Executive Summary

The economy supports strong well-being outcomes

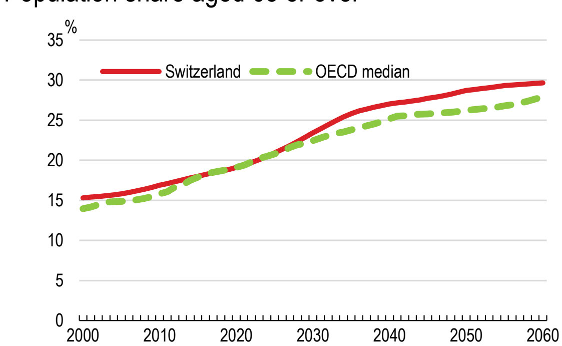
Switzerland has the third-highest GDP per capita in the OECD, thanks to high employment rates and productivity levels. These support, and are supported by, good health outcomes and a well performing education system.

Broad measures of living standards, such as subjective well-being and personal security, are amongst the highest in the OECD. Switzerland's carbon intensity is low, reflecting low energy intensity and almost carbon-free electricity. However, transport accounts for 40% of energy-related greenhouse gas emissions and contributes to air pollution, which exceeds international guidelines.

Adapting to demographic change is becoming pressing. Retiring baby boomers and increasing life expectancy will push the share of the population aged 65 years or more to 30% in coming decades (Figure 1). This trend, along with the digital transformation, will bring new opportunities for individuals and the economy. To realise these benefits and avoid ageing becoming a burden on firms and employees, a range of public policies including pensions, employment and health care policies, will need to adapt.

Figure 1. The population is becoming older

Population share aged 65 or over



Source: OECD, *OECD Economics Department Long-term Model*

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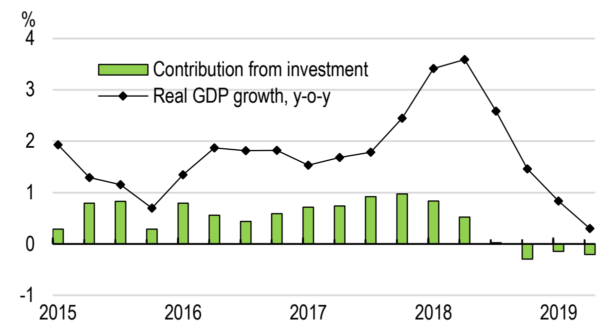
Output growth is projected to be moderate and risks are building

The economy has slowed sharply after a buoyant 2018. This partly reflects the unwinding of the boost from international sporting events, as Switzerland hosts major international associations. Rising trade tensions and a slowing in Europe are also weighing on activity. Monetary policy has been very accommodative while fiscal policy has been neutral.

Investment has been weak, as have exports and imports (Figure 2). However, consumption is solid and unemployment is low. Shortages are growing in some sectors, such as technical fields. Real wages are still flat. With low cost pressures, consumer price inflation is positive but low.

Figure 2. Growth has slowed from a rapid pace



Source: OECD, *OECD Economic Outlook* database

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Growth will strengthen in 2020 thanks to one-off factors (Table 1). Abstracting from international sporting events, growth will be close to trend. A recovery in wage growth and healthy labour market will support consumption. But risks to the outlook from global tensions remain prominent.

Table 1. The economy is set to pick up in 2020

(Annual growth rates, %, unless specified)	2018	2019	2020
Gross domestic product (GDP)	2.8	0.8	1.4
Private consumption	1.0	1.1	1.4
Government consumption	0.3	1.1	1.1
Gross fixed capital formation	1.1	0.4	1.5
Exports of goods and services	2.9	-0.4	2.7
Imports of goods and services	-0.3	-0.6	3.3
Unemployment rate (% of labour force)	4.7	4.5	4.5
Consumer price index	0.9	0.5	0.4

Source: OECD, *OECD Economic Outlook database,* October 2019.

The policy rate has been negative – at -0.75% – since 2015 and the central bank's foreign reserves remain high. Low interest rates are contributing to risks from housing market exposures and interest rate-related risks in the financial sector are high.

Making greater use of fiscal space would help monetary policy to normalise. Fiscal surpluses exceeded 1% of GDP in 2017-18. There is space to increase spending within the debt-brake rule. Revenue has been stronger than budgeted and expenditure has been persistently below the ceiling. The debt-brake rule should treat spending overruns and savings symmetrically. When inflation is firmly on an upward trend, monetary policy should begin to tighten, taking into account risks of exchange rate appreciation.

Tighter macroprudential regulation would curtail financial stability risks. Stronger lending standards for investor mortgages, which have become riskier than owner-occupier loans, will be introduced in 2020. Action should be reinforced by creating a formal framework for lending standards enforced on a comply-or-explain basis.

