020




Source: OECD Employment and Labour Market Statistics database.

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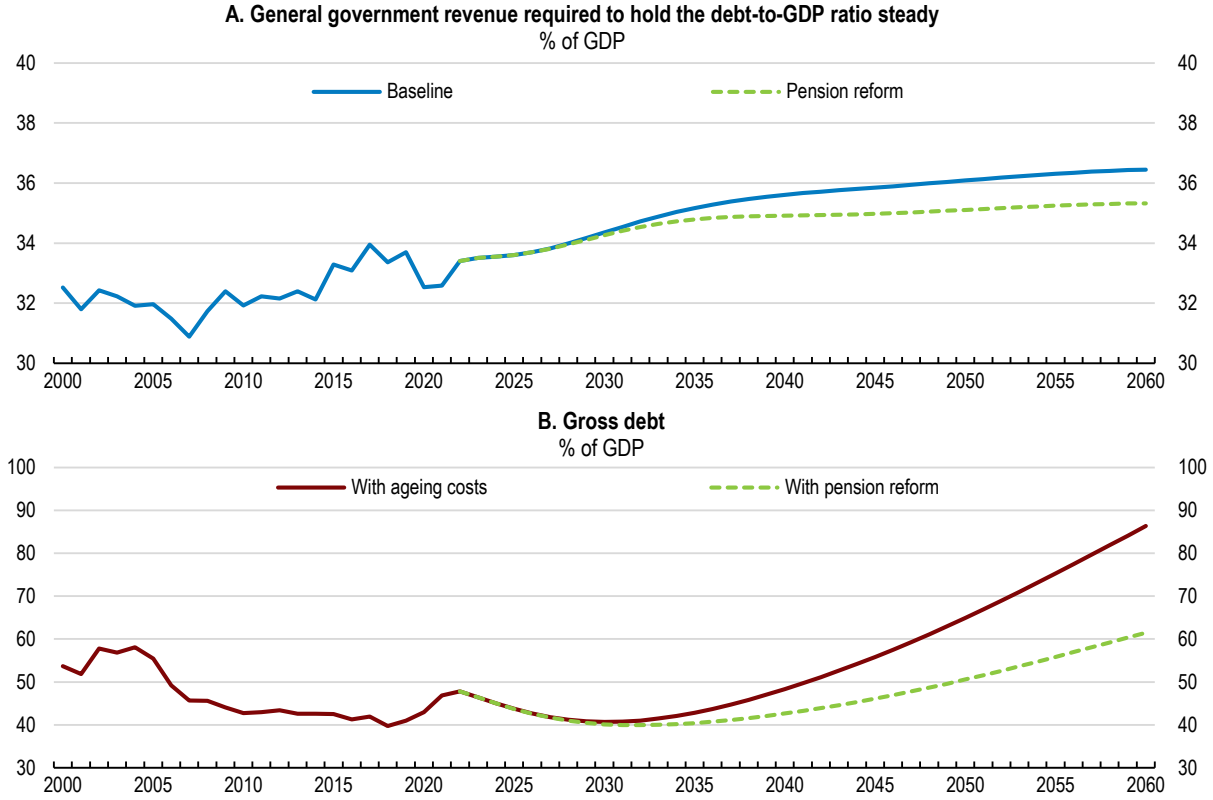
## Figure 1.24. Ageing creates fiscal pressures



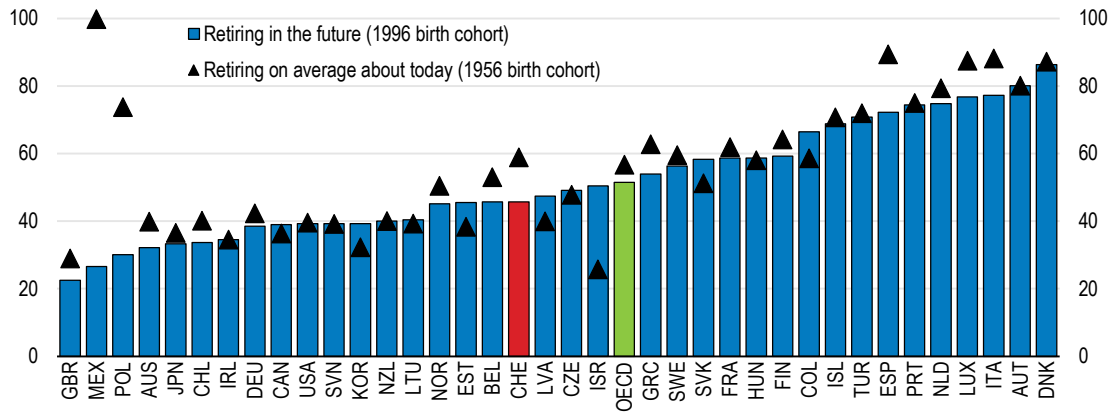

Note: The projections are illustrative and differ from national projections (FDF, 2021). The OECD Long-term model considers demographics but also the Baumol effect – i.e. the tendency for the relative price of services to increase over time. It is also assumed that other primary expenditures (other than health and pensions) are affected by ageing. The assumption is that governments would seek to provide a constant level of services in real per capita terms. This translates into higher fiscal pressure when the employment / population ratio falls. This component adds about 2 pp of GDP by 2060 (see Box 1.1 and Figure 1.13 in Guillemette and Turner, 2021). In addition, the scenarios assume that public pensions will grow at ½ the pace of wages, in line with the current Swiss law. Panel A shows the required increase in public revenues to keep debt-to-GDP ratio steady amid rising costs due to ageing. Panel B assumes that rising ageing costs are financed with deficits (applied on a zero primary balance scenario). In both cases, pension reform entails the following: first equalising retirement age for men and women at 65, then retirement age gradually rises to 67 in 2034, and by half of the expected gain in life expectancy thereafter (to reach 68 in 2058).
Source: OECD calculations.

StatLink https://stat.link/fb4xo0

Pension replacement rates from the mandatory pension system (the first pillar and the mandatory part of the second pillar) are set to drop significantly for average earners (Figure 1.25), from currently high levels. Furthermore, as already discussed in the last Survey (OECD, 2019a), the first pillar's funding faces serious pressures. The compensation fund managing first pillar assets and liabilities has run a deficit (excluding investment returns) since 2014 (Federal Social Insurance Office, 2020).

## Figure 1.25. The replacement rate from mandatory pension schemes is expected to fall

Gross replacement rate for mandatory schemes, %




Note: Full-career average earners retiring at the normal retirement age of the respective cohort, men.
Source: OECD (2019), "Will future pensioners work for longer and retire on less?", Policy Brief on Pensions, OECD Publishing, Paris. www.oecd.org/els/public-pensions/OECD-Policy-Brief-Future-Pensioners-2019.pdf

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Reforms have proven difficult and many such efforts were rejected by referendum in the past. A recent reform, effective from 2020, will raise social security contributions by 0.3 percentage points, earmark an additional 0.2 percentage points of VAT revenues to the first pillar, and raise federal government's contribution from 19.6% to 20.2% of total expenses. The reform boosts revenues, delaying the time when the compensation fund will go into negative equity by four years (to 2034) (Federal Social Insurance Office, 2019). However, it does not tackle the problem sustainably. Raising the statutory retirement age and linking it to increases in life expectancy, as well as improving incentives to work beyond that age are key reforms that would raise revenues, ease spending pressures and help sustain growth. This would also help increase replacement rates in the second pillar. Other OECD countries such as Denmark and the Netherlands for example, have already instituted reforms to lift the statutory retirement age and subsequently link it to life expectancy.

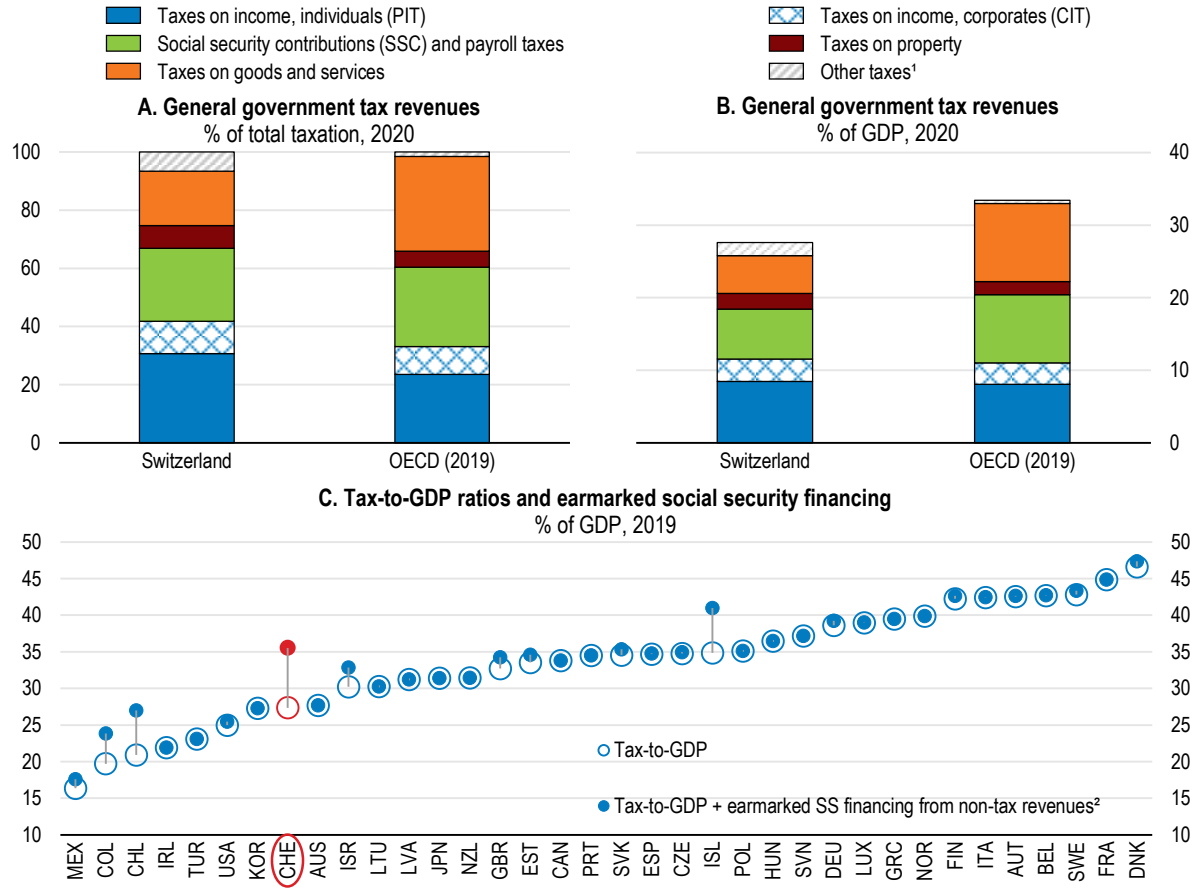
The mandatory part of the second pillar faces pressures from unsustainable minimum conversion rates that threaten sustainability and intergenerational fairness. It is a hybrid system (unlike a pure defined contribution system) and the rate at which accumulated capital is converted into an annual pension benefit is set by law. This rate has been unchanged since 2004 despite rising life expectancy and lower investment returns. At 6.8% it is well above an actuarially fair rate, which is estimated at 4.5-5%, depending on expected returns and retirement age (Helvetia, 2020). In response, pension funds have lowered returns accruing to current contributors, resulting in significant intergenerational transfers that are growing over time (Occupational Pension Supervisory Commission, 2019 and 2020). Moreover, many funds lowered effective conversion rates by lowering conversion rates from the extra-mandatory (voluntary) part of the second pillar. To lower liabilities, some funds encourage the insured to take a large part of their pension wealth as a lump sum upon retiring (OECD, 2019a). Some funds that rely mostly on the mandatory scheme even potentially face insolvency.

Based on the proposal by the social partners, the Federal council, in 2020, proposed a reform with the aim to reduce the conversion rate from 6.8% to 6%, together with some measures to cushion the transition and protect low-income workers from the resulting drop in pensions. Lowering the minimum conversion rate and making it a more flexible parameter (not set by law as it is now) is crucial to safeguard the sustainability of the second pillar. Lengthening the contribution period – lowering the starting age below 25 (currently set by law) and extending it beyond 65 - would help maintain adequate benefits while ensuring the sustainability of the pension system.

### *Making the tax mix more growth friendly*

A revenue neutral shift away from taxing personal income towards indirect taxes, including environmental taxes, could boost growth sustainably and reduce the exposure of government revenue to ageing. Switzerland's tax revenues as a share of GDP are relatively low (Figure 1.26). As discussed extensively in a special tax chapter in the 2011 Survey (OECD, 2012), Switzerland relies significantly more on direct taxation – personal income tax, corporate income tax and social security contributions paid to general government (as well as to private sector funds) - than most other OECD countries. Taxes on goods and services, on the other hand, are much lower (Figure 1.26). Such a tax mix is relatively more distortionary and harms growth, as taxing labour acts as a disincentive to work (Akgun, Cournède and Fournier, 2017; Arnold et al., 2011).

**Figure 1.26. Switzerland relies heavily on direct taxation**




1. Includes not allocable between personal and corporate income tax.
2. Earmarked financing of social security from non-tax revenues includes voluntary contributions to government and compulsory contributions to the private sector.
Source: OECD Revenue Statistics database.

StatLink https://stat.link/hrbjfw

The interplay between the tax and benefit systems results in disincentives to work, notably for second earners, contributing - together with high costs of childcare - to lower working hours and lower labour incomes for women. These issues are discussed in more detail in Chapter 2 of this Survey. There is room to reduce personal income tax, notably by reducing the burden on low-income households and second-earners, and flattening age-related progressivity in social security contributions.

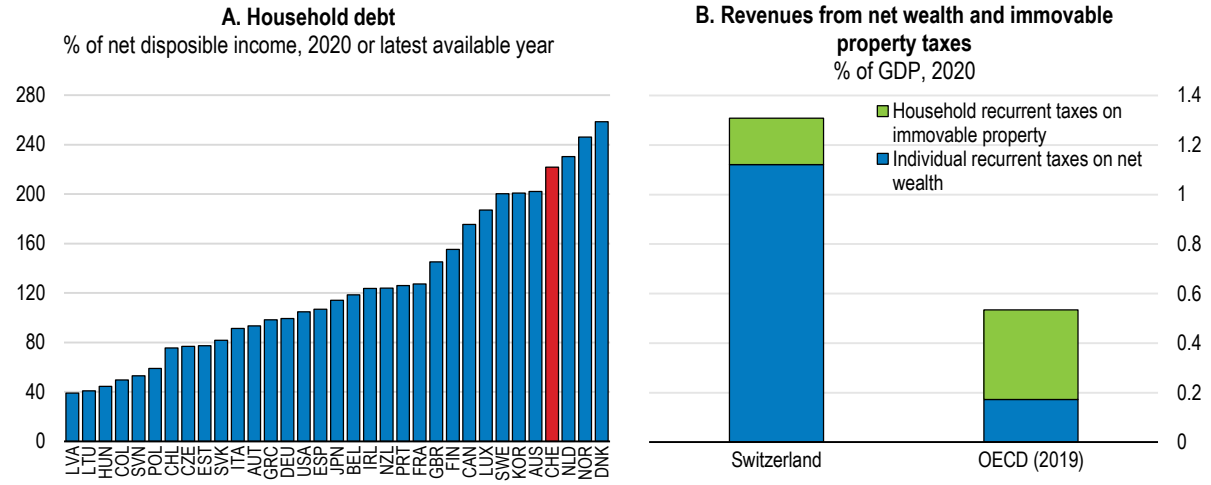
The personal income tax system also generates incentives for households to leverage their wealth. Interest paid on household debt is tax deductible with lax upper limits for deductibility. For instance, tax deductible

mortgage interest and maintenance expenses can exceed imputed rental income from housing. Moreover, a large part of capital gains realised by households is exempt from tax, further reinforcing incentives to leverage wealth. Swiss households have one of the highest indebtedness rates in the OECD (Figure 1.27) despite a low rate of home ownership. Limiting interest deductibility and broadening the capital gains tax base could strengthen equity - as it mostly benefits the wealthy - and help reduce the tax burden on labour or pay for the rising costs of the ageing population and climate change mitigation.

Switzerland raises high tax revenues from the net wealth tax (Figure 1.27), supported by a broad tax base and a relatively high share of wealthy individuals. Most cantons have abolished inheritance and gift taxes for transfers to direct descendants, but Switzerland's wealth taxes are levied on relatively lower levels of wealth (levied on part of the middle class) compared to other countries and can to some extent be viewed as replacing these other taxes. Switzerland could assess the merits of introducing a more broad based capital gains tax and inheritance and gift taxes that have been shown to be more efficient and have higher redistributive effects (OECD 2018b and 2021d). Moreover, net wealth taxes incentivise tax optimising behaviour and further increase incentives to borrow (and invest in assets such as owner-occupied houses or owner-managed businesses) as debt is deductible at face value from the net wealth tax base. A reform to improve the design of the net wealth tax could be considered to make it less regressive or more progressive, to limit debt deductibility and to improve coordination across cantons.

There is also room to increase revenues from the tax on immovable property, which is low in international comparison (Figure 1.27), although it is less distortive than most other taxes (Arnold et al., 2011). Raising taxes on immovable property at the local level can also make tax revenues of sub-national governments less prone to economic shocks and population ageing (Kim and Vammalle, 2012; Colin and Brys, 2019).

## Figure 1.27. The tax system contributes to high indebtedness of Swiss households, while reliance on taxing immovable property is low




Source: OECD National Accounts database; OECD Revenue Statistics database.

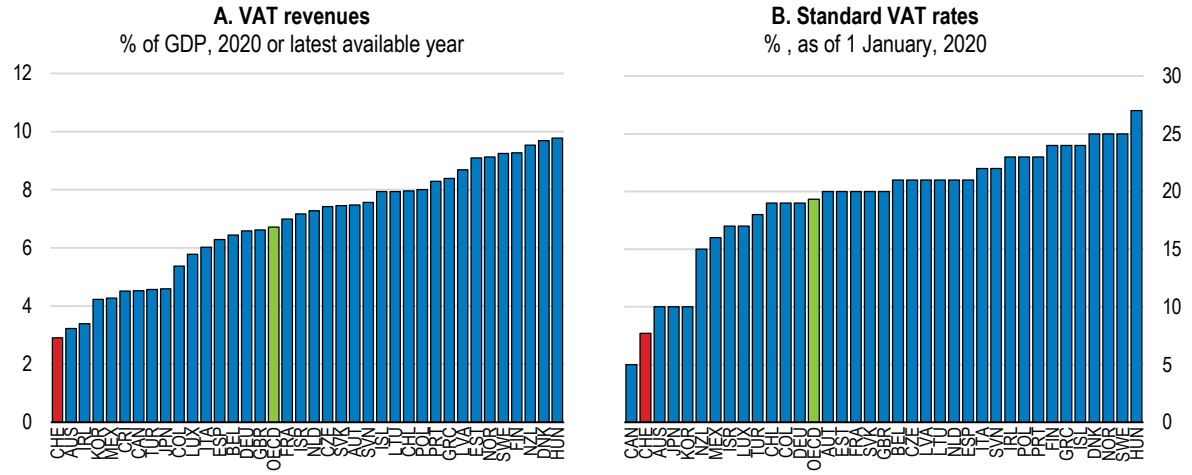
StatLink https://stat.link/5zoekx

There is room to raise the standard VAT rate and broaden the VAT base. Switzerland's standard VAT rate (at 7.7%) and VAT revenues in terms of GDP are among the lowest in the OECD (OECD, 2020e) (Figure 1.28). Reduced rates (2.5% and 3.7%) apply to a range of goods and services, such as accommodation services, food and drinks, agricultural supplies, water, printed materials, medicines and cultural and sporting events. According to the VAT Revenue Ratio indicator (OECD, 2020f) Switzerland loses a lower proportion (31%) of its potential VAT revenues than OECD countries on average (44%) due to exemptions, reduced rates, fraud and non-compliance. The use of reduced VAT rates could be further reduced nevertheless, in particular because the standard VAT rate is low. International evidence shows that reduced VAT rates are poorly targeted as they benefit richer households proportionally more (OECD,

2020e). Moreover, in cases such as pesticides and fertilisers they may encourage overconsumption with potentially harmful impact on the environment.

Broadening the base of the VAT and increasing the standard VAT rate – while reducing the personal income tax - would raise efficiency and be growth-enhancing, as recommended in previous Surveys (OECD 2012 and 2019a). Distributional concerns could be addressed through reductions in income taxes or targeted transfers for lower-income households.

## Figure 1.28. Switzerland's VAT rate and revenues are among the lowest in the OECD




Source: OECD Revenue Statistics database; OECD (2020), Consumption Tax Trends 2020: VAT/GST and Excise Rates, Trends and Policy Issues, OECD Publishing, Paris, https://doi.org/10.1787/152def2d-en

StatLink https://stat.link/fetkui

A recent corporate income tax reform, approved in the referendum and effective from January 2020, removed cantonal preferential tax regimes and introduced a new set of internationally accepted rules in line with the OECD/G20 BEPS project. The reform entailed the elimination of tax privileges for "status companies" (holding companies, mixed companies and auxiliary companies— also referred to as domiciliary companies) that previously paid a reduced (or null) corporate income tax at cantonal level (OECD, 2021e). The reform entailed the creation of patent boxes and the possibility for cantons to introduce additional deductions for R&D expenditures. Net profits from patents are to be taxed with a maximum reduction of 90% to be set at cantonal discretion. In addition, cantons may provide further incentives for R&D, whereby the enhanced R&D deduction at the cantonal level can reach a maximum of 50% (on top of the 100% baseline tax deduction) of the effective qualifying expenses. The value of eventual tax allowances will depend on the canton-specific corporate income tax rates that remain at the discretion of cantons.

Switzerland is expected to remain internationally competitive post-reform, with effective corporate income tax rates significantly below the OECD average. In response to the reform, cantons have lowered their corporate income tax rates, on average, by about 2-3 percentage points, and some will reduce them more in the coming years (Portmann and Staubli, 2020). In static terms, total tax revenues will fall (FDF, 2018). In the long term, however, the dynamic effects on the total tax revenues are likely to be positive (Daepp and Staubli, 2018) depending on behavioural responses from companies in terms of location, investment and hiring, and depending on the assumed international tax competition. In the short- to medium-term, the reform will therefore bring a revenue shortfall of up to 0.3% of GDP annually (Daepp and Staubli, 2018), putting some pressures on public finances (cantons will be partly compensated for potential revenue losses by higher revenue sharing of direct federal tax). Also, incentives for innovation based on income-based measures such as patent boxes reward existing patents rather than risky investment in R&D with uncertain benefits further in the future. In this, they tend to benefit large multinational companies, against small,

innovative start-ups that are more likely loss-making and credit-constrained (Appelt, et al., 2016). The reform is a step in the right direction nevertheless, as it eliminates unfair tax advantages for internationally active companies and introduces explicit incentives to R&D that did not exist before in Switzerland.

### *Fighting corruption and money laundering*

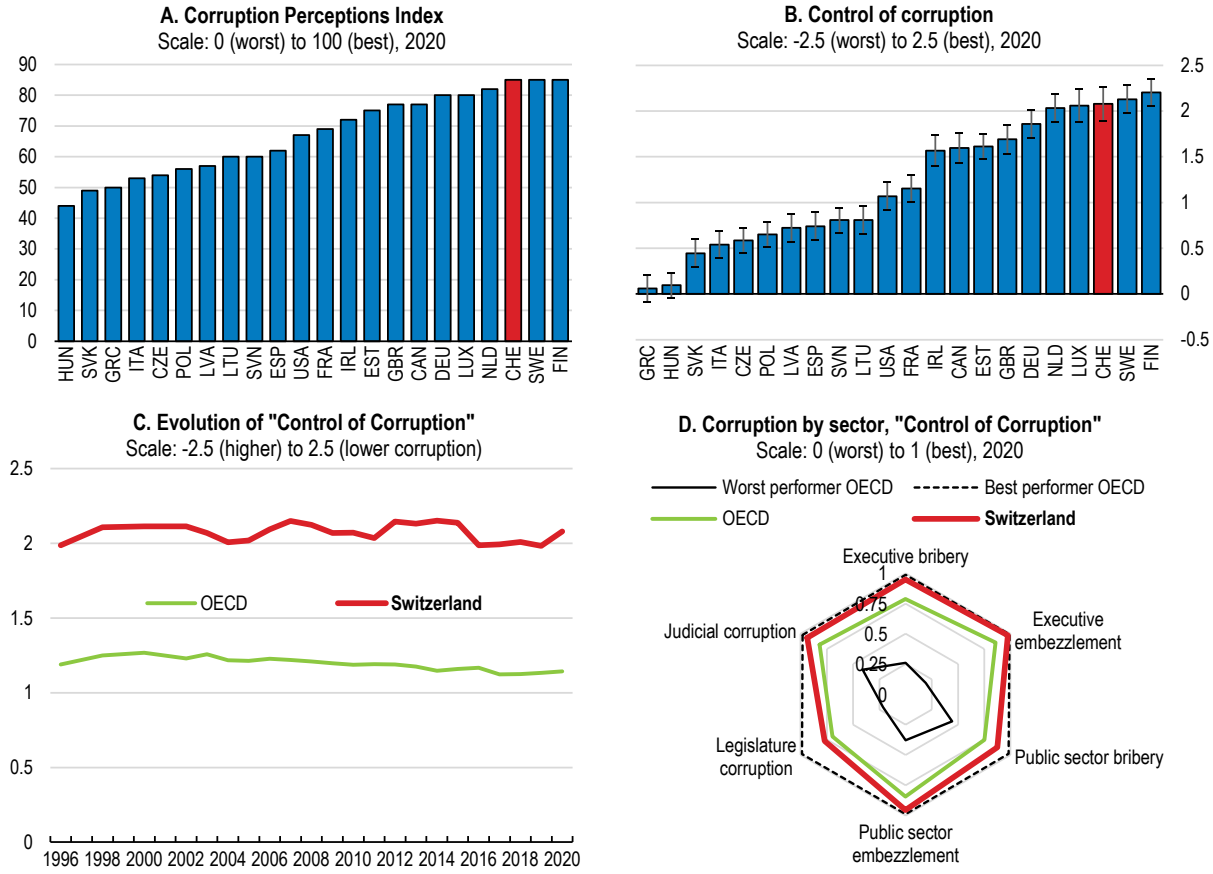
Indicators of control and perceived risks of corruption in the public sector suggest that Switzerland consistently scores among the best-performing OECD member countries (Figure 1.29). In its fourth evaluation round, the Council of Europe anti-corruption body, the Group of States against Corruption (GRECO) listed twelve recommendations to Switzerland to prevent corruption and improve public integrity in respect of members of parliament, judges and prosecutors (Council of Europe, 2017). Two years later, it found the level of compliance with recommendations satisfactory (Council of Europe, 2019). Notably, GRECO reported good progress concerning prosecutors and welcomed the commitment by the Federal Assembly to compile in a single document all rights and obligations of MPs. Good progress was reported also on the requirement to provide further details of professional activities in the declarations of interests for the members of parliament, but GRECO regretted that the recommendation on including quantitative data concerning MPs' financial and economic interests had not been complied with. There was also a lack of progress with respect to federal judges in improving the recruitment process in terms of quality and objectivity and in the development of the rules of conduct.

Recent efforts have been undertaken to strengthen Switzerland's approach to public integrity and corruption prevention across all branches of government through the Anti-Corruption Strategy 2021-24. Adopted by The Federal Council in November 2020, it includes high-level objectives to prevent and prosecute corruption, with the aim to maintain the reputation of Switzerland as the world renowned business centre with high integrity (Federal Council, 2020).

However, the prominent international position and high export orientation expose Switzerland to a relatively high risk of foreign bribery. Switzerland has one of the world's highest ratios of multinationals to inhabitants and these operate in sectors that are highly prone to foreign bribery including pharmaceuticals and trade in raw materials such as agricultural products, stone and metals, and energy products. Moreover, the international status of Switzerland's financial sector and focus on wealth management make the sector prone to greater risk of use for criminal purposes, particularly through money laundering, including the laundering of foreign bribery (OECD, 2018c).

These risks are acknowledged by the Swiss authorities and indicators show that Switzerland's anti-money laundering measures are quite effective in most aspects (Figure 1.30). According to the OECD Working Group on Bribery in International Business Transactions, Switzerland, through the continued action of the Office of the Attorney General, remains one of the most active countries in enforcing the foreign bribery offence (OECD, 2018c and 2020g). Switzerland has increased resources allocated to the Money Laundering Reporting Office (MROS), as was recommended previously.

## Figure 1.29. Switzerland performs well in control of corruption

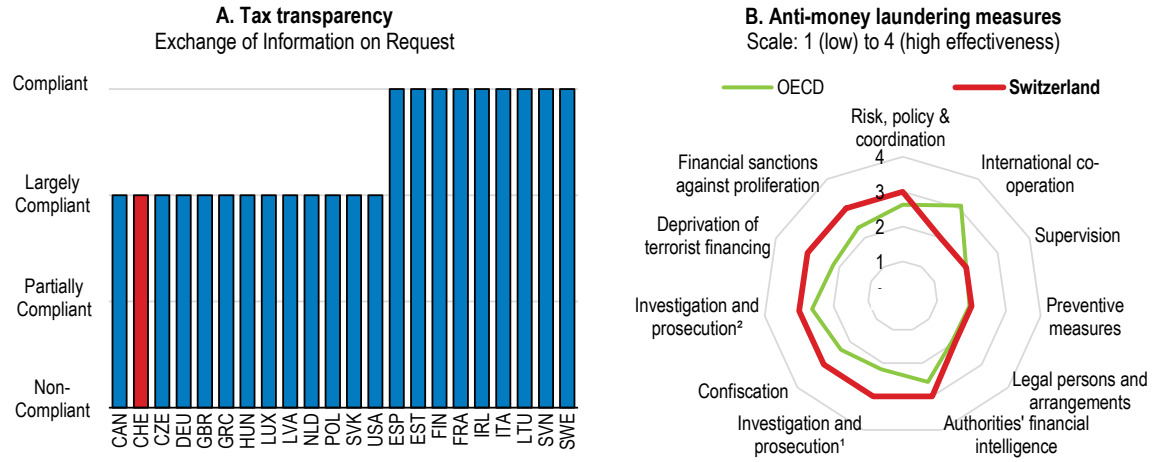



Note: Panel B shows the point estimate and the margin of error. Panel D shows sector-based subcomponents of the "Control of Corruption" indicator by the Varieties of Democracy Project.

Source: Panel A: Transparency International; Panels B & C: World Bank, Worldwide Governance Indicators; Panel D: Varieties of Democracy Project, V-Dem Dataset v11.

StatLink https://stat.link/wpsqzj

## Figure 1.30. Anti-money laundering measures are effective in most aspects




Note: Panel A summarises the overall assessment on the exchange of information in practice from peer reviews by the Global Forum on Transparency and Exchange of Information for Tax Purposes. Peer reviews assess member jurisdictions' ability to ensure the transparency of their legal entities and arrangements and to co-operate with other tax administrations in accordance with the internationally agreed standard. The figure shows first round results; a second round is ongoing. Panel B shows ratings from the FATF peer reviews of each member to assess levels of implementation of the FATF Recommendations. The ratings reflect the extent to which a country's measures are effective against 11 immediate outcomes. "Investigation and prosecution¹" refers to money laundering. "Investigation and prosecution²" refers to terrorist financing.
Source: OECD Secretariat's own calculation based on the materials from the Global Forum on Transparency and Exchange of Information for Tax Purposes; and OECD, Financial Action Task Force (FATF).

StatLink https://stat.link/yp8lzg

Nevertheless, the OECD Working Group on Bribery in its latest assessment from October 2020 (OECD, 2020g) urged Switzerland to address some weaknesses. Action is needed to ensure that sanctions imposed in foreign bribery cases are effective, proportionate and dissuasive. For instance, there are no legislative proposals providing for an increase in the statutory maximum fine for legal persons as was recommended by the OECD (OECD, 2020g and 2018c). Weak progress has also been noted in relation to whistleblower protection. Action should be taken to further strengthen existing protection for whistleblowers in the public sector at the federal level and broaden the legal framework for protection to cantonal officials. In the private sector, whistleblowers continue to expose themselves to criminal proceedings after reporting on corruption and foreign bribery. A bill designed to give protection to private-sector whistleblowers was rejected by parliament in March 2020. A parliamentary initiative on this subject is pending before Parliament but the outcome and timeframe remain uncertain (OECD, 2020g).

## Table 1.7. Past recommendations on ensuring sustainable and inclusive growth

| Recommendations in previous Surveys | Action taken |
|---|---|
| | |
| Strengthen the relationship between cantonal annual vehicle taxes and pollutants. | The responsibility for the vehicle taxes lies with the cantons. The first chamber of parliament has accepted a motion that asked for a stronger harmonisation of cantonal vehicle taxes. Various cantons promote battery electric vehicles and fuel cell vehicles through significantly lower motor vehicle taxes, and in some cases these vehicles are completely exempt. In addition, various cantons promote electric vehicles through purchase premiums and contributions to the charging infrastructure. |
| Limit the tax deductibility of mortgage interest so that, combined with maintenance outlays, it does not exceed the amount of declared imputed rent. | There is an ongoing parliamentary debate on a reform to abolish the taxation of the imputed rental value. According to its current version, as passed by the Council of States ("Ständerat"), it would be accompanied by a limitation of the deductibility of interest on private debt to 70% of taxable income from capital. |
| Increase financial incentives to work longer before retirement. | On 17 December 2021, the Parliament adopted a reform of the first pillar of the pension system (AHV 21 reform).<br>Ongoing reform of occupational pensions (second pillar): On 25 November 2020, the Federal Council sent a reform package to parliament. The reform proposal includes among other measures (e.g. reduction in the minimum conversion rate to 6.0%, compensatory measures) a reduction in the differences in contributions between younger and older insured persons. This aims at reducing wage costs for older workers. |
| Promote programmes to lengthen healthy working lives, including preventative health programmes. | No action taken. |

## Recommendations

| MAIN FINDINGS | RECOMMENDATIONS |
|---|---|
| **Supporting the economy to exit the crisis** | |
| The COVID-19 pandemic continues to raise uncertainty and challenges. Vaccination slowed markedly over the summer 2021. | Take appropriate measures to accelerate vaccinations. |
| Inflation is projected to remain low as the economy recovers, with substantial risks and uncertainty. | **Monetary policy should remain accommodative until the recovery is firmly underway.** |
| The Swiss financial system enjoys adequate capital and liquidity buffers. However, credit defaults and market corrections may materialise with delay. | **Consider reactivating the countercyclical capital buffer targeted at residential mortgages.**<br>**Progress further on managing the risks from "too-big-to-fail" banks, notably with strengthened liquidity requirements and resolution and emergency plans.** |
| The build-up of imbalances in the residential real estate market has continued, exposing debtors and creditors to interest rate and credit risks. | Consider a broader toolkit of macroprudential measures that would take account of affordability (e.g. debt-to-income and debt-service-to-income limits on mortgage loans).<br>Give the SNB and FINMA clear and strong mandates to propose and calibrate macroprudential tools. |
| **The deficit increased but gross general government debt remains low in international comparison and net debt is negative (positive net assets). Interest rates on issuing new debt remain at historically low levels.** | **Use the flexibility within the fiscal framework (the debt brake rule) to apply temporary adjustments and avoid a too rapid tightening in fiscal policy.** |
| **The crisis had differing impacts across sectors. A premature withdrawal of support could trigger unnecessary bankruptcies and labour shedding, and may result in scarring and poverty. A key challenge is to provide sufficient support for hard-hit firms and workers, while facilitating resource reallocation.** | **Continue to narrow policy support to hardest-hit sectors and vulnerable groups.** |
| Company distress could increase once support is withdrawn. The resulting rapid debt build-up could pose risks to financial stability while debt overhang in the corporate sector would adversely affect private investment and growth. On the other hand, too generous public support for too long risks keeping unviable firms artificially alive ("zombie" firms). | Continue providing liquidity to the hardest-hit firms in the short term if needed, while reducing the portion of the loan backed by the government guarantee or increasing the fee to access the programmes. |
| Effective insolvency procedures will be crucial to minimise the loss of resources and spur productivity-enhancing capital reallocation. Switzerland scores well on the strength of the insolvency framework but there is ample room for improvement in practice. | Enhance insolvency procedures by improving early access of debtors and creditors to cost-efficient and speedy insolvency proceedings and by ensuring adequate resources, including for recruiting and training staff. |
| **Boosting competition to raise productivity and growth** | |
| **Competition in the domestic market is still hampered by cantonal borders. The merger control framework remains too permissive and civil action against cartels is rare due to high complexity and short prescriptive periods.** | **Fully implement the Internal Market Act to ensure equal access to markets in all cantons.**<br>**Harmonise the merger control framework with that of the EU and strengthen the civil law on cartels.** |
| **The administrative burden on start-ups is higher than in top performers and resolving commercial disputes takes longer and is costlier than on average in the OECD.** | **Reduce the administrative burden on start-ups. Introduce "Silence is consent" licensing rules.**<br>**Expand the government one-stop shop (EasyGov.swiss) by integrating cantonal governments' services.** |
| State involvement in the economy is among the highest in OECD, particularly in network sectors (telecommunications and energy). SOEs in competitive market can benefit from unfair advantages, distorting competition. | Reduce public ownership and keep reducing the competitive distortions due to public ownership. |
| In many cantonal SOEs, the separation of ownership, management, regulatory and market watchdog function is not guaranteed. Some regulations favour public enterprises and cross-subsidisation cannot be ruled out. | Bring the standards of corporate governance, transparency and regulatory and competitive neutrality for cantonal SOEs to the same level as for federal SOEs. |
| **Barriers to trade in services are higher than in most other OECD countries. Switzerland also imposes some constraints on inward foreign direct investments (FDI) mainly through equity restrictions. Agriculture is heavily shielded from foreign competition and it receives high direct support payments.** | **Lower restrictions on trade in both goods and services, notably in agriculture. Remove the barriers to FDI where applicable and keep them low.** |
| **Ensuring effective use of resources to raise sustainability** | |
| **Municipal waste per capita is above the OECD average and has not decreased for the last 15 years, despite a number of policy instruments aimed at reduction.** | **Prepare a federal waste prevention strategy including indicative targets for municipal waste reduction.** |

| | |
|---|---|
| Environmentally harmful subsidies and tax exemptions remain in place that reduce the effectiveness of environmental policy instruments, notably in agriculture, forestry and public transport.<br>**The measures and targets of the proposed revised CO2 Act would have set important milestones on the way to reaching the net-zero greenhouse emissions target by 2050. However, plans to further raise the carbon tax and introduce an air-ticket levy have recently been halted (with the rejection of the revised CO2 Act by a popular vote). Exemptions to the carbon tax may reduce its effectiveness.** | Reassess and remove environmentally harmful subsidies and tax exemptions – including in agriculture - to make pricing and incentives more coherent across sectors.<br>**Continue efforts to broaden the base of the carbon tax by reassessing exemptions and align pricing of CO2 emissions with international climate cost benchmarks.** |
| **Switzerland could better leverage its internationally competitive financial and corporate sectors, and high saving rate to boost green investment and foster eco-innovation. The financial sector is still heavily invested in oil and coal extraction, and much less in renewable energy or electro-mobility.**<br>More ambitious support for green technology and green R&D could benefit the environment as well as economic growth. Plans to boost public support for energy-efficiency in buildings and green innovation further in the form of a climate fund have been halted. | **Continue increasing transparency in relation to climate compatibility of financial portfolios. Strengthen the disclosure of climate-related risks for large companies and the financial sector.**<br>Continue to promote investment to boost energy efficiency and increase public funds for environmentally-related R&D and green innovation. |
| **Population is ageing rapidly. First pillar funding faces serious pressures and pension replacement rates from the mandatory pension system are set to go down significantly.** | **Fix the retirement age at 65 for both genders and link it to life expectancy.** |
| In the second pillar, the rate at which accumulated assets are converted to a pension is set by law. The rate is too high, resulting in substantial redistribution within the second pillar from younger to older workers and retirees. Some pension funds may face insolvency. | Lower the parameter used to calculate annuities ("minimum conversion rate") and make it a more flexible technical parameter set by ordinance.<br>Lower the age to participate in occupational pensions (the second pillar). |
| Switzerland relies significantly more on direct taxation, notably personal income tax, than most other OECD countries. Switzerland's standard VAT revenues are among the lowest in the OECD. The revenue from the tax on immovable property is low. | Improve work incentives by reducing personal income taxes, notably for second-earners. Raise VAT and taxes on immovable property, while addressing adverse distributional impacts. |
| The personal income tax system and net wealth tax design generate incentives for households to leverage their wealth. Reliance on the net wealth tax is high, while a large part of capital gains is not taxed. | Limit mortgage interest deductibility in personal income tax and broaden the capital gains tax base.<br>Consider reforming the design of the net wealth tax to make it more progressive, limit debt deductibility and improve coordination across cantons. |
| Switzerland is highly export-oriented and serves as international business hub, including in high-risk sectors for foreign bribery, such as trade in raw materials, pharmaceuticals, and international asset management. In the private sector, whistleblowers continue to expose themselves to criminal proceedings after reporting cases involving corruption and foreign bribery. | Increase the statutory maximum fine for legal persons in foreign bribery cases, to ensure that sanctions imposed are effective, proportionate and dissuasive.<br>Strengthen existing protection for whistleblowers in the private and public sector, including at the cantonal level. |

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# 2 Fostering a strong labour market to support the recovery and sustain growth

Véronique Salins and Urban Sila

Switzerland has a well-functioning labour market with low unemployment, a highly skilled workforce and well-paid jobs. It has proved resilient during the COVID-19 crisis, helped by extensive government support to employment and incomes. As activity recovers, the authorities face the challenge of adapting support measures to avoid hindering job reallocation and productivity growth while ensuring adequate support to vulnerable firms and workers. The pandemic has also reinforced certain pre-existing challenges. The already sizeable gender pay gap risks widening, and older workers face a higher risk of long-term unemployment. Making the labour market more inclusive would help the recovery and raise productivity. Switzerland would benefit from bringing under-represented groups more effectively into the labour market. Raising skills and lowering inequities in education and training will also be essential to facilitate job transitions and ensure that workers and firms benefit from technological change and the digital transformation.

## Introduction

Switzerland boasts a well-functioning labour market, with low unemployment, high participation and well-paid jobs. The legislation allows for high flexibility in hiring and dismissing workers and the workforce is highly skilled, which makes it well placed to adapt to economic shocks as well as to structural shifts due to technological change. Still, population ageing constrains growth in labour utilisation and the country faces high-skilled labour shortages.

Moreover, the COVID-19 pandemic represented an unprecedented challenge for the functioning of the Swiss labour market. Containment measures led to prolonged closures of many businesses, especially in the services sector, and temporary border closures and supply bottlenecks affected the manufacturing sector. Many companies faced a steep drop in revenues and uncertain prospects, resulting in a temporary oversupply of labour and pressures on unemployment, hours worked and incomes.

Swift and broad policy interventions to support workers and firms contributed to the remarkable resilience of the Swiss labour market. There was only a limited rise in unemployment and impact of the pandemic on participation remained low. Instead, the shock was reflected in an unprecedented number of workers on short-time working compensation scheme. Policy support also included loss-of-earnings compensation for self-employed workers and the provision of additional liquidity support for firms. Together, these schemes helped limit job losses and effectively sustained incomes of workers and households, preventing a rise in poverty and deprivation. In turn, the measures contributed to a rapid catch up in consumption and activity when pandemic restrictions were lifted.

As activity recovers, the Swiss authorities face the challenge of gradually adapting support measures to avoid hindering resource reallocation and future productivity growth, while ensuring adequate support to vulnerable firms and workers. A protracted and widespread use of job retention schemes bears the risk of supporting jobs that are no longer viable, slowing down growth. Policy needs to shift towards active labour market measures to facilitate job transitions and the reemployment of displaced workers. At the same time, remaining crisis-support measures need to become increasingly targeted, to ensure that adequate safety nets remain available to the most vulnerable and hard-hit workers.

The impact of the pandemic has also reinforced certain pre-existing challenges of the Swiss labour market. The already sizeable gender pay gap risks widening as women have been more likely to be put on the short-time working compensation scheme. Also, during the crisis, they took on more of the additional workload generated by childcare. Foreign workers also faced a higher risk of becoming displaced, since they disproportionally work in the most affected sectors. Older workers face an increased risk of long-term unemployment in the wake of the crisis, due to relatively greater difficulties in finding work once displaced. Moreover, low-skilled workers experienced a higher probability of job losses than more educated workers. Switzerland would benefit from bringing under-represented groups more effectively into the labour market, including by upskilling.

Before the crisis, the entry into the labour market of young people was remarkably efficient. Through its focus on vocational education and training (VET) the Swiss education system effectively integrates young people into the labour market. Nevertheless, disruptions in skills provision caused by temporary closure of schools, training centres or businesses as well as by the widespread use of teleworking risk impacting youth prospects durably, in particular for the disadvantaged students.

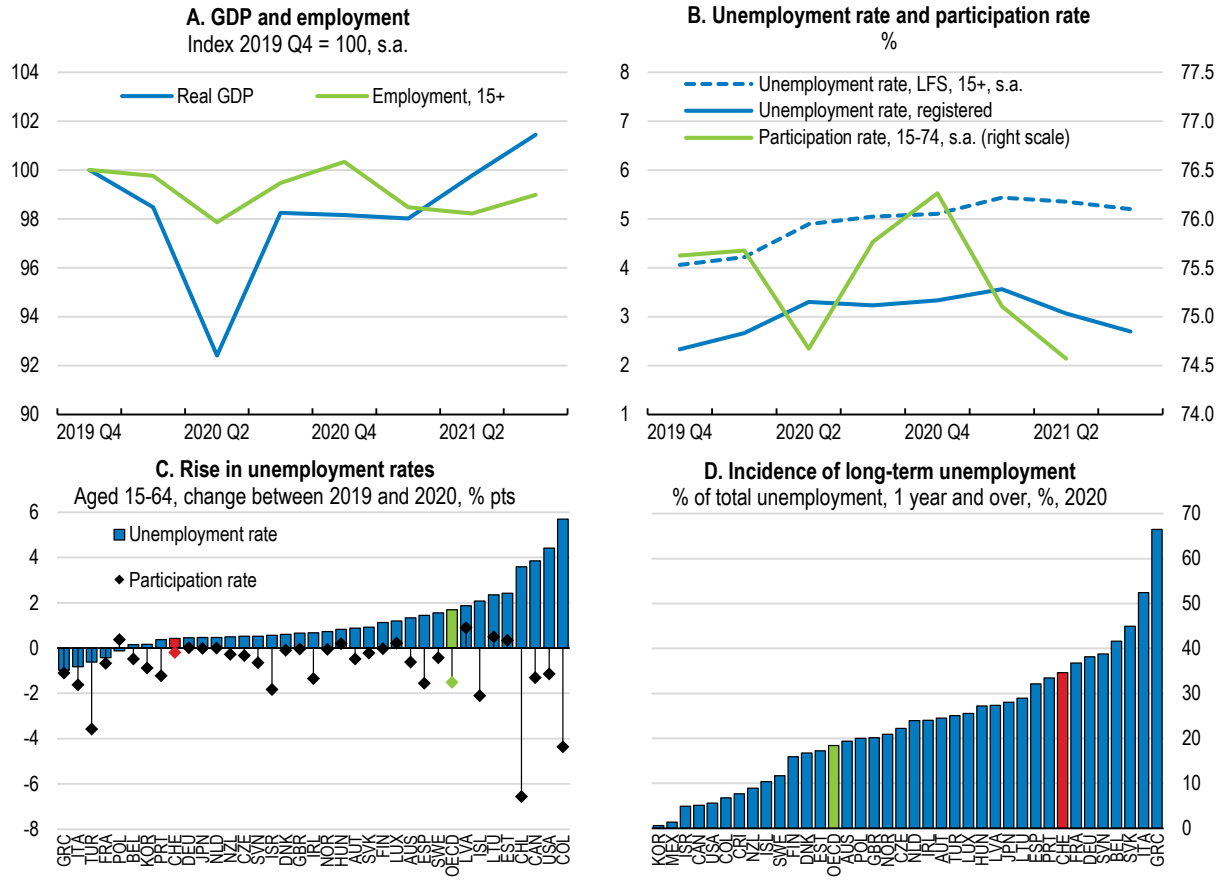
The chapter is structured as follows. The next section describes the impact of the pandemic on the labour market and identifies its main strengths and weaknesses, building on the insights of the new OECD Jobs Strategy. The following section discusses policy options to foster job reallocation while providing adequate support to vulnerable workers. Policies to encourage more workers to actively participate in the labour force and to improve the inclusiveness of the Swiss labour market are discussed in the last section.

## High resilience and substantial government support shielded the labour market during the crisis

### *Adequate policies effectively supported the labour market during the crisis*

Switzerland's labour market is well functioning and has proved resilient in the face of the COVID-19 crisis (Figure 2.1, Panel A). The harmonised unemployment rate increased to 5.1% in 2020Q4, one percentage point higher than in the fourth quarter of 2019 (Figure 2.1, Panel B). In comparison, the unemployment rate increased by 1.7 percentage points on average in the OECD economies over the same period (Figure 2.1, panel C). It has slightly declined from the beginning of 2021 but remains higher than its pre-pandemic level, while the registered unemployment rate was, by October 2021, back to its December 2019 level. However, the incidence of long-term unemployment, at 35% of total unemployment in 2020, is relatively high (Figure 2.1, Panel D), and among the unemployed registered at a public placement office, the share of the unemployed who had been out of work for more than a year rose from 11½ per cent at end-2019 to 25½ percent by December 2021 according to the State Secretariat for Economic Affairs data. The extension of unemployment benefits duration during lockdown phases of the pandemic may partly explain this sharp increase as the exhaustion of the maximum benefit durations was avoided or postponed for job seekers with already longer unemployment spells.

**Figure 2.1. The labour market has shown resilience, helped by swift policy support**




Source: OECD Economic Outlook database; OECD Short-Term Labour Market Statistics; SECO.

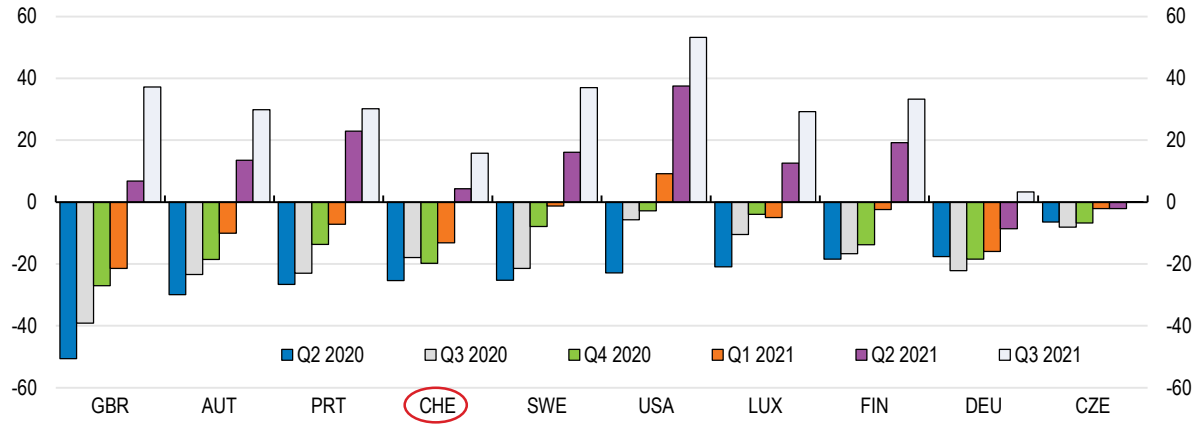
StatLink https://stat.link/jde19b

Total employment declined slightly during the first two waves of the pandemic but caught up as the economy recovered. The participation rate has declined since the beginning of 2021 but remains one of the highest in the OECD. Moreover, during the peak of the crisis the stock of vacancies declined less than

in a number of other OECD economies (Figure 2.2). Still, in the first quarter of 2021, it remained 13% below the pre-crisis level but the number of vacancies quickly rebounded in the second and third quarters with the lifting of restrictions.

### Figure 2.2. The number of job vacancies exceeded their pre-crisis level in the second quarter of 2021

Percentage change in the stock of job vacancies since January 2020, seasonally adjusted




Source: OECD Short-Term Labour Force Statistics; SFO.

StatLink https://stat.link/zu9142

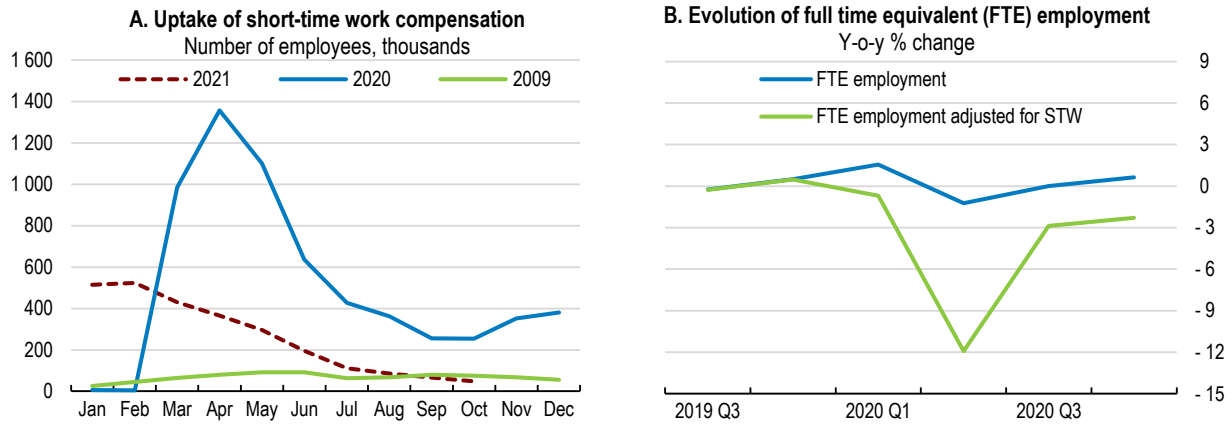
Much of the impact of the crisis was reflected in an unprecedented uptake of the short time working compensation (STWC) scheme. In April 2020, at the peak of the crisis, STWC was received by 1.36 million employees, about a quarter of the active population, 14 times more than at the peak of the global financial crisis (Figure 2.3, panel A). While full-time employment only decreased by 1.2% year-on-year in the second quarter of 2020, an estimated drop in full-time employment that takes into account the average reduction in working time associated with the use of the STWC scheme stands at a staggering 11.9% (Figure 2.3, Panel B). The number of beneficiaries declined swiftly during the third quarter of 2020 to about 254 thousand people in October. However, at the turn of the year and in early 2021, when the government started reintroducing containment measures amid the second wave, the demand for the STWC scheme rose again, albeit to a lesser extent. Full-time employment in the fourth quarter of 2020 increased by 0.6% year-on year, but accounting for workers on the STWC scheme, it would have declined by 2.3%.

Swift action by the federal authorities to shorten and simplify the application process and extend its eligibility to fixed-term employment contracts, temporary workers and apprentices greatly facilitated the use of the STWC (see Box 2.1 and section 2). The uptake of the STWC scheme among temporary workers, although significantly less than among workers with permanent contracts, was sizable (Figure 2.4 and Box 2.2). This offered effective protection to the group of workers that is usually the first to be adversely affected during an economic downturn. Moreover, the widespread use of the scheme effectively helped support worker's incomes, fostering a rapid rebound in consumption with the release of restrictions.

The Federal authorities also created a specific compensation scheme for self-employed workers whose activity was impacted by restrictions. The new instrument, temporary in nature, covered a gap in employment protection for the self-employed, who account for 14.4% of total employment but are not otherwise eligible for unemployment benefits. Total costs of self-employed compensation for loss of earnings amounted to 2 billion CHF in 2020, 0.3% of GDP. Moreover, unemployment insurance benefits were temporarily extended by up to six months between March and August 2020 and by up to three months between March and May 2021. Both the STWC exceptional provisions and the compensation for loss of earnings for the self-employed were extended to 2021 with social welfare expenditures related to COVID-19 (including expenses for the STWC, compensations for loss of earnings and unemployment insurance)

expected to amount to CHF 7 billion in 2021, about 1% of 2020 GDP. In December 2021, most measures were further extended to the end of 2022.

### Figure 2.3. The short-time working scheme significantly cushioned the impact of the pandemic on employment




Source: OECD Economic Outlook database; OECD Short-Term Labour Market Statistics; SECO; FSO; OECD calculations

StatLink https://stat.link/mnpo49

### Box 2.1. Emergency support measures during the COVID-19 crisis

Since March 2020, the authorities have adopted various policy tools to shield workers and firms from the economic impact of the crisis.

- The *short-time working compensation (STWC) scheme* is the main instrument for bridging loss of work due to the crisis. Unemployment insurance (through which the scheme is administrated and funded) temporarily covers 80% of the loss of earnings attributable to the reduction in hours worked, capped at CHF 196 per day. In 2020, CHF 20.2 billion of additional funding was transferred to the unemployment insurance fund to cover the associated expenditures, of which CHF 10.8 billion (1.5% of GDP) was used. The STWC existed before the pandemic and firms experiencing a temporary downturn in activity could request it through the cantonal employment office. However, in March 2020, the application process was shortened and simplified, and the "waiting period" (period of two or three days per month during which an employer had to cover the full cost of employees on STWC) was abolished. The coverage of the STWC was also extended to types of employees not eligible within the usual legal framework: those with fixed-term employment contracts, temporary workers and apprentices (these exclusions occur in the usual framework because fixed-term employment contracts cannot be terminated, temporary jobs are not considered as viable over the long run and because on-site presence is important for apprentices as work practice is part of the education). In addition, for low-income workers (earning less than CHF 3470 per month), the generosity of the compensation was raised in December 2020 to represent 100% of the loss of salaries (from 80%). Most of these measures were initially planned to expire by the end of August 2020, but were first extended into 2021 and later until the end of 2022.

- The *corona compensation for loss of earnings scheme* targets mainly the self-employed, directly or indirectly affected by the containment measures. It also provides daily compensation for employees and the self-employed who are in self-quarantine or need to stay at home to look after their children because of suspended child-care. In all cases, it amounts to 80% of pre-COVID crisis earnings, capped at CHF 196 per day. In 2020, the federal authorities allocated CHF 5.3 billion to the income compensation scheme, of which CHF 2.2 billion were effectively used. In December 2021, the scheme was extended until end-2022.

- Support to SMEs took the form of *federal government bridging credit guarantees* to SMEs, the "COVID-19 credit". The guarantees were issued for loans by private banks to help otherwise solvent companies cope with temporary liquidity issues. They covered 100% for the loans of up to CHF 500 000 and 85% for credits between CHF 500 000 and CHF 20 million. Banks in turn were able to access the needed liquidity for these loans at the SNB policy rate, via the SNB COVID-19 refinancing facility. CHF 40 billion worth of guarantees was made available. In practice, CHF 18 billion of loans were given out by banks in 2020. The period for the submission of applications for loans ended in July 2020. The COVID-19 credits were complemented by CHF 100 million in guarantees for start-ups.

-The *hardship clause* programme, implemented by cantons, was set up in December 2020 to bring additional support to firms affected by the restrictions. The programme provides loans, guarantees or grants to companies that were either closed by government measures for at least 40 days or, whose sales dropped by at least 40% over a 12-month period. Two thirds of the funding is provided by the Confederation and the rest by cantons. In addition, in order to support the hardest hit companies, the Federal Council has lifted the ceiling for grants to small and medium enterprises. It has also allowed the cantons to tweak the eligibility requirements of the programme to suit specific local needs, which the Federation will finance in case of additional costs. The programme was allotted CHF 8.2 billion for 2021. In December 2021, the legal basis for the scheme was extended until the end of 2022.

Support to the economy was made available through other channels as well. For example, additional sector-specific measures in the form of loans, grants or subsidies were introduced to support firms and workers in sports, culture, tourism and airline industries. Many cantons also provided additional support to firms in the hardest hit sectors.

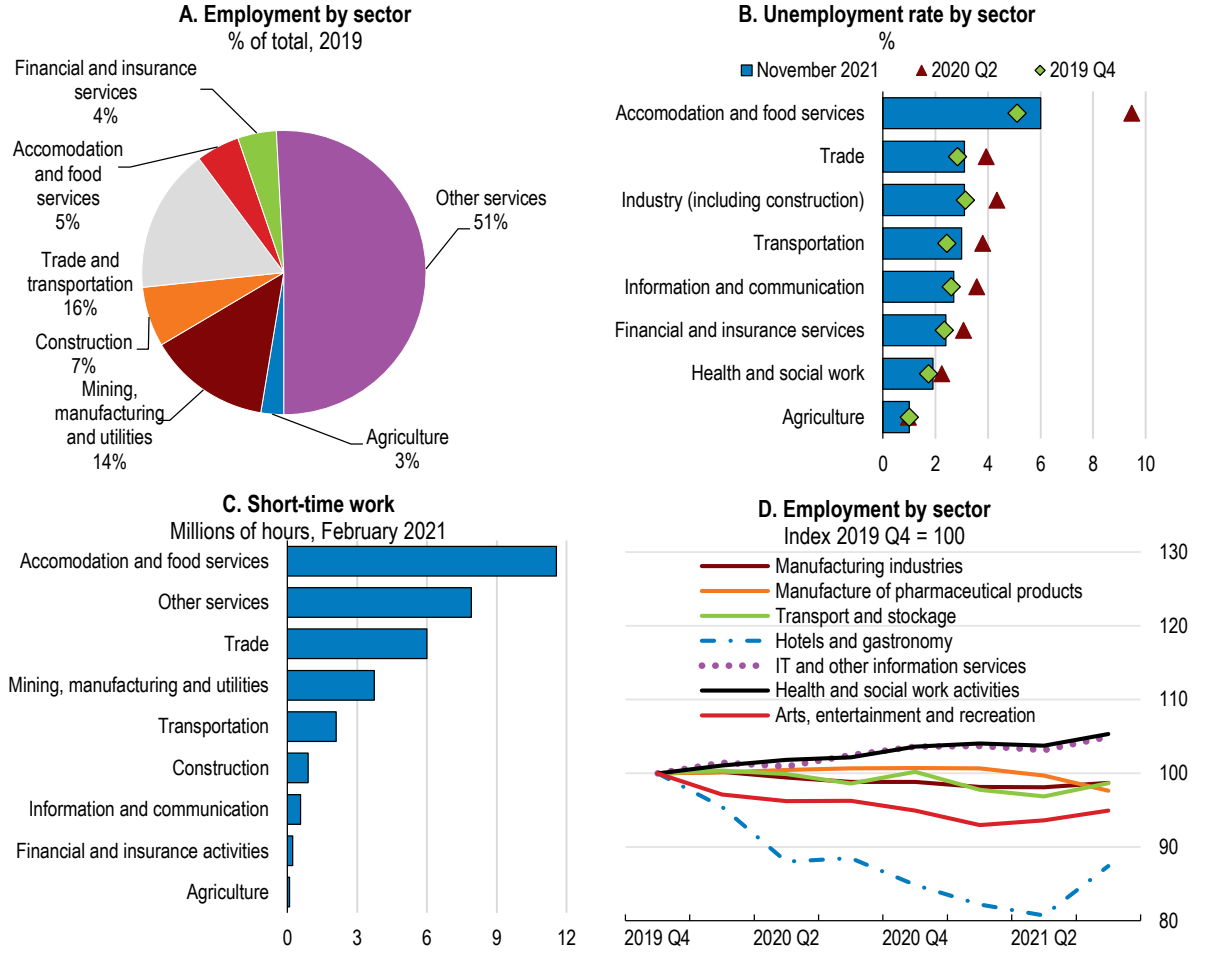
### *The impact of the crisis varied considerably across groups of workers and sectors*

Labour market developments differed widely across sectors. The activity of businesses most exposed to the containment measures, requiring close contact between consumers and producers, large crowds, or cross-border travel, were most severely affected.

The hospitality industry, which represents 5% of total employment, has been hit especially hard. Among all sectors, it displayed the highest losses in full-time equivalent employment and the highest recourse to the short-time work compensation scheme (Figure 2.4). In April 2020, about ⅔ of its 2019 workforce was receiving short-time work compensation, about 30% in November 2020, and about 45% in March 2021. The number of unemployed workers in the sector roughly doubled between January 2020 and January 2021 and according to surveys, in May, a wide majority of businesses considered further staff cuts in the coming months (KOF, 2021a, and 2021b). Employment prospects only improved during the summer 2021 when many restrictions were lifted. In July 2021, the share of the 2019 workforce receiving STWC fell to about 6%. Lasting restrictions and subdued demand severely affected the employment outlook in many other service activities, notably in art and recreation and transport. In the manufacturing sector, the machine, watch and metal industries faced a large drop in demand in 2020 (Arni, 2020), but saw a more rapid rebound in 2021.

Some sectors, on the other hand, experienced a much lower impact of the pandemic or even benefitted from it and hired new staff during the crisis. For sectors that could operate effectively with remote work, or that could effectively offer their products and services online, the challenges of the pandemic turned into an opportunity. Employment in the IT sector, in particular, remained higher than before the crisis throughout 2020. In the context of the pandemic, employment in the health care and social services and in the pharmaceutical industry displayed a similar pattern (Figure 2.4). Employment was also resilient in public administration and education and job postings data highlighted a normalisation of hiring behaviour starting in the summer 2020 in the construction and financial services sectors (X28-Novalytica, 2021).

## Figure 2.4. The impact of containment measures differed across sectors




Source: OECD National Accounts Statistics; State Secretariat for Economic Affairs (SECO); Federal Statistical Office (FSO).

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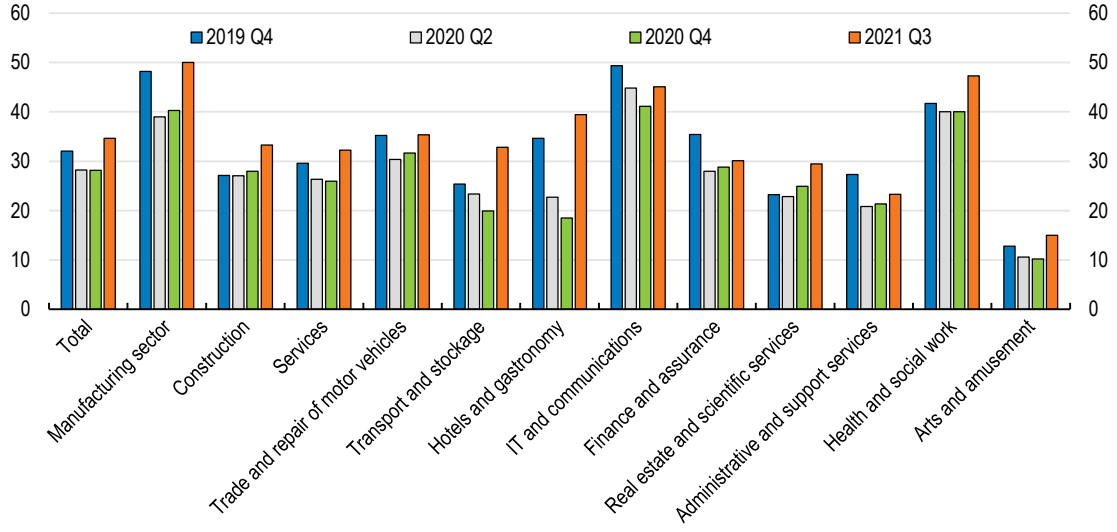
Shortages in skilled labour, which were sizable in some sectors before the pandemic, eased with the drop in activity (Figure 2.5). However, the reported difficulties in hiring qualified workers remained elevated in the manufacturing, IT and communication, and health and social work sectors. Moreover these difficulties significantly increased with the economic recovery in the second and third quarters of 2021 to stand close to, or above, their pre-crisis level.

In spite of effective policy support, many households saw their incomes drop. Relatively high resilience in aggregate masks a large heterogeneity across groups of workers. The KOF Swiss Economic Institute (KOF, 2021d) reports that the pandemic widened economic and health disparities, impacting disproportionately low-income households. While the rise in the unemployment rate did not differ significantly between men and women, or across age groups, foreign-born workers experienced a larger increase in their already higher unemployment rate, compared to Swiss-born workers. Moreover, using survey data, Hijzen and Salvatori (forthcoming) show that uptake of the STWC was more frequent for women than men. They also point to a larger use of the STWC schemes for low- to middle-skilled workers and a larger probability to lose jobs for the low-skilled and workers on temporary contracts, suggesting that the crisis had a significantly stronger impact at the lower end of the wage distribution (Figure 2.6 and Box 2.2).

## Figure 2.5. Skilled labour shortages temporarily eased during the pandemic

Difficulties in recruiting, qualified personnel found with difficulty or not found at all, %




Source: Federal Statistical Office (FSO).

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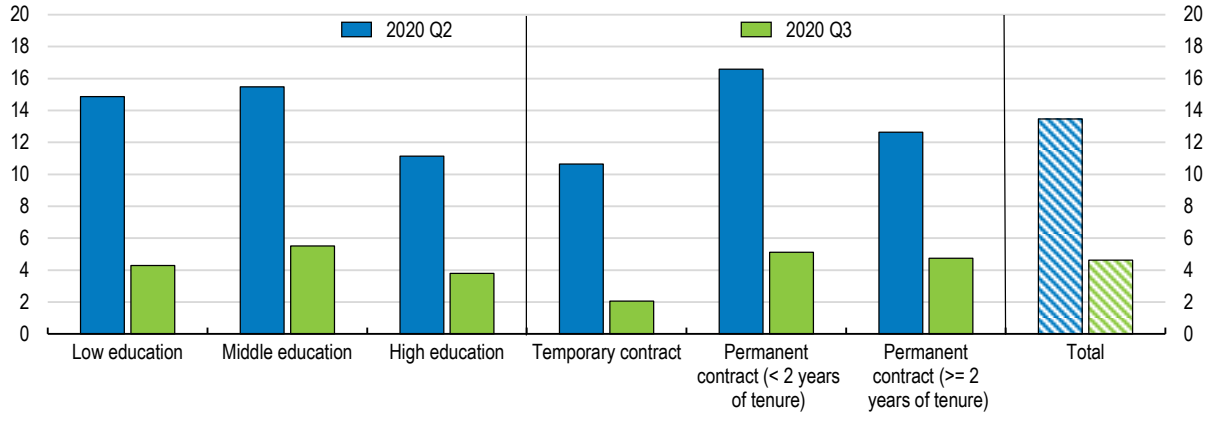
## Figure 2.6. Short time work use differed across groups

Percentage of dependent employees




Source: OECD Employment Outlook 2021.

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### Box 2.2. The Swiss Short Time Work scheme effectively protected jobs in 2020

The overall resilience of the Swiss labour market is in large part due to the use of its short-time work compensation (STWC) scheme that helped to keep the risk of job loss for employees at bay. Hijzen and Salvatori (forthcoming) use longitudinal data from the Swiss Labour Force Survey to study labour market transitions during the year 2020. Two key transition probabilities are calculated between consecutive quarters for different groups of employees since the onset of the Covid-19 crisis: (i) the probability of moving to non-employment, and (ii) the probability of being placed on STW. The results show that, as the crisis hit and economic activity fell dramatically, the probability for an employee to be placed on STW jumped from about 1% before the crisis to the unprecedented level of 13% in the second quarter of 2021.

As a result, the risk of job loss for an employee remained subdued at 4% - only 1 percentage point higher than in the five years before the crisis.

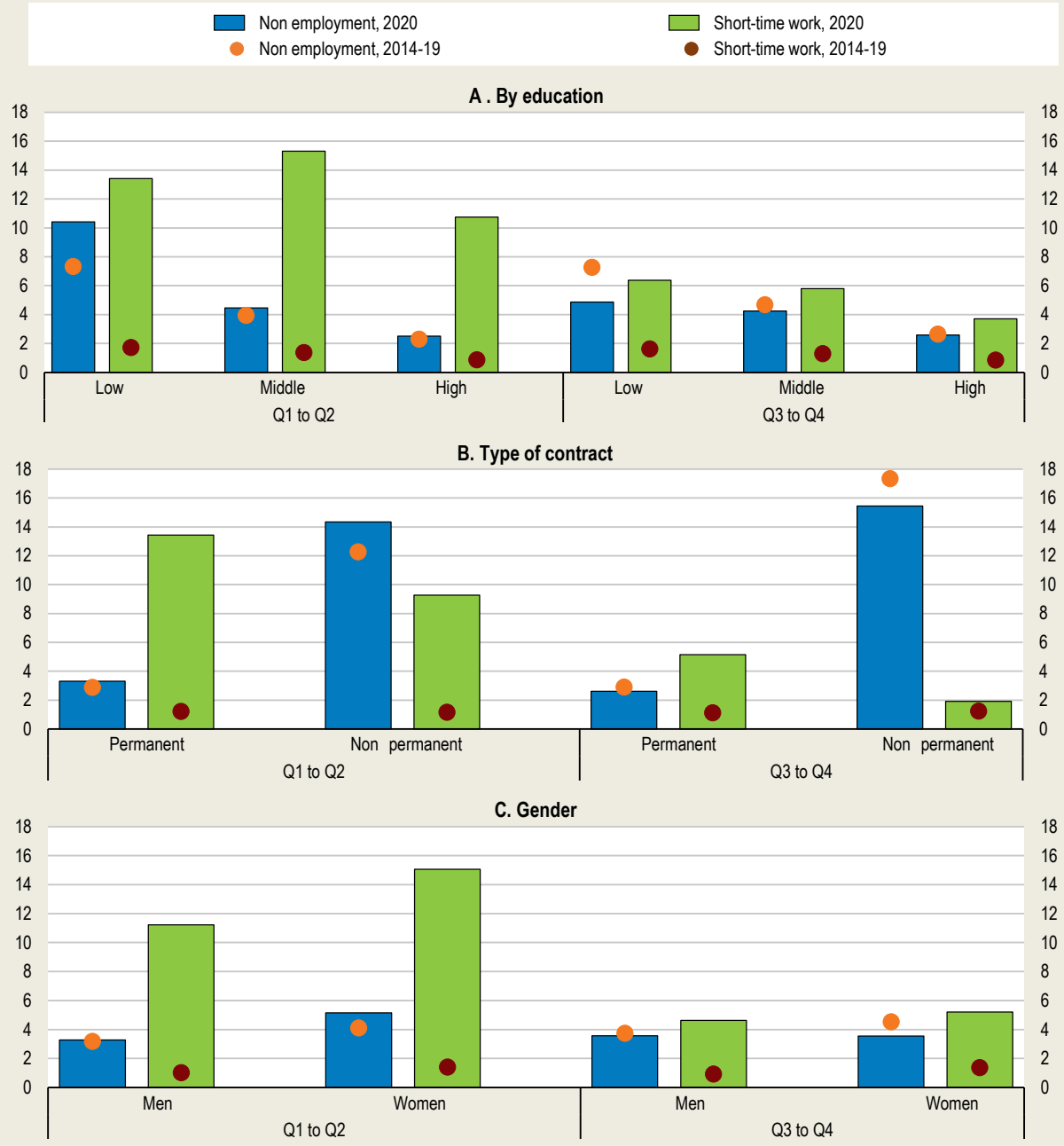
The analysis provides some evidence that the scheme might have been somewhat less effective in preserving the jobs of the low educated and workers on temporary contracts during the first quarter of the crisis. In Q2 2020, these groups saw a larger increase in the risk of losing their employment compared to other groups, but not a higher probability of being placed on STWC scheme. For example, the probability that a low educated worker lost his or her employment between Q1 and Q2 was 10% - an increase of 3 percentage points compared to the pre-crisis period much larger than that seen for mid educated workers (Figure 2.7). By contrast, the low educated were less likely to be placed on STWC scheme than mid-educated workers (13% vs 15%). However, there is no indication this continued to be the case in subsequent quarters. The temporary removal of the waiting period and the extension of eligibility to workers on temporary contracts may have been particularly important for encouraging the use of short-time work for young and low-educated workers.

While women, part-time, young and older workers were disproportionately affected by the crisis at first, there is no indication of discriminatory use of the STWC scheme to preserve jobs across gender, part-time status and age groups. Women, for instance, saw a larger increase in the risk of job loss than men during the first wave of the pandemic, but this was due to the type of jobs they hold. Indeed, once occupation, contract type and industry are controlled for, the impact of being female on job loss becomes statistically insignificant. At the same time, women were also more likely to be on the STWC (15% vs 11%) (Panel C of Figure 2.7) independently of the type of jobs they hold. This suggests that they were initially hit harder than men by the crisis but also that the STWC scheme protected them from unemployment. In later quarters, both women and men saw a reduction in the risk of job loss compared to the recent past. By the end of the year, the difference in the risk of job loss became smaller than in the pre-crisis period – with both women and men facing a risk of job loss of around 3.5% between Q3 and Q4. Similarly, the difference in the probability of STWC between women and men became smaller over time, even though women remained slightly more likely to be on the scheme than men by the end of 2020 (5.2% vs 4.6%).

Overall, the design of the Swiss short-time work scheme complemented with the additional measures to boost its use appears to have been fit for purpose. Going forward, there is a growing risk that jobs that remain on STWC support are no longer viable, as already witnessed by the growing fraction of jobs supported by STWC that are eventually terminated.

## Figure 2.7. Probability that an employee moves to non-employment or short-time work between consecutive quarters

Percentages




Source: Hijzen and Salvatori (forthcoming)

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### *The legacy of the crisis could weigh on the labour market*

Based on the OECD Job strategy dashboard on the overall performance of the labour market (see Box 2.3, OECD, 2108a and 2018b), Switzerland is among the top-performing countries on most measures (Figure 2.8), and above the OECD average in all categories but one (the gender labour income gap). The employment rate is high, unemployment and labour underutilisation are low. Workers receive comparatively high wages and labour market insecurity is low. Moreover, there is a relatively high level of equality in incomes and opportunities. However, the gender labour income gap is persistently high and some disadvantaged groups face barriers in the labour market.

#### Box 2.3. Implementing the OECD Jobs Strategy during the COVID-19 crisis and beyond

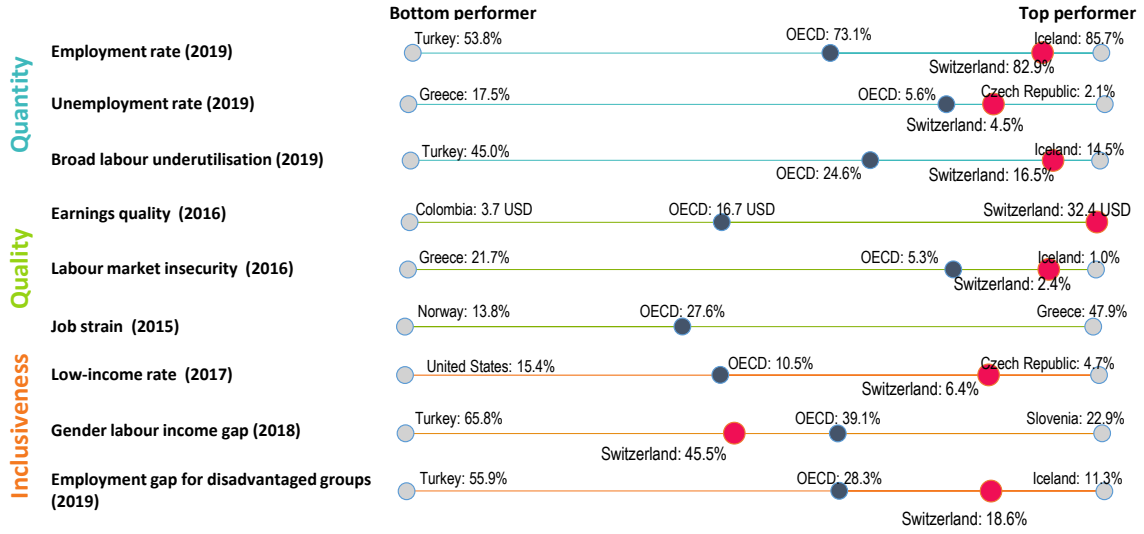
The objective of the OECD Jobs Strategy is to support policy-makers in member and partner countries with achieving good labour market outcomes, including during times of social and economic upheaval such as those currently experienced by most OECD countries. The Jobs Strategy goes beyond job quantity and considers job quality and inclusiveness as central policy priorities, while emphasising the importance of resilience and adaptability for good economic and labour market performance in a changing world of work. Given its emphasis on resilience and adaptability, the Jobs Strategy is particularly relevant in present context as the COVID-19 crisis is testing the resilience of labour markets and has accelerated some of the pre-existing structural trends to which labour markets will have to adapt.

The OECD actively supports countries with the implementation of the OECD Jobs Strategy through the identification of country-specific policy priorities and recommendations. This is done through the preparation of special Jobs Strategy chapters in the OECD Economic Surveys as well as more analytical background papers on the implementation of the OECD Jobs Strategy in specific countries. In the case of Switzerland, the special chapter is supported by additional analytical work on the impact of COVID-19 crisis on different socio-economic groups and the role of job retention schemes. The implementation process will be concluded with a synthesis report that will draw lessons from the country reviews and highlight good practices across the full range of policy tools identified by the OECD Jobs Strategy.

For further details see http://www.oecd.org/employment/jobs-strategy/.

## Figure 2.8. The Swiss labour market performs well in international comparison

Dashboard of the labour market according to the OECD Jobs Strategy




Note: Employment rate: share of working-age population (20 to 64) in employment (%). Unemployment rate: Share of persons in the labour force (15-64 years) in unemployment (%). Broad labour underutilisation: share of inactive, unemployed or involuntary part-timers (15 to 64) in the population (%), excluding youth (15 to 29) in education and not in employment. Earnings quality: gross hourly earnings in US dollars adjusted for inequality. Labour market insecurity: expected monetary loss associated with becoming and staying unemployed as a share of previous earnings. Job strain: share of workers in jobs in which there typically exists a high level of professional demand and insufficient resources to meet that demand. Low income rate: share of working-age persons living with less than 50% of median equivalised household disposable income. Gender labour income gap: difference between average annual earnings of men and women divided by average earnings of men (%). Employment gap for disadvantaged groups: average employment gap between prime-age male workers and five disadvantaged groups (women with children, young people not in education or full-time training, workers aged between 55 and 64, people born abroad, people living with disabilities), as a percentage of the employment rate for prime-age male workers.
Source: OECD calculations based on statistics for 2019 or the last available year and various sources.

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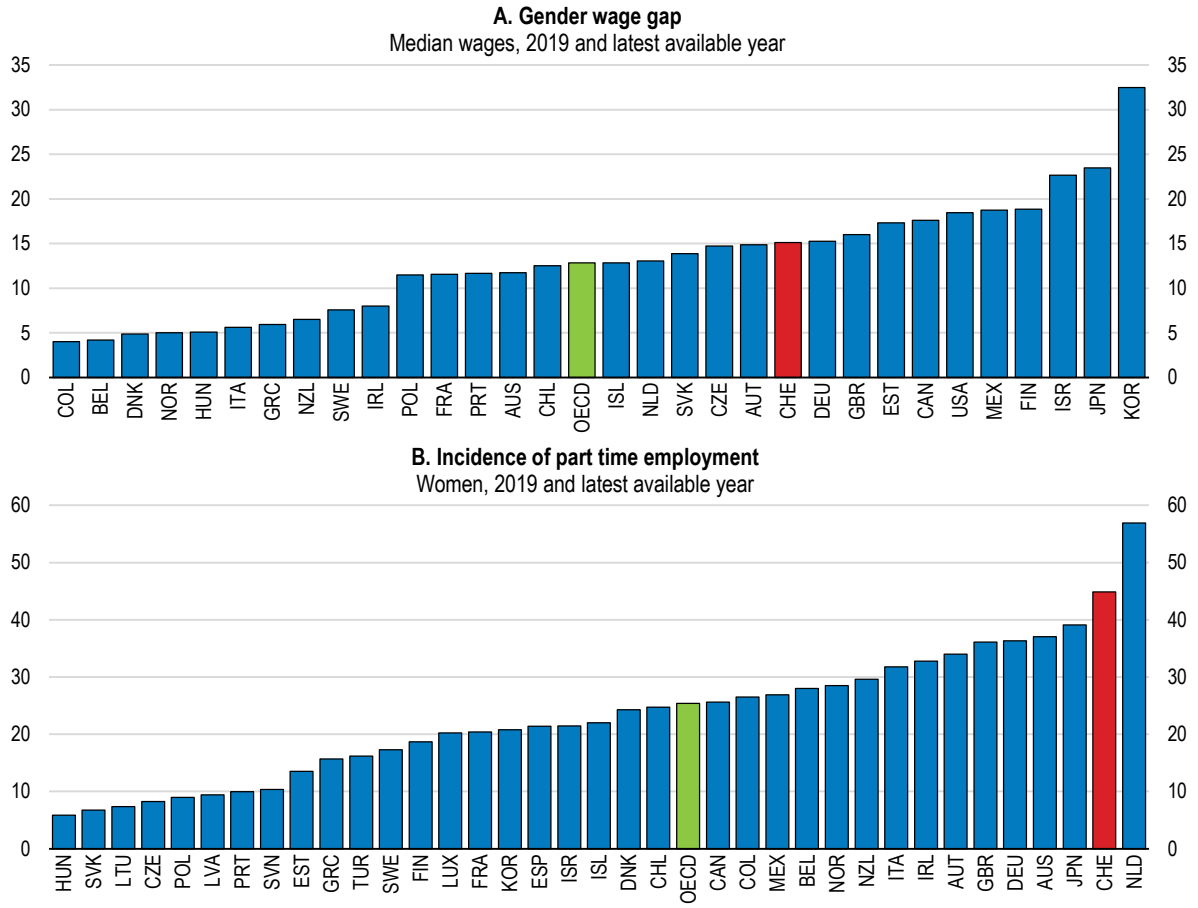
The gender wage gap for full-time workers, at 15% in 2019 (when considering median wages, 19% when considering average wages), is above the OECD average (Figure 2.9, Panel A). While female employment is very high in Switzerland, close to 45% of women work part-time (Figure 2.9, Panel B). This further aggravates the gap in labour incomes between men and women that stood at 45.5% in 2018, well above the OECD average. The gender gap is also related to low labour participation of mothers with young children. This group shows a roughly 15% gap in employment compared to prime-age men.

During the recent crisis, the reduction of working hours has been only slightly more pronounced for women than for men. The most affected sectors such as the hospitality sector disproportionately employ women, but this is also the case for sectors whose employment remained robust during the crisis, such as public administration, education and health care (Figure 2.10, Panel A). Nevertheless, survey data indicate that the burden of caring for children during lockdown and closures of day-care facilities fell disproportionally on women. This can probably partly explain why the uptake of the STWC in the first transition period analysed (Q1 to Q2) was more frequent for women even after controlling for occupation (see Box 2.2). This was the time when school closed for several weeks.

## Figure 2.9. The sizeable gender wage gap and high incidence of part-time work weigh on women's labour incomes




Note: Panel A: Gender wage gap for workers in full-time employment. Panel B: Part-time employment is based on a common 30-usual-hour cut-off in the main job.
Source: OECD Labour Force Statistics database.

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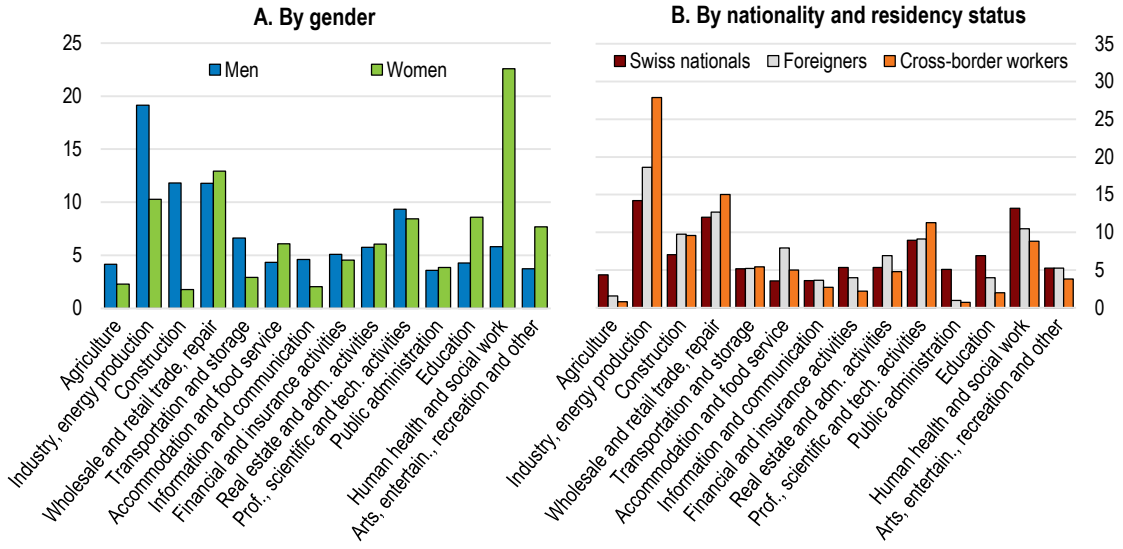
## Figure 2.10. Women and foreigners disproportionally work in the most affected sectors

Effective working hours by sector, % of total, 2019




Source: Federal Statistical Office (FSO).

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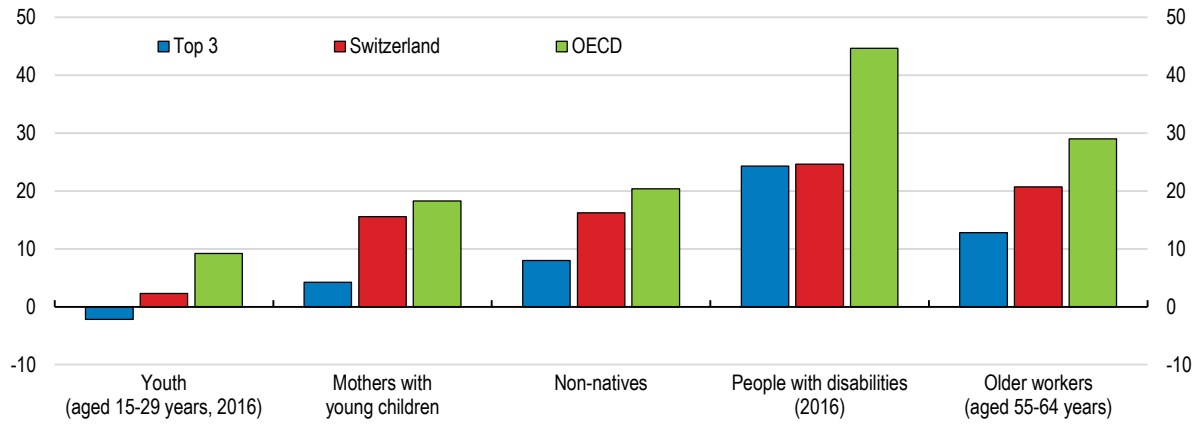
Switzerland compares well internationally on the labour market integration of under-represented groups (Figure 2.11), but some groups face challenges. Older workers (aged 55-64) have almost 20% lower employment rates than prime-age men, a gap below the OECD average but significantly above best performers. Data shows that the crisis has not affected the employment of older workers disproportionally but previous experience suggests that their reintegration in the labour market following an unemployment spell is significantly more challenging than for prime-age workers (SECO, 2019a and 2020). Hence, they are more likely to end up in long-term unemployment. Also, non-native workers have a significantly lower employment rate, with an employment gap to native workers of 17%, and their unemployment rate rose further during the crisis (to 8.5% versus 3.9% for native workers in 2020 Q4) in part because they disproportionately work in the most affected sectors (SFO, 2021). They are, in particular, over-represented in the hospitality sector (Figure 2.10, Panel B). The impact of the pandemic on the specific situation of cross-border workers is more difficult to assess as Swiss statistics on unemployment and STWC scheme use (to which they are eligible) by country of residence are not available. However it is noteworthy that the number of cross-border workers among the active population did not decline during the pandemic: it stagnated during the first half of 2020, at about 340 thousand, and rose thereafter to reach 352 thousand by the third quarter of 2021. As these workers are significantly over-represented in the manufacturing sector (Figure 2.10, Panel B), these developments partly reflect the evolution of activity in manufacturing: a significant drop during the first wave of the pandemic, which led the sector to massively use the STWC scheme, followed by a relatively rapid recovery.

With regard to youth (15-29 years), Switzerland is among the best performers in terms of the employment gap. During the crisis, youth unemployment (15-24 years) significantly increased during the second and third quarter of 2020, but it quickly returned to the pre-pandemic level by the end of the year. Similarly, young workers were less likely to be placed on STWC than older workers in the second quarter of 2020 but in the later stages of the crisis the protection offered by the scheme appears to have been quite even across age groups (see Hijzen and Salvatori, forthcoming).

### Figure 2.11. Employment gaps are sizeable for some groups

Employment gap[1], per cent, 2019 or latest year available




1. The employment gap is defined as the difference between the employment rate of prime-age men (aged 25-54 years) and that of the group, expressed as a percentage of the employment rate of prime-age men. Youth excluding those in full-time education or training. Mothers with young children refers to working-age mothers with at least one child aged 0-14 years. Non-natives refers to all foreign-born people with no regards to nationality.

Source: OECD (2018), Good Jobs for All in a Changing World of Work: The OECD Jobs Strategy, OECD Publishing, Paris, https://doi.org/10.1787/9789264308817-en; OECD Labour Force Statistics; OECD Family database; OECD Migration Statistics.

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## Exiting the crisis and facilitating job reallocation

### *Balancing adequate support and incentives for workers' reallocation*

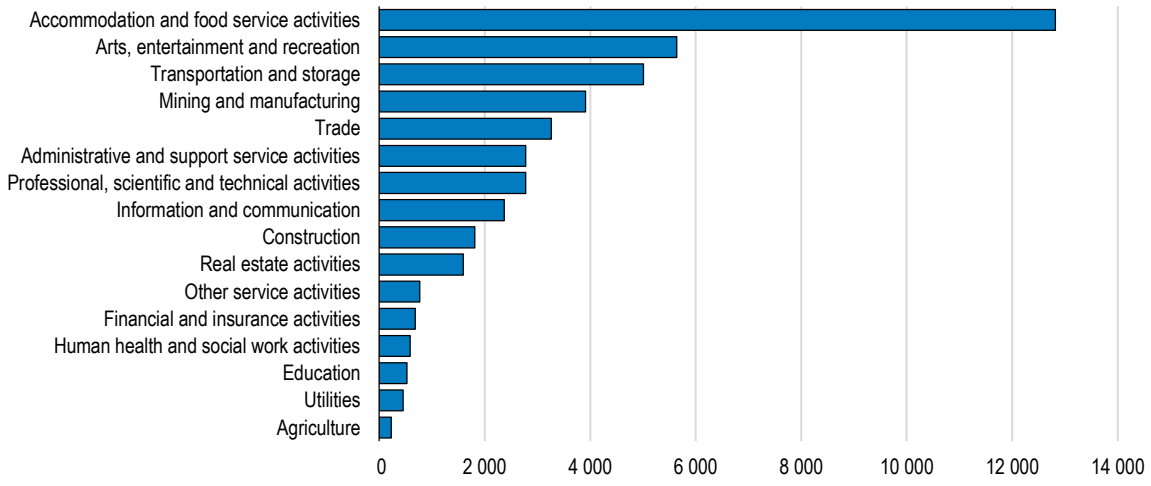
During the early stages of the pandemic when activity was heavily constrained by containment measures, the short-time working compensation (STWC) scheme was the main instrument to support the economy and the labour market. It provided the necessary support to firms to keep their workers, helping them avoid costly firing and rehiring while sustaining workers' incomes. The corona compensation scheme for loss of earnings also played a role, supporting the self-employed, people in quarantine and parents who had to stay at home for childcare duties.

Nevertheless, extended job retention schemes may disincentivise workers to look for a new job, slowing economic restructuring. There are risks that the Swiss economy will not just simply go back to its previous state once containment measures are finally removed. For instance, the air transportation sector as well as tourism operators expect lower client flows for several years to come (Arni, 2020). The massive increase in the use of online tools and services during the pandemic may also prove durable and have a more permanent impact on the economic structure and the labour market. Protracted containment measures have significantly weighed on the financial health of some enterprises, especially in the most affected sectors where concerns about potential bankruptcies rose significantly in the first months of 2021 (KOF 2021c). The risk therefore is that the schemes protecting jobs channel public money to protect the status quo.

However, for now, there is little evidence that the schemes protected unviable jobs or that they inhibited workers' reallocation. Data shows that support overwhelmingly went to firms in sectors affected by government-mandated restrictions (Figure 2.12). Meanwhile, job vacancies remained generally depressed in 2020 and in the first quarter of 2021 (see Figure 2.2), limiting opportunities for job mobility. Still, the number of vacancies across sectors displayed a large heterogeneity of labour demand and they strongly rebounded during the second and third quarters of 2021. However, based on FSO survey-based job statistics, the difficulty for firms in hiring staff decreased in 2020 in comparison with 2019 in a wide majority of sectors.

### Figure 2.12. Short-time work was massively used in the sectors most affected by restrictions

Short-time working compensation (STWC) disbursements by sector, CHF per person employed, March 2020-October 2021




Source: OECD calculations based on SECO, BFS, OECD National Accounts database.

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Concerns about the possible adverse effects of the STWC on job reallocation grow in cases where restrictions persist and an elevated number of workers remain on the scheme for a prolonged period of time. Questions about the viability of jobs that are being supported for a prolonged period are likely to intensify, while the risk of undermining job creation and reallocation increases as vacancies pick up. Yet, as pointed in the latest OECD Employment Outlook (OECD, 2021a) assessing the viability of jobs is very difficult for government even in normal times, let alone in a context where economic restrictions remain important and market signals are weak (see also OECD, 2020a). Therefore, the government needs to adapt the STWC scheme to provide better incentives for firms and workers - who are likely to have a better sense of the viability of a given job than governments - to use support only for jobs that are temporarily at risk but remain viable in the longer term.

Before the crisis, firms facing a temporary downturn could request the STWC from the cantonal employment office, upon agreement with the employees. An advance notification of the claim needed to be made at least 10 days ahead of the expected reduction in working hours. The compensation, paid by the unemployment insurance to the enterprise, represented 80% of the employee's loss of earnings attributable to the reduction in working hours. It also covered the employer's share of social security contributions associated with reduced hours (except for the employers' contributions for family allowances and for the second pillar of the pension fund). Only permanent employees were eligible to receive a STWC for a maximum duration of 12 months (with a possible extension to 18 months if necessary) for every two-year period. Requests needed to be renewed every three months. However, enterprises had to pay full wages of two working days ("waiting period") per month during the first six months of the scheme, and three working days thereafter, increasing the stake of the firm in the scheme.

During the early stages of the pandemic, the federal authorities took a broad set of measures to facilitate the uptake of the scheme and broaden its coverage. With regards to the process, from March 2020 to June 2021, the claim process was simplified and digitalised. Up to December 2021, the 10-day advance notice for claims was eliminated. Between September 2020 and December 2021, the cantonal authorities' reassessment of a firm's request were set to occur every 6 rather than 3 months. With regards to benefits, the "waiting period" of two (or three) days was suppressed from March 2020 to June 2021, reducing the cost to firms. Starting in July 2021, a waiting period of one day per month was reintroduced. In September 2020, the maximum duration of the scheme was extended to 18 months and, in March 2021, to 24 months.

To protect the incomes of the most vulnerable workers, between December 2020 and June 2021, workers on STWC earning up to CHF 3470 received 100% compensation of their earnings. In addition, during the first wave of the pandemic and from January to September 2021, apprentices and workers on fixed-term employment contracts were also made eligible to receive STW compensations. It was also the case for temporary agency workers but only during the first wave of the pandemic.

While these arrangements to the pre-existing STWC scheme offered necessary protection to workers and companies, they should be scaled back as restrictions are lifted and the economy recovers, to let economic restructuring take place. However, a transitory phase is warranted to ease pressures on hard-hit sectors.

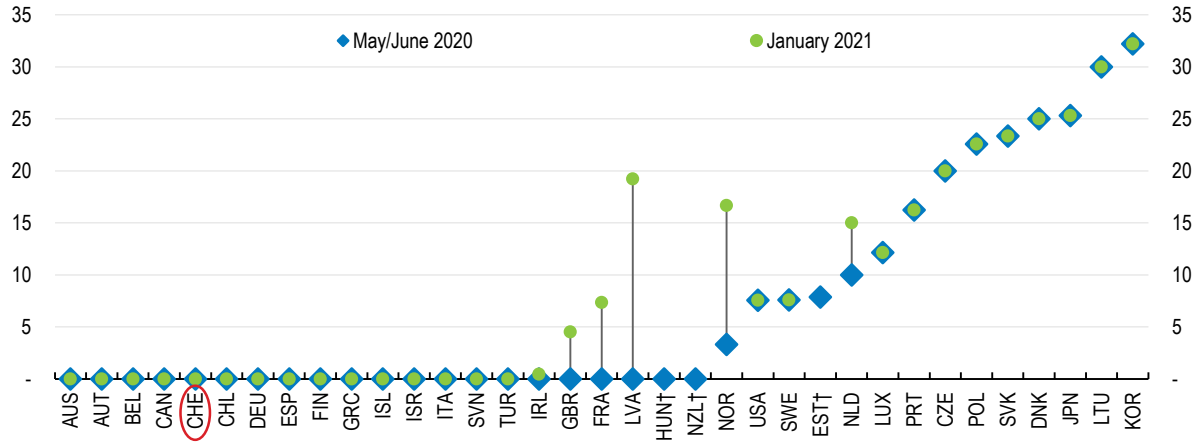
Going back to the initial, stricter, duration of the STWC scheme can ensure that support is time-limited and is not used to support firms with structural difficulties. The extended maximum duration of support in Switzerland, at 24 months, is relatively long in international comparison (OECD 2021a). The length of the scheme also reaches 24 months in Germany but is limited to 3 months in Portugal, for instance. In France, the length of support can reach 24 months as well but only if the activity of employees is not reduced by more than 40%. Prolonging the maximum duration of the scheme, even if warranted at the beginning of the crisis when the duration of the shock was not known, bears the risk of supporting jobs that are no longer viable.

Empirical evidence from the global financial crisis (GFC) shows that in the context of a temporary shock, the use of the STWC in Switzerland was effective in preventing unemployment rather than postponing it, reducing scarring effects from the shock. However, the results hold for the majority of firms that left the scheme before the end of its maximum duration when it was economically viable to do so. In contrast, businesses that used the scheme up to its legal end tended to lay off workers after its termination (OECD 2020a, Kopp and Siegenthaler, 2019). In Italy, where the GFC had long-lasting effects and the STWC scheme was targeted to low-productivity firms, the effects of the program were more mixed with many layoffs being postponed rather than prevented, slowing down job reallocation (Guipponi and Landais, 2018).

The STWC scheme can also be adapted to require participating firms to cover part of the cost of hours not worked. This can strengthen incentives to use the scheme to only support jobs that are likely to resume regular work schedules soon after the crisis. The reintroduction in July 2021 of a co-payment by employers (this co-payment was suspended for the first three months of 2022 due to elevated uncertainty) in the form of a one-day waiting period per month and employee in STWC is a step in the right direction. However, the incentive is quite limited and could be raised to 2 or 3 days of waiting period as in the initial setting of the scheme, at least in sectors that are not facing restrictions any longer. Some OECD countries provide alternative examples of measures aiming at increasing firms' financial participation in job retention schemes (Figure 2.13). From July 2021, employers in Germany taking part in a job retention scheme will become liable again to social security contributions (OECD 2021a). In France, since July 2020, firms have been required to pay 10% of the cost of hours not worked in sectors that are no longer subject to restrictions.

## Figure 2.13. Several countries have recently (re)introduced or increased co-financing by firms in job retention schemes

Cost of hours not worked for firms as % of labour cost for the maximum permissible reduction in working time, May/June and January 2020




Note: † Schemes no longer operational in January 2021. Mandatory employer contributions for private insurance are not taken into account (consistent with the OECD methodology of Taxing Wages). Norway: for the first 3 months (60 days).
Source: OECD Employment Outlook 2021, Chapter 2.

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The STWC scheme in Switzerland mostly applied the same rules to all firms. While eventually equal treatment of all firms is desirable, the transitory phase could provide for some differentiation across sectors and firms to take into account the heterogeneous impact of the restrictions. From July 2021, France, for instance, applied different rules for sectors that remained subject to government-imposed restrictions as seen in the example above. Since August 2020, Portugal requires firms to pay for 30% of the costs of hours not worked when working time is reduced by less than 60%, while there is no co-financing for firms with larger reductions in working time. Moreover, firms with a reduction in sales of more than 75% can receive additional wage subsidies to contribute to the cost of hours worked (OECD, 2021a). Some differentiation was introduced also in Switzerland, from December 2021. Places facing tighter restrictions (access only for vaccinated people or people who have recovered from COVID-19 and present a negative test result) such as nightclubs or indoor pools are entitled to the short-time working compensation also for on-call workers with an open-ended employment contract, workers with fixed-term contracts and apprentices.

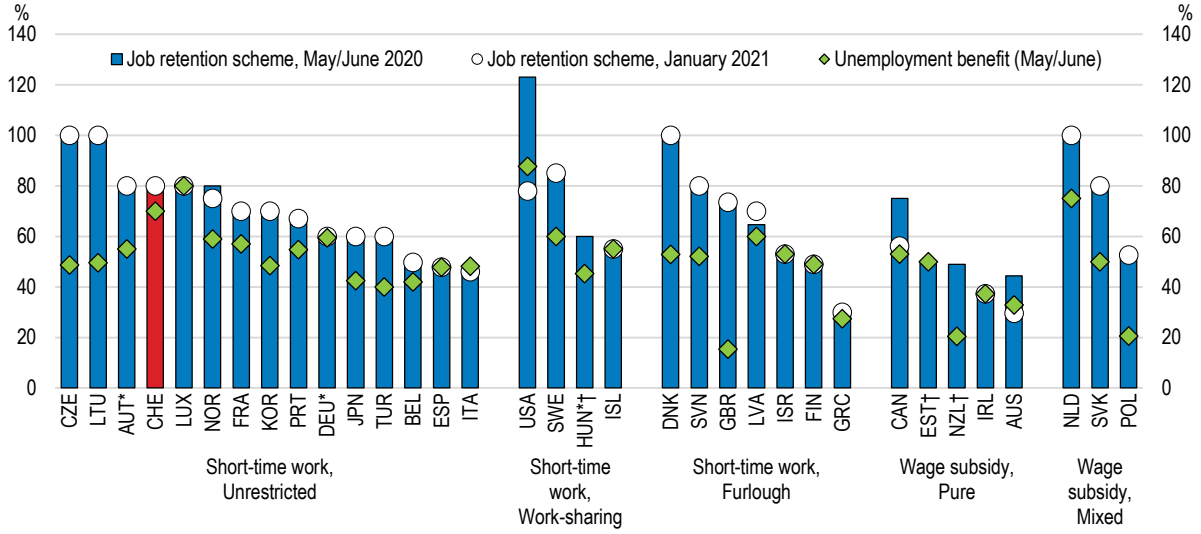
Balancing job retention and reallocation also requires striking the right mix of in-work (job retention schemes) and out-of-work (unemployment benefits) support. In most OECD countries where job retention schemes are in place, gross replacement rates within those schemes were more generous than the unemployment benefits, at least in the early phase of the crisis (Figure 2.14). This was also the case in Switzerland where the hours not worked, on STWC, were subsidized at 80% of the worker's hourly earnings compared to 70% under the unemployment insurance scheme (for workers with no dependent children and/or an insured wage above CHF 3797). The gap is not large. However, the decision of the Parliament in December 2020 to increase the replacement rate of hours not worked under the STWC scheme to 100% for workers earning up to CHF 3470, made it significantly bigger for low-income workers.

More generous STW benefits than unemployment benefits might boost acceptability of the scheme by employees, and help prevent a situation where too many unemployed people search for a limited number of jobs at the same time (OECD 2021a, Guipponi and Landais 2018 and Lalive, Landais and Zweimüller, 2015). The gap may also help employees internalise the additional benefit of keeping the existing employer-worker match to the employer, due to the value of the job-specific human capital and costs of

firing and hiring. However, reducing this gap over time should be envisaged to avoid hindering workers' willingness to look for a new job. Moreover, the increase of the STWC replacement rate to 100% for low-income workers, while warranted in the early time of the crisis as they have been disproportionally affected by the pandemic, should remain temporary, as currently planned.

### Figure 2.14. Gross replacements rates in job retention schemes tend to be higher than in the unemployment benefit systems

% of gross wage, evaluated at the average wage for the maximum permissible reduction in working time




Note: Net terms (after taxes and other benefits). † Ended schemes in January 2021. Unemployment benefit for a single adult with no children and two months of unemployment.
Source: OECD Employment Outlook 2021, Chapter 2.

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Some subsidized jobs are likely to become permanently unviable, with a high risk of workers losing their jobs eventually. In this context, supporting transitions from subsidised to unsubsidised jobs could be warranted. This could be done through the provision of effective public employment services (PES) to beneficiaries of the STWC scheme. In Switzerland, workers on the STWC scheme are allowed to voluntary register with a regional placement office (RPO) and access its services which include job–search assistance, career guidance and counselling (OECD 2021a, OECD 2020b). However, such registration is neither mandatory nor actively promoted by the federal or cantonal authorities, raising doubts about its actual uptake. Targeted support to employees in STWC would be warranted as Hijzen and Salvatori (forthcoming) show that in Switzerland during the pandemic, employees on STWC scheme in a given quarter were significantly more likely to lose their job the following quarter compared to other employees. Support could take the form of regional placement offices reaching out to workers on protracted spells in the STWC scheme (especially if their working hours have been significantly reduced) with information about the process and the potential benefits it can provide. The use of a simplified application process has facilitated the uptake of the STWC during the peak of the crisis but has provided little information on the identity and personal characteristics of the beneficiaries to the public employment services. With the progressive recovery, the digital application process should be revised to increase the set of information on beneficiaries available to the PES and allow for a better follow-up of their situation. More generally, incentives for workers on reduced hours to participate in training could be provided as this would be beneficial for all workers on STWC scheme, including those who expect their position to be maintained. In New Zealand, for instance, the Ministry for Social Development contacted firms on job-retention schemes with information about training opportunities. In France and Germany, financial incentives are provided to firms or workers to encourage training.

### *Seizing the opportunity to reconsider the social protection of the self-employed*

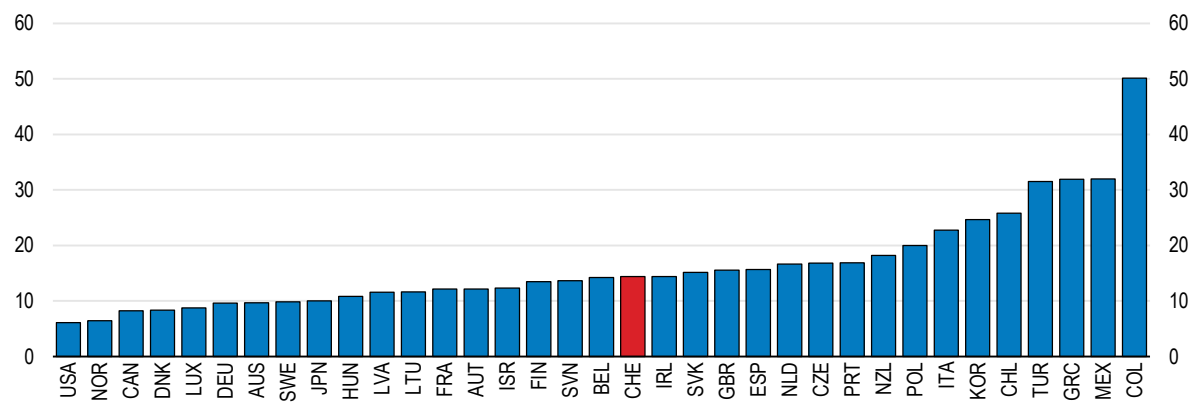
Through the corona compensation for loss of earnings, the government offered support to the self-employed during the crisis. This was welcome, as the self-employed experienced a larger decline in effective working hours than employees (effective working hours decreased by 5.5% for the self-employed in 2020 compared to 4.5% for employees according to SFO data). As a result, they also faced a larger drop in income among the people in employment according to the sixth edition of the SRG Corona Monitor survey carried out by the Sotomo research institute (Sotomo, 2020).

The incidence of self-employment is relatively high, but strict rules classify a number of non-standard workers as dependent employees, ensuring social protection. The self-employed represented 14.4% of total employment in 2019, a higher share than in many advanced economies (Figure 2.15) despite quite strict qualifying criteria. To be recognised as self-employed a person needs to work for more than one client, act in his or her name, must be free to organise his or her work and must carry the financial risks associated with their activity (CIAA 2016 and Bonoli 2017). These strict rules, for example, grant most "platform" workers the status of dependent employees and, as such, a broader social protection coverage.

The social protection of the self-employed, on the other hand, shows large gaps in Switzerland as in a number of OECD economies (Figure 2.16). The self-employed have access to first pillar provisions of old-age pension and to invalidity insurance as well as to income compensation during maternity leaves and family benefits. However, they are not systemically covered by the second-pillar of pension and invalidity insurance. In many cases, self-employed workers need to insure themselves at their own initiative if they want to complement the first pillar provisions (Bonoli 2017). The tax system provides incentives to contribute to these schemes. Moreover, self-employed workers are little covered by unemployment insurance as they can only claim unemployed benefits if, in addition to self-employment, they have completed a minimum contribution period of at least 12 months of paid employment in the four years preceding the unemployment spell.

**Figure 2.15. Self-employment represents a sizable share of employment in Switzerland**

Self-employment, % of total employment, 2019 or latest available year




Source: OECD Annual Labour Force Statistics database.

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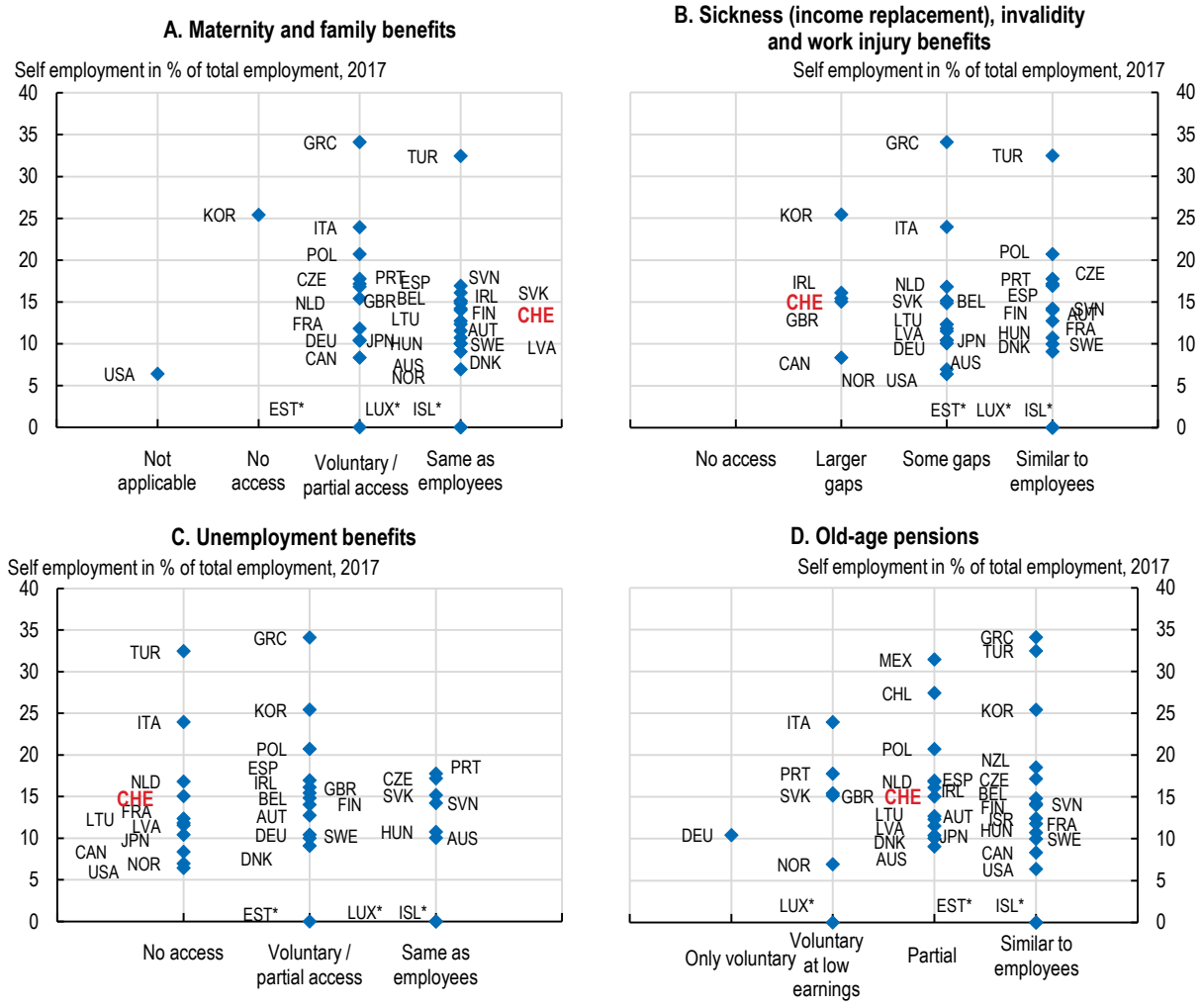
Unlike the STW scheme, the compensation for loss of earnings for the self-employed did not exist before the crisis and is expected to remain temporary. This is warranted, as perpetuating the scheme within its current design would raise important equity and moral hazard issues. Still, setting up a more permanent mechanism targeted at this group of workers could ensure a more equitable provision of employment and social protection to workers irrespective of the form of their employment, as emphasised in the new OECD Jobs Strategy. Already before the pandemic, a number of countries, including Austria, Canada, France and Spain, extended entitlement to unemployment benefits to self-employed workers. In cases where the distinction between dependent employment and self-employment becomes more blurry, and where the

transitions from one status to another become more frequent (ILO-OECD, 2020), a harmonisation of social coverage across employment status could be warranted. This would also allow for the portability of social benefits across categories of employment, whereby built-up entitlements would not be lost in labour market transitions (OECD 2019d). Denmark, for instance, recently strengthened the portability of earned entitlements across different jobs and forms of employment (OECD 2020b).

## Figure 2.16. Access to social protection is limited for self-employed workers

Statutory access to social protection for the self-employed, compared to dependent employees by social protection branches, 2017




Note: Gaps between standard dependent employees (full-time open-ended contract) and self-employed workers. "Partial access" to benefits can arise if a) eligibility conditions, benefit amounts or receipt durations are less advantageous for self-employed workers; b) insurance-based and non-contributory benefits co-exist and individuals can access only the latter (e.g. only basic pension and not earnings-related); or c) the self-employed can choose to declare a lower contribution base while dependent employees pay contributions on full earnings (possibly subject to a ceiling). "No access": compulsory for dependent employees but self-employed are excluded. * Data on self-employment incidence is missing/incomplete for Estonia, Iceland and Luxembourg and refers to 2015 for the Slovak Republic and to 2014 for Latvia.
Maternity and family benefits: "no access": access to neither maternity benefits nor family allowances, "voluntary/partial access": voluntary or partial access to both schemes, or full access to one, but no access to the other. "Not applicable": schemes do not exist.
Sickness, invalidity and work injury benefits: "no access": "no access": access to none of these benefits, "larger gaps": less than full access to all of the benefits and no access to at least one; "some gaps": no access to one benefit and at least partial access to the others, or voluntary or partial access to all three benefits; "similar to employee": at least partial or voluntary access to all benefits, and at least full access to one.
Old-age pensions: "voluntary at low earnings": coverage is generally similar to employees but opt-out is possible if earnings are below a certain threshold. "Similar to employees": mandatory coverage as for employees but contributions may still differ.
Source: OECD (2019d), OECD Employment Outlook 2019: The Future of Work, OECD Publishing, Paris. https://doi.org/10.1787/9ee00155-en.

StatLink https://stat.link/9vjkp4

At the same time, extension of the unemployment benefit coverage to the self-employed comes with significant policy challenges. It raises moral hazard issues as it is difficult to assess whether their unemployment is involuntary and to evaluate earnings losses. Also, higher volatility of self-employed earnings relative to employees makes the calculation and collection of contributions more challenging. The administrative burden is another obstacle that can deter self-employed workers from participating. Moreover, for low-income self-employed workers, the need to shoulder both the employer and employee share of contributions may be challenging (ILO-OECD 2020, OECD 2018f).

To deal with these challenges, some lessons can be drawn from international experience. Acknowledging the diversity of situation of self-employed workers, a number of countries have set voluntary schemes for unemployment protection. The experience of Sweden and Austria shows that these schemes tend to be prone to adverse selection and rarely lead to substantial levels of effective coverage and protection (OECD, 2018g and ILO-OECD 2020). In this context, a mandatory contribution could be considered, with appropriate mechanisms in place to support the participation of those with lower contributory capacity. In South Korea, for instance, the issue was addressed by subsidising contributions for low-income self-employed workers. In Switzerland, the difference in contributory capacity of self-employed workers is already taken into account for some social protection segments (the first pillar of old-age pensions and invalidity insurance and maternity insurance) with their contribution rate depending on annual earnings and ranging from about 5.4% to 10%. However, in designing such policy, care should be taken to ensure equal treatment of employees and the self-employed. This could be achieved, for example, by lowering the contribution rates of low-wage employees. Moreover, allowing for interruptions or delays in contribution, as in Korea, could help deal with the higher volatility of self-employed workers earnings. The moral hazard raised by the difficulty to control the activity and income of self-employed workers who claim unemployment benefits can be addressed by requiring them to close their business before making such a claim as in Sweden or Denmark. In Belgium, only self-employed workers whose company went bankrupt or who had such a low income from self-employment that either their social security contributions were waived or they did not reach a minimum earning threshold for two years are entitled to benefits (OECD, 2018g).

### *Boosting active labour market policies*

Active labour market policies (ALMPs) are an important element for labour market resilience by helping displaced workers find jobs more quickly and through effective matching of jobseekers with emerging job opportunities. During the early waves of the pandemic, the rise in unemployment and the pervasive use of the short-time working compensation (STWC) scheme in particular posed major challenges to benefit administrators and employment services in managing the vast volume of incoming support claims. Still, Switzerland is one the few OECD countries which had a mechanism in place before the COVID-19 outbreak to tackle a potential crisis on the labour market. This proved very useful in dealing with the emergency (OECD 2021a).

Public employment services budgets are directly linked to the number of registered jobseekers in cantons and can be adjusted during the year. This flexibility enabled a swift increase in human resources in 2020 to support public employment services. Staffing levels are estimated to have increased by more than 10% (OECD 2021a), helping to respond to the growing demand from jobseekers.

Labour market and activation policies are highly decentralised which can lead to higher responsiveness to local market needs (OECD 2020c). The cantons are responsible for local public employment services and for the administration of AMLPs for the unemployed. At the federal level, the State Secretariat for Economic Affairs (SECO) sets the basic policy parameters and is responsible for financing and administering some active labour market programmes as well as for advising and supervising cantonal PES. At the local level, the benefit and placement functions are separated between the unemployment-fund on the one hand, and the local employment services on the other hand. The unemployment funds are in charge of settling both unemployment benefits and the STWCs. Local public employment services (PES) offices carry out job

placement, refer clients to ALMP programs and monitor job-search requirements. In addition to federal AMLPs, most cantons also fund, design and implement their own labour market programmes.

While a decentralised framework of AMLP provision can boost responsiveness, it requires a well-designed national-level accountability framework to function successfully in the long term (Weishaupt, 2014). The main element of federal control is the publication of benchmarking outcomes for local PES performance, which is expected to exert peer-group pressure on local offices for continuous improvement of performance (Duell et al, 2010). These indicators give priority to a quick placement into a job but also evaluate the durability of the placement. Moreover, inter-cantonal sharing of experiences, in particular regarding good practices in terms of activation measures, is strongly encouraged by the Confederation.

The execution of labour policies and performance vary widely across cantons, despite the coordination instruments. With the gradual lifting of pandemic restrictions, additional efforts to diffuse good practices for active labour market programs as soon as they have been identified and to ensure that adequate strategies have been set up to boost jobs recovery would be warranted to give the unemployed in all cantons an equal chance of reemployment. Past evaluations highlight the importance of establishing a clear placement strategy for jobseekers in each canton as cantons where it was missing tended to underperform. The use of targeted measures for specific groups of jobseekers varies widely across cantons and could be more widespread as they are associated with more positive outcomes in terms of placement (Federal Council, 2016).

During the crisis, many job placement services across OECD economies moved on-line to comply with distancing requirements and technology utilisation was scaled up at an unprecedented pace. Such move represents a unique opportunity for PES to expand digital services more permanently to better serve their customers in the post-pandemic world. Some services that were only available face-to-face before the pandemic can now be accessed remotely, including job-search assistance, counselling and career guidance. Switzerland should build on these investments to further improve the efficiency of PES processes and facilitate their access. Appropriate support should also be provided to clients without digital skills or with complex needs, including basic IT training to navigate PES e-services. Classroom training has also been delivered online, but more could be done to expand access and coverage. At the same time, PES should retain some face-to-face capacity to ensure continued support to clients without digital skills or with complex needs.

The Swiss PES system puts a strong emphasis on the job-search requirement for the unemployed to be eligible for the unemployment insurance and gain access to services. In normal times, jobseekers need to present at their monthly face-to-face meeting with their counsellors proof of their job applications during the past period. Their unemployment benefits can be temporarily reduced if they cannot provide such evidence. The job-search requirement was temporarily delayed and adjusted during the peak of the crisis but reintroduced in its original form in autumn 2020. The incidence of benefit sanctions in case of non-compliance is also comparatively high. While these measures have proven useful in the past to raise re-employment (Federal Council, 2016), they may be less effective in time when jobs opportunities are limited. In this context, a stronger emphasis on measures aiming at boosting hiring and promoting the mobility of workers, including the beneficiaries of the STWC could be envisaged.

Evidence from the global financial crisis suggests that hiring subsidies can boost job growth and be cost effective (Cahuc, Carcillo Le Barbanchon, 2018). They need to be well targeted to be cost effective and adequately support groups in need. Many OECD countries, including Australia, France, Italy and the United Kingdom, have recently introduced or renewed such measures. Several employment incentives exist in Switzerland that could be further developed. In the intermittent pay scheme, for instance, a wage subsidy is paid to registered unemployed persons if their wage or income from a new job is lower than their unemployment benefit. Past evaluations have found that the scheme worked particularly well for long-term unemployed, young, low skilled and hard-to-place jobseekers (Duell et al, 2010, Wunsch 2021). Temporary job-insertion allowances is another available tool. It is paid to employers who hire jobseekers that

previously encountered difficulties in finding employment. Start-up incentives could also be boosted to encourage take up of self-employment. A substantial body of evidence shows that new companies account for a large share of job creation (Criscuolo, Gal and Menon, 2014, Haltiwanger, Jarmin and Miranda, 2013). Currently, support is only available for the planning and preparation phase but not for the start-up phase itself (Duell et al, 2010).

### *Fostering geographical mobility*

With only 1.7% of residents having moved residence to another canton each year on average from 2015 to 2019 according to the Federal Statistical Office data, inter-cantonal mobility is low. In comparison, 2.5% of the OECD population changed their region of residence per year, on average, between 2015 and 2018 (OECD 2020h). Linguistic barriers as well as differences in schooling, tax systems and regulations lead many workers to commute rather than change canton of residence in spite of federal authorities' efforts to harmonise cantonal laws. As a result, in 2019, 9.5% of the employed population in Switzerland had a one-way commuting time of one hour or more to reach work, compared to 7.7% on average in the EU according to Eurostat data.

With differentiated impacts of the crisis across regions and territories, facilitating geographical professional mobility could help better match labour supply and demand and foster recovery. Further steps could be taken to facilitate mobility. For instance, the nationwide mobility of licensed professionals is guaranteed by the Law on Internal Market, but in practice, cantonal restrictions and administrative barriers have been frequently observed, especially regarding access to jobs for healthcare specialists (ComCo 2020, OECD 2019a). Linkages between eligibility for cantonal social benefits and length of residency should also be reviewed (i.e. the required length shortened), to avoid lock-in effects. In the Vaud canton, for example, households need to have lived in the canton over the last three years to be eligible for supplementary family benefits. Five years of residency are required in the canton of Geneva. Administrative barriers can also weigh on mobility of foreign workers. Cantonal legislation requires a minimum residence period of between two and five years in the canton or municipality before foreign nationals can apply for naturalisation. Furthermore, the acquisition and use of land and real estate by foreigners is highly restricted (OECD, 2020d).

High housing prices in Switzerland are also likely to hinder residential mobility. In principle, the high rate of renting in Switzerland – almost 60% of households – should support mobility. However, Swiss tenancy laws restrict rent increases, so long-term tenants pay well below market prices (OECD, 2015). This generates lock-in effects, limiting workers' ability to adjust to changing job prospects and hampering downsizing of residency by older households. The tenancy law should be adjusted to minimise lock-in effects, accompanied by targeted housing allowances or additional social housing for low-income households (OECD, 2015).

## Making the labour market more inclusive

As discussed in the first section, the pandemic disproportionately affected low-income workers. With population ageing already constraining labour utilisation growth, Switzerland would benefit from bringing under-represented groups more effectively into the labour market, including by up-skilling them. Moreover, care needs to be taken that closures of schools, of training centres and of enterprises in the most affected sectors as well as widespread use of teleworking do not broaden inequities in education and weigh on young people's entrance on the labour market.

### *Addressing the gender income gap*

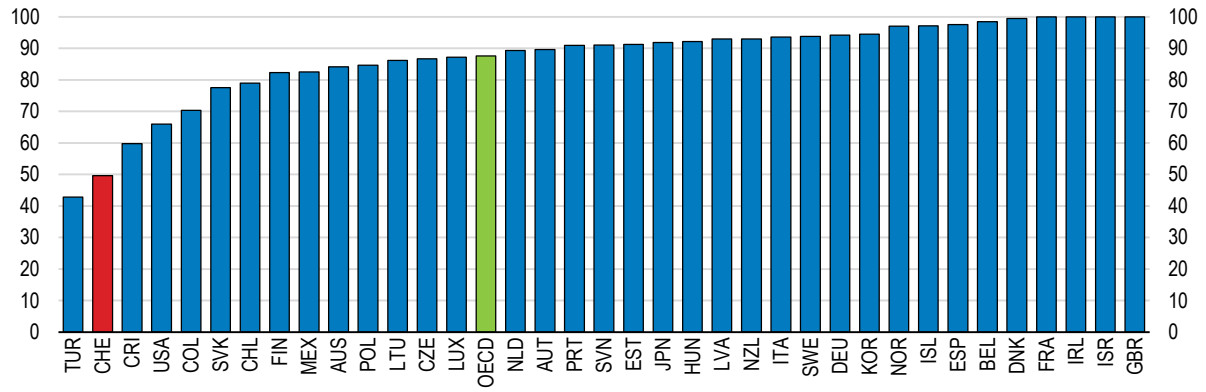
The sizable gender income gap and disproportionately high incidence of part-time work among women call for measures to address women's disincentives to work full time. The high cost of childcare, and low supply of early childhood education as well as an organisation of the school day that is not well aligned with working hours have long been reported as major reasons for difficulties of mothers to join the labour force

full-time (OECD 2017a, OECD 2013). Moreover, the income tax system leads to high marginal taxation of second-earner incomes, adding further disincentives to work.

Increasing the supply of affordable childcare remains a priority. In 2018, only 50% of children aged 3 to 5 years were enrolled in early childhood education and care, well below the OECD average of 87% (Figure 2.17). Since 2003, the government set up a dedicated program to expand childcare provision that is expected to end in 2023 and is estimated to have helped create 65 000 new childcare places. Potential remaining supply shortages are however difficult to assess in the absence of adequate estimates of demand. According to the social partners, they remain sizable (USS, 2021) and a recent policy brief from the Federal commission on family issues reports that children from disadvantaged families are significantly less likely to have access to childcare facilities (COFF, 2021). High income families use childcare facilities 50% more than low income households. A recent parliamentary initiative called for a more long-lasting financial support to parents and improvements in childcare services (SECC-N, 2021).

### Figure 2.17. Enrolment in early childhood education and care is low

Children enrolled in early childhood education and care services, 3 to 5-year-olds, %, 2018




Note: Data include children enrolled in early childhood education and care (ISCED 2011 level 0) and primary education (ISCED 2011 level 1).
Source: OECD (2020), "How do early childhood education systems differ around the world?", in Education at a Glance 2020: OECD Indicators, OECD Publishing, Paris, https://doi.org/10.1787/7e21871e-en.

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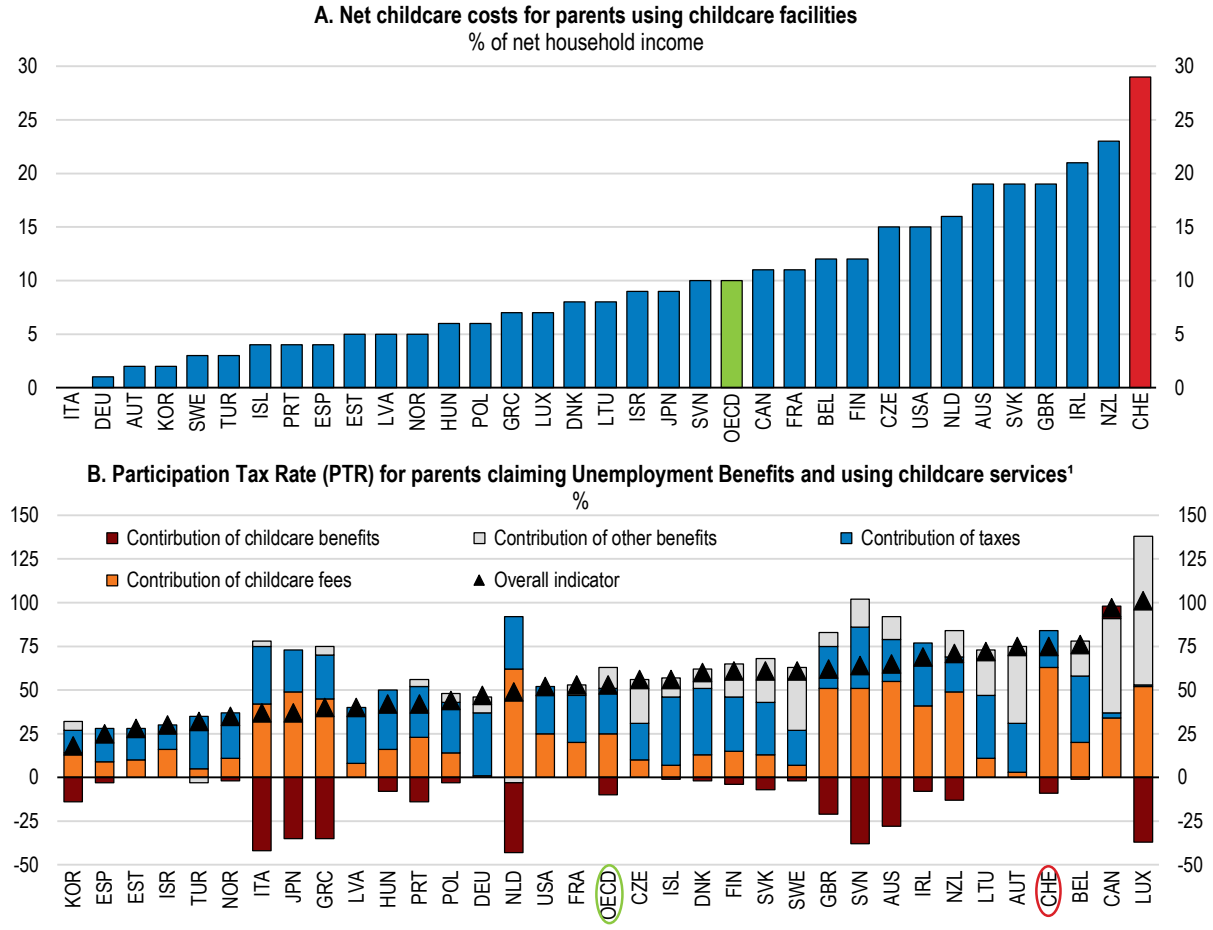
The OECD Tax-Benefit model indicates that net childcare costs (for parents using childcare facilities, after benefits designed to reduce gross childcare fees) are high. For a couple with two young children earning the average wage, the net childcare cost represented 29% of the net household income, well above the OECD average of 10% (Figure 2.18, Panel A). Adding to these costs the high marginal personal income taxation of second-earners associated with the current family-based income tax system leads to a very high participation tax rate (proportion of earning that is lost to either higher taxes, lower benefits and net childcare costs when a parent takes up a full-time job) for second earners, often women. For instance, for a family with two young children using childcare facilities, the cost for a second earner to move from inactivity (or long-term unemployment) to full-time employment (earning the average wage) represents 75% of the average wage, versus 53% on average in the OECD countries (Figure 2.18, Panel B).

Various mechanisms help reduce these costs but they generally remain elevated, and support measures are not well-targeted. The federal personal income tax system allows for a tax deduction for childcare fees charged by a third-party of up to CHF 10 100 and a tax deduction of CHF 6 500 per child irrespective of declared childcare costs (along with a tax credit of CHF 251 per child), but, with more than 40% of Swiss families not paying federal income taxes, this provision has little impact on childcare affordability for low income households. A government initiative to raise these tax deductions was recently rejected by popular vote owing to such equity concerns.

## Figure 2.18. The disincentives for second-earners to move to full time employment are very large

Couple with 2 children earning the average wage, 2020 or latest available year




1. This indicator measures the financial disincentives to participate in the labour market. It calculates the proportion of earnings in the new job that are lost to either higher taxes or lower benefit entitlements when a jobless person takes up employment and claims unemployment benefits. Higher values means higher financial disincentives.

Source: OECD Social Expenditure Database, http://www.oecd.org/social/expenditure.htm; OECD Family database, http://www.oecd.org/social/family/database.htm.

StatLink https://stat.link/692c4p

Families also receive cash benefits. Amounts vary across cantons but a nationwide legal minimum is set at CHF 200 per child per month. Cantons can complement these benefits by additional allowances or fee subsidies (that can be more specifically targeted towards low income households) but there is a large heterogeneity of cantonal policies in this regard. As a result, the proportion of childcare costs covered by parents varies widely across cantons (OECD 2021d). Further harmonising cantonal family policies would be a welcome step.

Providing fee reductions, childcare benefits or tax credits at the federal level rather than tax deductions would help increase childcare affordability without providing more generous support to better-off families. Moreover, targeting could be further improved by introducing income-tests on childcare benefits at the federal level (OECD 2020e). These transfers would need to be carefully designed and decrease with income only gradually to avoid creating large changes in marginal effective tax rates at thresholds and causing work disincentives. In Sweden, for instance, a maximum fee to be paid by parents as a percentage of household income is set at the national level while municipalities can set lower fees. With cantons responsible for the design of the personal income tax at the subnational level, adjustments may need to be done at both federal and cantonal level to ensure coherence of the taxation system.

Along with a higher number of affordable places in early childhood education and care, it is important to ensure quality. Evidence shows that early childhood education and care provides a crucial foundation for future learning and is important for success later in life, but much of the benefit crucially depends on the quality (OECD, 2018c, OECD 2017b). Early childhood education and care provision is quite fragmented in Switzerland. Different types of early childhood education and care providers are available (both centre-based and family-based) raising challenges with respect to ensuring consistency in quality. The responsibilities for regulations and standards setting and curriculum development are at the level of cantons, and consistency is not ensured across the nation. The government has developed a unified curriculum from birth to four years "the Orientation Framework for Early Childhood Education and Care" that helps set the basis for quality control but monitoring of its implementation is lacking (OECD 2021d). The authorities should ensure effective coordination and monitoring to safeguard quality across different providers, including by making sure that children benefit from equal learning and development opportunities. Ensuring a qualified workforce in the sector is also warranted, including by providing incentives for life-long professional development.

Reforming taxation of second earners to reduce disincentives to work is another avenue to boost female full-time labour participation. A popular initiative has been launched in 2021 calling for individual-based rather than family-based income taxation, as recommended in a previous OECD Economic Survey (OECD 2017a). Following a Parliament request, the Federal Council is also currently assessing various individual taxation models. Reducing the second earner marginal effective tax rate could also be achieved under the current, family-based, setting, for instance, by adjusting the marginal tax brackets for joint filers or providing tax deduction (or allowance) for the second earner.

The statutory federal paternity leave of two weeks is short by international standards. It has been recently introduced, which is a step in the right direction, but due to its short length, its impact on mothers' post-maternity reintegration into the labour force remains questionable. There is a wide heterogeneity of policies across OECD countries, but on average, the length of paid leave reserved for fathers is eight weeks. This is because many countries complement paternity leave with entitlements to paid parental leave or home care leave reserved to fathers, which are not available in Switzerland. Establishing a federal statutory parental-leave system (to be divided between parents) as in most European countries would provide additional support to mothers wishing to reintegrate into the labour force faster. For instance, for Denmark, Druedhal et al. (2019) found that the increase in earmarked leave for fathers led to shorter maternal leave and an increase in mothers' earnings for up to eight years after birth. While the results in terms of women labour market outcomes are more mixed for Sweden and Norway (see for instance Dalh at al., 2014 and Ekberg et al., 2013), Patnaik (2019) shows that in the province in Quebec, Canada, the introduction of parental leave reserved to fathers increased the likelihood for women to work full-time. Moreover, a number of studies shows that fathers who take more parental leave are more involved in children activities later on (see for instance Almqvist and Duvander, 2014 and Huerta et al. 2013) which could help change social norms in terms of parental task specialisation.

The large gender pay gap is not only due to the large incidence of female part-time employment. Even when working full time, women earn on average 19% less than men, one of the widest gaps in the OECD. According to the Federal Statistical Office estimates (FSO, 2021), about 45% of this gap cannot be explained by factors such as professional status, years of services, sector of activity or level of education. Moreover, this unexplained difference has increased since 2014.

A law was passed in 2018 that requires companies with over 100 employees to conduct regular gender pay audits and inform employees and shareholders of the results. While welcome, these measures do not help address gender pay gap in smaller enterprises where the FSO finds the largest unexplained wage difference. To raise awareness of the issue, the federal government launched in December 2020 the Logib 2 pilot initiative. The tool enables all employers to carry out a gender equal pay analysis and unlike its previous version, is suitable for smaller organisations and companies (from 2 to 49 while the initial Logib tool could only be used by firms with more than 50 employees). The government could collect these data

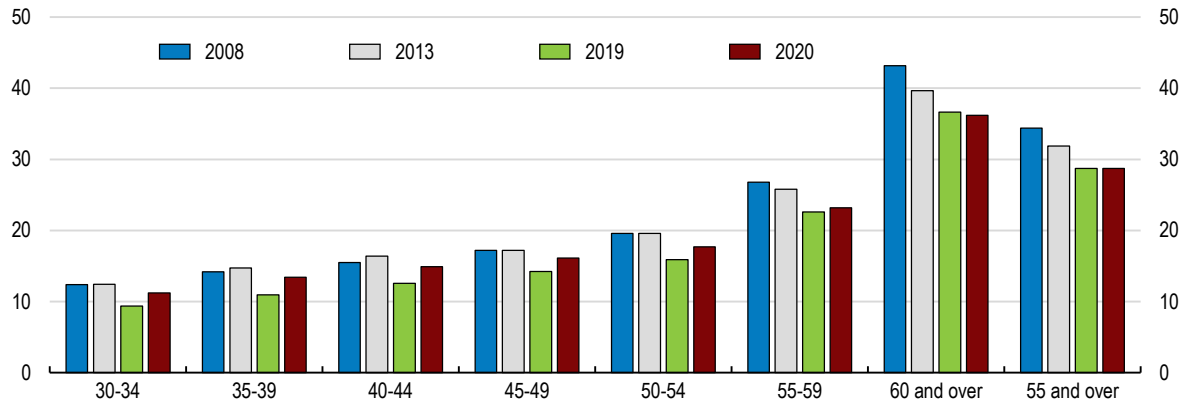
and set-up a salary comparison website for workers in domestic firms to raise awareness of gender discrimination and facilitate corrective actions. Korea, for instance, has recently introduced this type of website, which shows salary brackets of private sector employees according to six criteria – firm size, type of business, occupation, job career, gender and academic background (OECD, 2020g).

### *Supporting the employment of older workers*

The rise of unemployment among workers aged 55-64 since the beginning of the pandemic raises concerns. Once unemployed, older workers find it more difficult than prime-age workers to reintegrate into the labour market (SECO 2019a, SECO 2021). The risk of long-term unemployment is accordingly significantly higher for older workers (Figure 2.19). Swiss cantonal employment offices identify a number of barriers to reemployment of workers aged 50 or more: employer's preferences, high reservation wages, employees' lack of confidence or skills to effectively search and apply for jobs, narrow specialisation, weak computer skills and health status (Egger, Dreher and Partner AG, 2019).

**Figure 2.19. Incidence of long-term unemployment increases with age**

Incidence of long-term unemployment (1 year and over) by age group, %




Source: OECD calculations based on SECO.

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To support older workers' re-employment, the authorities launched a reform package that includes additional spending on activation policies for older workers. New measures include a pilot program for 2020-2021 providing free situation analysis and career guidance for workers aged 40 and over that should be extended to all cantons over 2021-2024. While in Switzerland people are not granted access to activation policies funded by the unemployment insurance for two years after the expiration of their unemployment benefit entitlements, an exceptional access to training is granted for jobseekers aged over 50. Additional funding is also allocated to cantons for 2020-2024 to enable them to better support hard-to-place jobseekers, especially seniors, with more individualised measures such as counselling, coaching or mentoring. While welcome, these reforms are only temporary. An assessment of their efficiency should be carried out to expand them if they bring positive results.

The Federal Act on Transition Benefits for Older Unemployed persons was adopted by parliament in June 2020 to supplement these activation policies. Starting in 2021, it introduces transition benefits up to retirement for individuals aged 60 or over who have exhausted their unemployment benefits. These benefits are means and asset tested. Eligibility conditions also require at least 20 years of contributions to the pension scheme of which at least five years after the age of 50. Still, the scheme risks reducing incentives for eligible people to undertake training and to search for work before reaching the age of 60. Such effects have been observed in Finland (OECD, 2018d) and Poland (Gałecka-Burdziak and Góra, 2017). Supplementing eligibility conditions with requirements to participate in community services or continue looking for a job would mitigate this risk.

Financial disincentives for employers also weigh on the employment of seniors. As in many OECD countries, wages rise with seniority, raising the risk that older workers' wages grow above their productivity. In Switzerland, the salary gap between workers aged 55-59 and workers aged 25-29 in full employment is above the OECD average (OECD 2014). Moreover, minimum contributions to the second-pillar pension funds rise with age, with employers paying at least half of them. Currently, the contribution rate represents 7% of the insured salary for the 25-34 age group, 10% between 35 and 44, 15% between 45 and 54 and 18% for older workers. This creates disincentives to hire older workers.

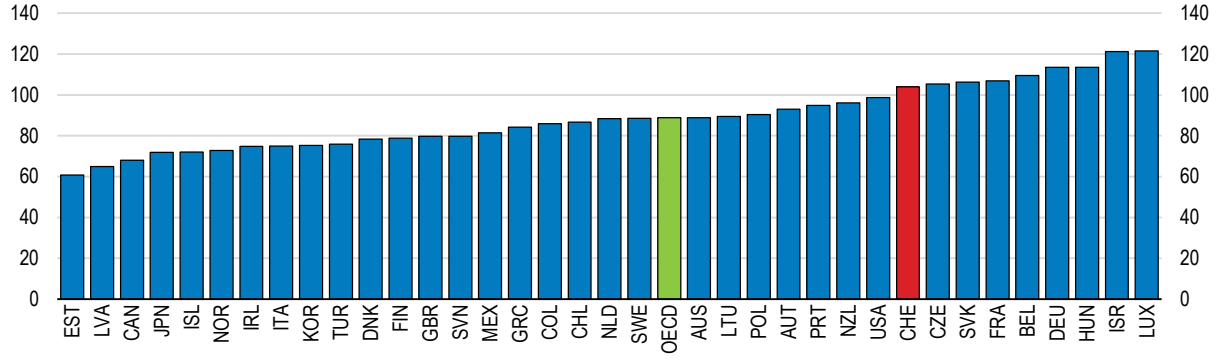
Ways to introduce greater flexibility to the pay system should be discussed with social partners. In Korea, for instance, where seniority has a large impact on wages, the authorities have worked with social partners to develop new criteria and better connect wage-setting practices with job requirements and skills (OECD 2018e). In 2020, the Federal Council proposed a reform of the second pillar inspired by an earlier proposal of three out of four main social partners which includes a provision to flatten the contribution rates. Only two different contribution rates would be maintained, at 9% for workers aged 25-44 and at 14% for older workers. For workers aged 55 and over it would lead to a significant decline in the contribution rate, a welcome development to improve their employability. An alternative way to achieve this goal would be to adjust employers' contribution to a flat rate so that only employees' contributions increase with age.

### *Raising skills and lowering inequities in education*

Switzerland has a comparatively well-educated and skilled population, but inequities in education were a concern even before the pandemic. The latest Programme for International Student Assessment (PISA), in 2018, pointed to similar or above OECD average performance of 15-year old students in the three tested competencies - reading, numeracy and science proficiency – but also to a significant gap in performance between socio-economically advantaged and disadvantaged students in reading (Figure 2.20). With a difference in score of 104, the gap is larger than in the OECD on average (89), and has widened over the last decade (OECD 2018e). School principals report less staff shortages and material shortages than the OECD average but disadvantaged schools, where disadvantaged students tend to be more often clustered (OECD, 2017a), are more likely to experience teacher shortages.

**Figure 2.20. Performance in reading varies widely across socio-economic groups**

Gap in reading performance between advantaged and disadvantaged groups, score difference, 2018




Note: A socio-economically advantaged (disadvantaged) student is a student in the top (bottom) quarter of ESCS (PISA index of economic, social and cultural status) in his or her own country.
Source: OECD, PISA 2018 Database, Table II.B1.2.3.

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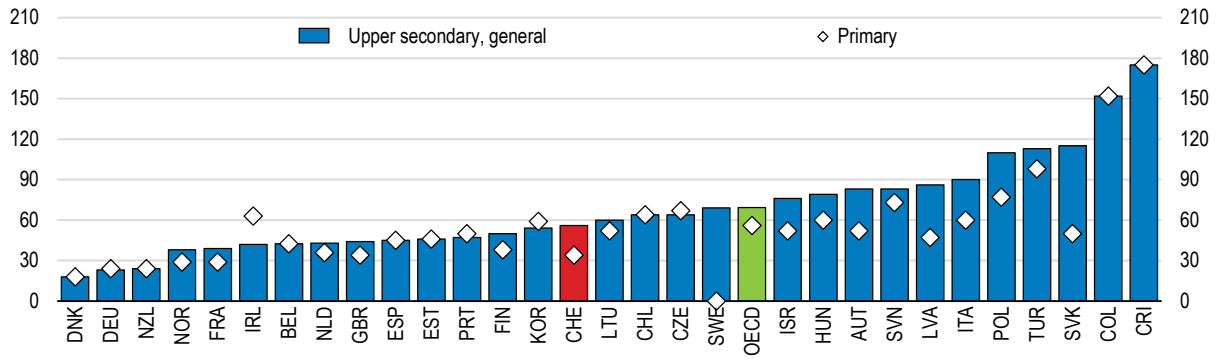
The COVID-19 crisis has reinforced inequities in education as students from disadvantaged socio-economic groups are more vulnerable to learning losses during school closures. They are not only less likely to have access to a quality education, but they are also less likely to benefit from digital infrastructure, a quiet place to study and a supportive environment for effective distance learning (OECD 2021c). In Switzerland, during 2020, schools were closed for about 35 instruction days in primary education and 55

instruction days in secondary education, below the OECD average (Figure 2.21). Indeed, during the pandemic, the Swiss government placed a high priority on face-to-face teaching, especially for younger students. Still, learning losses can be substantial. Based on the results of an online survey conducted in Austria, Germany and Switzerland, Huber and Helm (2020) find that a sizeable portion of students reported learning at home during the first two weeks of the lockdown for at most two hours per day. Across the OECD economies, a number of studies point to a large variation in children's learning experience during school closures across family income and parents' education (Stantcheva 2021). In the Netherlands for instance, Enzgell et al. (2020) find that learning delays were much more pronounced among students with less educated parents. In the United States, Chetty et al. (2020) document a large divide in progress for math lessons completed online across income groups with the gap growing over time.

### Figure 2.21. The pandemic crisis led to widespread closure of schools

Number of instruction days where schools were fully closed, 2020




Note: Data for United Kingdom refer to England only. Most typical number of instruction days for Colombia, Germany, Italy, New Zealand and Slovak Republic. Minimum number of instruction days for Denmark.
Source: OECD/UNESCO-UIS/UNICEF/World Bank Special Survey on COVID. March 2021.

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School closures during the pandemic further raised awareness of these inequalities. Many OECD countries, including Switzerland, took action during the crisis to improve inclusiveness in distance education (OECD 2021c). This included flexible and self-paced digital platforms, agreement with mobile communications operators and internet firms to enhance access and provision of additional economic support to lower-income households. However, and in contrast with most OECD countries, in the survey on Joint National Responses to COVID-19 School Closures Switzerland did not report any measures to assess gaps in student learning accumulated during the schools closure nor remedial measures to address gaps (OECD 2021c). In France, for instance, the initiative Devoirs Faits, which supports students with completing their homework through dedicated time at school, was strengthened in September 2020 to support students with educational challenges during the pandemic. The results of experiments of free individual tutoring online for disadvantaged middle school students in Italy and online peer-mentoring for university students in Germany are encouraging. They significantly improved student academic performance, studying behaviour and motivation (Stantcheva, 2021). Such interventions could be experimented in Switzerland through pilot programs as they could be beneficial even after the crisis, allowing children from disadvantaged socio-economic background to have access to extra time, mentoring and support.

The Swiss education system is renowned for its high focus on vocational education and training (VET) and emphasis on apprenticeship training. With more than two thirds of Swiss young people (aged 15-20) enrolled in the VET system, the impact of the crisis on the apprenticeship market became a major concern. Students in the vocational stream can sign-up for a two- to four- year apprenticeship after completion of lower-secondary school. Potential apprentices go through a recruitment process and a training contract is drawn up between the apprentice and the firm offering the apprenticeship, a necessary pre-condition to

start the VET program. The programme typically involves a dual engagement of practical work and study (OECD 2017a). This means that the crisis affected apprentices' training via two major channels, the closure of vocational training centres and the closure of firms in the most affected sectors. In addition, the widespread use of teleworking may have made training in the workplace more difficult and less effective as practical aspects of the training could not be delivered.

Despite the pandemic and the slowdown in the labour market, early-2021 data shows that Switzerland has been quite successful in supporting matches between firms and students. By end-February 2021, a third of the students looking for an apprenticeship for the summer 2021 had already signed a contract, a share comparable to previous years (SERI 2021). Government measures supported this outcome. Virtual outreach has been reinforced, including through the development of online job markets. The federal authorities have also created a specific program (Apprenticeships COVID-19) that helps finance measures in favour of apprentices' insertion in the labour market. The Confederation funded up to 80% of the costs of these measures with expenditures amounting to CHF 23 million as of October 2021. Targeted areas include applicants' mentoring or coaching and development of new training models in sectors affected by the closure of many businesses. Financial support can also be requested by firms, to create positions or maintain existing contracts. Earlier in the crisis, the resilience of the apprenticeship system was also supported by enlarging the eligibility of the STWC to apprentices. On the other hand, and in contrast to some other OECD economies, Switzerland does not report specific measures targeted to the vocational and training system to assess or make up for the potential learning gap (OECD 2021c). In Estonia, for instance, vocational students benefited from additional study time. Expanding the duration of programs could also be considered for apprenticeships in the most affected sectors. In South Korea, for example, an extension of the training period or flexible training time has been allowed (OECD 2020f).

Going forward, technological change and increased digitalisation is a major challenge for vocational and educational training (VET) systems as it alters patterns of demand for both technical skills and key competencies. Technological progress puts a number of jobs at risk of disappearing due to automation (Vandeweyer and Verhagen, 2020), while creating new job opportunities. With workers likely to change tasks and occupation more frequently over a longer work-life span, a strong grounding of cognitive skills becomes more important. To some extent, the Swiss VET system is well-positioned to address this challenge as a number of extensions of the curriculum and flexible education pathways offer opportunities to vocational students to gain higher qualifications including through tertiary education. As a result, about one third of young VET graduates work in high-skill occupations, a share significantly above the European average of 18% (Vandeweyer et al, 2020). However, a majority of apprentices do not choose the path to tertiary education and overly narrow specialisation of VET students could become a concern. While an obvious solution would be to reinforce the academic component in VET upper-secondary curricula, it may have some detrimental effects on the motivation of students (Vandeweyer et al, 2020, OECD, 2017a). It is therefore crucial that VET graduates have continued opportunities to up-skill and re-skill after entering the labour market.

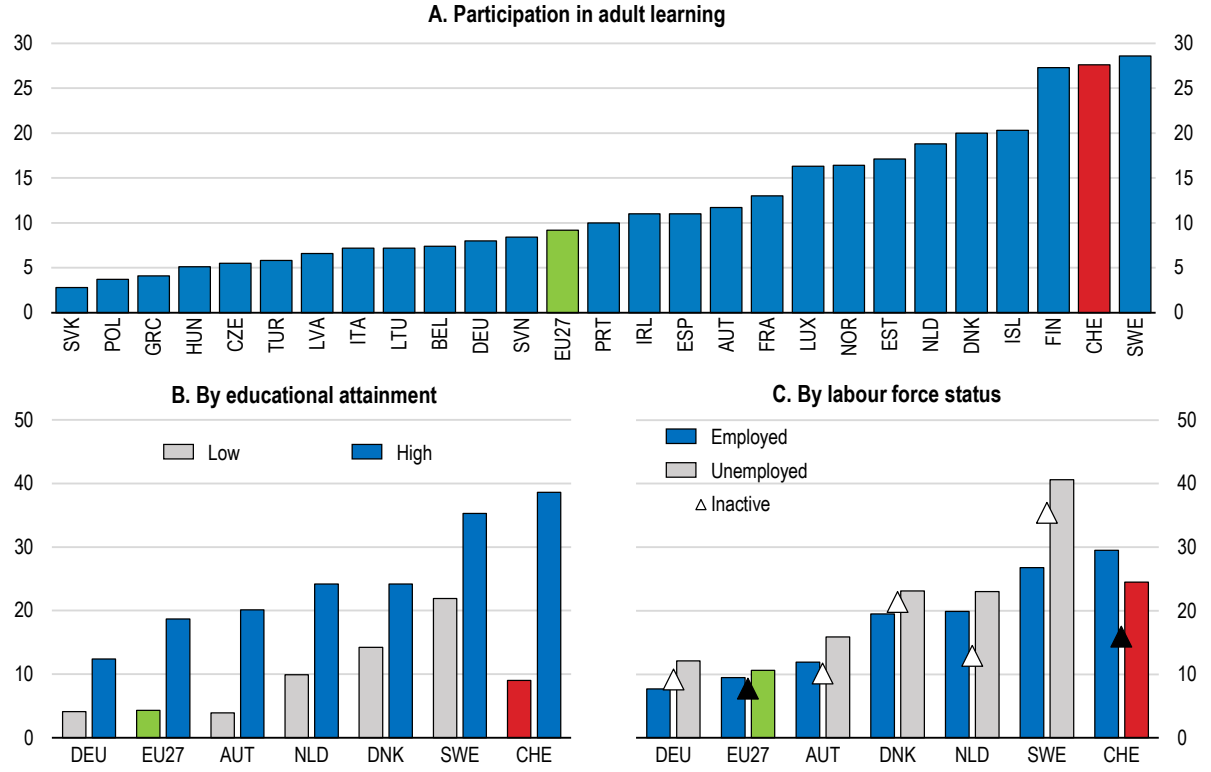
With evolving skills demand, the necessity to offer opportunities for adult learning is not only pressing for VET students but also for less qualified workers. While participation rate in life-long learning in Switzerland is one of the highest among European countries, the participation rate is significantly lower for groups of workers with less education or out of work (Figure 2.22). The pandemic has accentuated this pattern: while the decline in participation affected all groups of workers (compared to 2019, participation declined by 18% in 2020 for the 25-74 aged resident population) it was more pronounced for people with secondary education or lower. Recent data also point to a disproportionately high decline in participation for older workers (FSO 2021b). With lower digital skills than younger workers (Figure 2.23), they may have been less able to benefit from virtual training during the pandemic.

The Continuing Education and Training Act, which came into force in 2017, provides a framework for government action in broadening access to adult education. Through this law, the federal government co-finances cantonal programmes for the promotion of basic skills for adults. A recent initiative of the

government ("Simplement mieux!... au travail") subsidises employer-provided training in basic skills training, including IT. It should help better target adult learning toward low-skill workers. Subsidies or vouchers for targeted groups could also be considered. Such initiatives are already implemented at the cantonal level. Twenty-one cantons have established basic skills promotion programs which provide subsidised training opportunities for all adult residents.

## Figure 2.22. Participation in adult learning is high but should be broadened

Percentage of population aged 25-64 participating in education and training during the last 4 weeks, 2020




Note: Includes formal as well as non-formal education and training. The reference period for the participation is the four weeks prior to the interview. Low education refers to below upper secondary education (ISCED 0-2) and high education refers to tertiary education (ISCED 5-8).
Source: Eurostat database.

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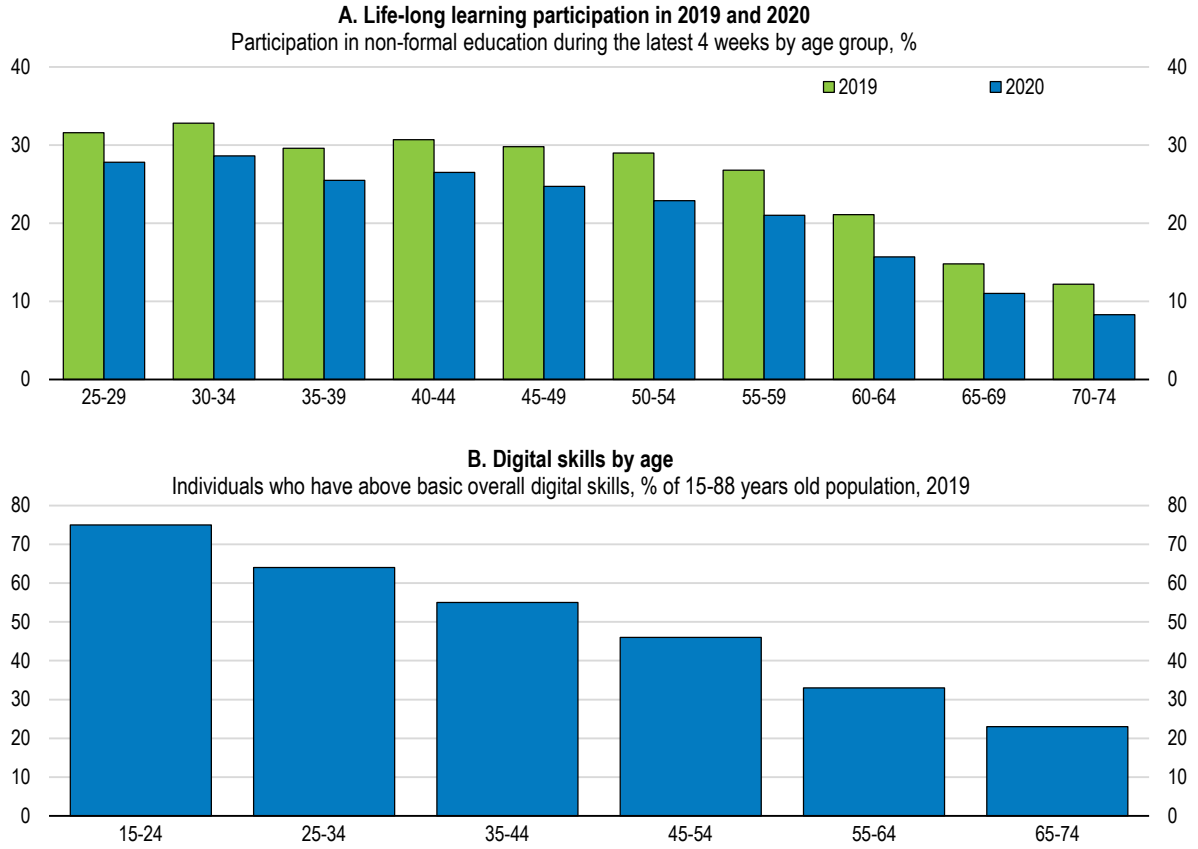
**Figure 2.23. Participation in life-long learning has declined during the pandemic, especially for older workers who tend to have lower digital skill**




Source: FSO, Swiss Labour Force Survey (SLFS), FSO, Omnibus TIC survey.

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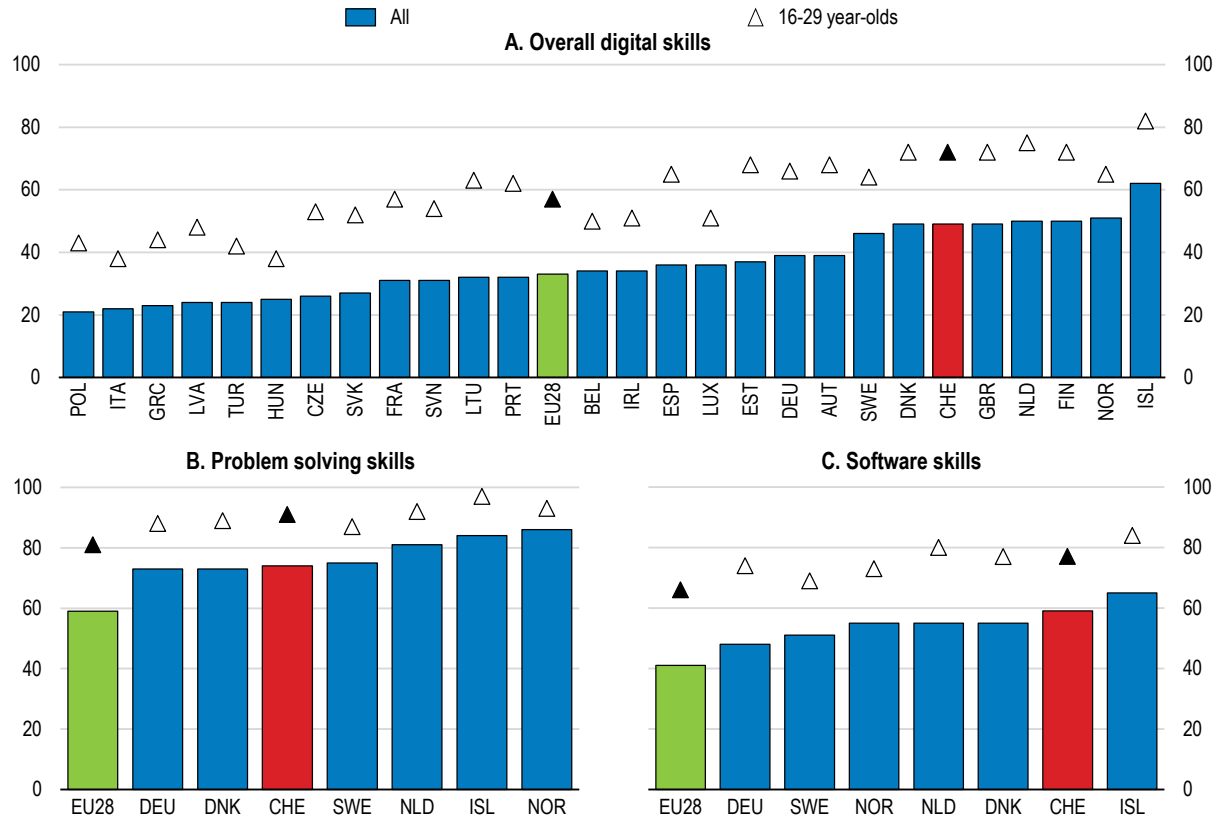
For all workers, raising intermediate and advanced digital skills will be essential to foster stronger productivity growth. ICT-related sectors displayed high vacancy rates before the pandemic and their activity has rebounded sharply after the ease of restrictions. The advanced IT-related skills of Swiss adults are comparatively high, especially for young people, but lag top performers (Figure 2.24). Raising the number of graduates from scientific and technical fields would help address shortages in the medium term. This would require encouraging female participation in these fields which tends to be very limited (OECD 2017a). Moreover, as mentioned in the previous surveys (OECD 2017a, OECD, 2019a), easing immigration requirements from non EU-countries would also help limit skills shortages. Swiss university graduates from non-EU countries, for instance, have only 6 months to find a job after completing their studies to be allowed to stay in Switzerland. According to Economiesuisse, the Swiss Business Federation, only 10-15% of these students remain in the country after their studies. The Swiss parliament has recently given the Federal Council a mandate to facilitate the stay in Switzerland and access to the labour market for third-country nationals with Swiss university degrees in areas with a proven shortage of skilled workers.

## Figure 2.24. Swiss adults' digital skills are solid but lag the top performers

Share of the population with more than basic skills, %, 2019




Source: Eurostat, Digital Skills database [isoc_sk_dskl_i].

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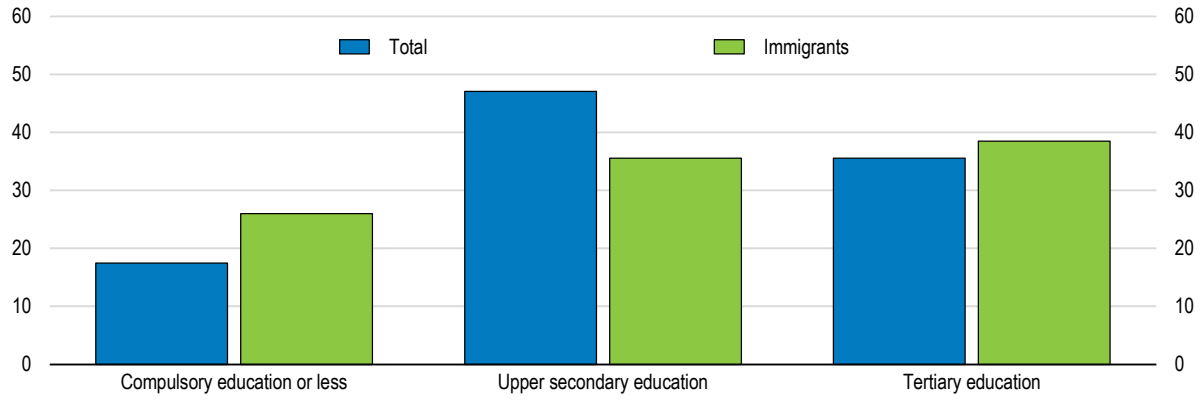
Better integrating immigrants into the labour market is essential to foster labour force participation and productivity by better harnessing their skills. Immigrant population represents about a third of the permanent resident population aged 15 and older and is highly heterogeneous in terms of educational attainment. Immigrants are much more likely than natives to have only completed mandatory education but also slightly more likely to have a tertiary education degree (Figure 2.25 and FSO, 2020). With few jobs suited to those with low education and skills in the Swiss labour market (see chapter 1, Figure 1.15, Panel B), the unemployment rate is substantially higher for immigrants who have only completed mandatory education (8% in 2018 compared to 5% for immigrants with upper secondary education and 4% for immigrants with tertiary education). Upskilling low-skilled immigrants is therefore essential to reduce inequalities in the labour market and strengthen labour utilisation in the economy.

Providing migrants with vocational and educational training is also an important avenue towards better labour force integration. Cantons offer pre-VET programmes to young immigrants to help them acquire needed core competencies, including language skills, to enrol in VET programmes. However, an age limit (21 to 23 years) for accessing these programmes is set, limiting the opportunities for older migrants to enter VET. This issue was partially addressed in 2018 when Swiss authorities launched a pilot pre-VET programme specially targeted to refugees with a higher age limit, to up to 35 years. Refugees represent only 4% of all foreign residents in Switzerland but face significant challenges to enter employment as many of them do not speak the local language and have acquired little school education. Early evaluation of the programme shows positive results with two third of the students continuing training in a certifying VET

programme (Cedefop/OECD, 2021). In this context, authorities should pursue the initiative and consider extending it to a larger group of migrants by raising the age limit for access to pre-VET programmes.

### Figure 2.25. Immigrants have heterogeneous educational attainment

Education attainment by group of population, % of population aged 15 years and older, 2019




Source: FSO, Swiss Labour Force Survey (SLFS).

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Broader and faster recognition of foreign qualifications would also facilitate immigrants' integration into the labour market and potentially reduce skill-mismatches. To get a certified VET qualification in Switzerland, it is possible to ask for validation of prior formal or informal learning at the cantonal level but the process is long and cumbersome. It requires language skills as a comprehensive validation dossier must be compiled, so that professional experts can assess the equivalence of competencies. Moreover, validation procedures only exist for 20 of about 230 initial VET qualifications and are not offered in all cantons (Cedefop/OECD, 2021). Therefore, regular or shortened apprenticeships are often easier and quicker ways for many adult refugees to get VET qualifications certified (Spadarotto, 2019). Measures to simplify the recognition process of foreign qualification would improve efficiency.

| Main findings | Recommendations |
|---|---|
| **Facilitating job reallocation** | |
| **The extensions to the short-time working compensation scheme during the pandemic have adequately protected workers and firms but risk hindering job reallocation and restructuring during the recovery.** | **Once most restrictions are lifted, scale back the short-time working compensation scheme and reintroduce firms' financial participation to the costs of the scheme.** |
| Workers on short-time working compensation scheme have a higher risk of losing their job and they increase their job search efforts. Follow-up of their situation by the public employment services is hampered by the lack of information on beneficiaries. | Collect more information on the beneficiaries of the short-time working compensation scheme to enable more effective follow-up of their situation by the employment services. Promote the voluntary registration of workers on protracted spells of short-time working compensation scheme to public employment services and provide incentives for training. |
| Active labour market policy programs are well provisioned and flexible but display large differences of placement outcomes across cantons. | Ensure that cantonal strategies to boost job recovery are developed.<br>Strengthen active labour market policies at the cantonal level by promoting good practices for efficient job placement of targeted groups. |
| Long-term unemployment is rising. In crisis time, financial incentives have proven especially effective to improve employment prospects of long-term unemployed workers.<br>Administrative barriers and lock-in effects due to strict rent controls weigh on geographical mobility. | Expand the use of financial incentives to facilitate the return to jobs of unemployed workers.<br>Foster geographical mobility by adjusting the tenancy law to reduce restrictions on rent increases, accompanied with targeted housing allowances.<br>Reduce barriers to internal mobility of licensed professionals. |
| **Increasing labour market inclusion** | |
| **The gender income gap is high in Switzerland, in part due to high incidence of part-time employment. The interplay between the tax and benefit systems and a high cost of childcare result in lower working hours and lower labour incomes for women.** | **Keep expanding the supply of childcare and provide targeted measures (mean-tested fee reductions, childcare benefits or tax credits) to improve affordability.**<br>Ensure effective quality control of childcare providers' services.<br>**Reduce disincentives to work for second earners, by moving from family-based to individual-based taxation or through tax adjustments and slower withdrawal of benefits.**<br>Expand paternity leave with a statutory parental leave system with entitlement reserved to fathers. |
| Once unemployed, older workers have more difficulties than prime age workers to find a job due to narrow specialisation and lack of job search experience. Rising pension contribution rates with age also plays a role. | Flatten the age-related progressivity in pension fund second-pillar contribution rates.<br>Assess and, if effective, scale-up pilot activation programs for older workers. |
| **Raising skills and lowering inequities in education** | |
| **Students from a disadvantaged background are significantly more likely to underperform and less likely to graduate with a tertiary degree.** In addition, school closures and distance learning during the pandemic are likely to have disproportionally affected disadvantaged students. | **Improve access to early childhood education and care for low-income households.**<br>Assess learning gaps that occurred during the pandemic and provide remedial measures targeted to disadvantaged students. |
| Immigrants' unemployment rate is more than twice higher than Swiss natives and a relatively higher share of migrants did not study beyond mandatory school. | Broaden access to programmes aiming at providing pre-vocational education and training qualifications to low-skilled migrants by increasing the age limit to participate.<br>Simplify and speed-up the process for recognition of foreign qualifications. |
| Switzerland faces shortages of skilled labour, including in the ICT sector. | Ease non-EU immigration restrictions and allow non-EU students more time to search for a job in Switzerland after completion of their studies. |

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# SWITZERLAND

The Swiss economy has shown resilience but the COVID-19 pandemic continues to raise uncertainty and challenges. Effective government support has helped protect employment and buttress household incomes. Nevertheless, some sectors and groups have been hit hard, with a disproportionate impact on low-middle skilled and low-wage workers. Fostering productivity growth is crucial to maintain high living standards in the future. Switzerland is one of the top OECD performers in terms of labour productivity, but productivity growth has slowed markedly over the past three decades. Lower barriers to free and open competition within the internal market and continued openness to international markets would spur competitive pressures and raise productivity and growth. In addition, effective and sustainable use of resources can sustain stronger and more inclusive growth. Raising labour market inclusiveness, by keeping higher numbers of older workers in employment as well as reducing the gender pay gap, would help the recovery and improve living standards of all.

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