Switzerland's financial sector is also exposed to climate-related risks. Information about exposures would help investors to make more informed decisions. The sector's financing decisions can contribute to climate change mitigation. Improving climate-related disclosure for banks, pension funds and insurers could increase investment in sustainable assets and reduce risks associated with carbon-intensive asset exposures.

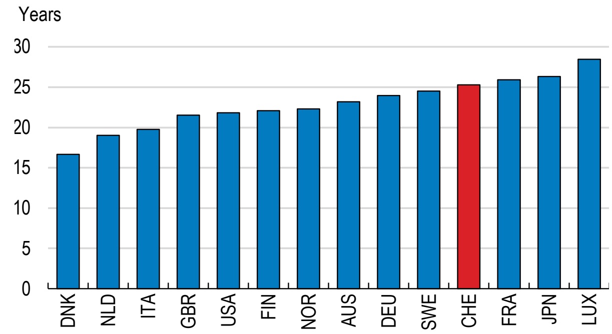
Stronger action now would better prepare for population ageing

Policies have not kept up with rising life expectancy. In particular, the statutory retirement age has remained at 65 years for men since its introduction in 1948 despite Swiss life expectancy at 65 having gained eight years. Women's retirement age is 64. Current settings imply that a relatively long time will be spent in retirement (Figure 3).

The pension system currently provides adequate incomes in retirement. For most employees the system offers high replacement rates, including through extra-mandatory schemes. However, replacement rates from the mandatory pension system will fall in coming decades. This risks increasing income inequality or adding to fiscal pressure through other social assistance. In the second pillar the rate at which accumulated assets in the mandatory part of the system are converted to a pension is set by law. The rate is too high, lowering the benefits available for younger generations.

Figure 3. Retirement is set to be relatively long

For a man born in 1996



Source: OECD (2017), *Pensions at a Glance 2017: OECD and G20 indicators;* United Nations, (2019), *World Population Prospects: The 2019 Revision*.

StatLink https://doi.org/10.1787/888934020996

Public spending on old-age pensions and health care will increase as the population ages. The burden is smaller than for many OECD countries but will largely fall on cantons and municipalities. Despite recent reforms the public first pillar scheme still faces sustainability challenges. Given fiscal rules, rising ageing-related costs threaten to crowd out other public spending.

Raising the statutory retirement age would mitigate the economic cost of ageing. It would increase individuals' retirement savings, reduce public pension financing needs, add to government revenues and raise economic growth. Women's retirement age should be raised to men's. The age should then be gradually lifted to 67 and linked to life expectancy thereafter.

Barriers to working longer should be addressed. Employment rates of older workers up to 65 years are comparatively high. Still, seniority wages together with higher rates of social security contributions act as disincentives to hiring and retaining them. The annual conference on old-age workers, which gathers social partners and other stakeholders, should be used to find ways of introducing greater flexibility into the wage-setting system. This could include training opportunities. Additional pension benefits from working beyond age 65 are being considered and welcome.

Shifting the tax mix towards more growth-friendly sources would help prepare the system for ageing. Plans to raise the VAT rate and lower personal income taxes for second-earners go in the right direction. Greater use of VAT, recurrent tax on immovable property and environmentally related taxes can help fund cuts in personal income tax for low-income earners.

Containing health care costs is rightly a government priority. Average health spending per person is the second-highest in the OECD. Planned reforms will tackle hospital costs, specialist fees and pharmaceuticals prices. The roll-out of electronic patient dossiers has the potential to enhance co-ordination, efficiency and outcomes. Incentives should be offered to practitioners to secure greater participation and reap the full benefits of the reform.

Long-term care needs increase with old age. Over one-fifth of those aged 65 or more received long-term care in 2017. But the system is fragmented and out-of-pocket expenses for home-based care can be unaffordable even with moderate needs. This creates incentives to move to a nursing home even with low care needs, which is neither cost-effective nor welfare-improving.

Switzerland can reap greater benefits from technological change

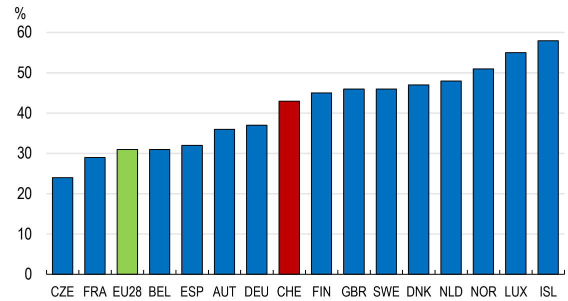
With its well educated workforce, excellent infrastructure, and high levels of R&D, Switzerland is well placed to benefit from new technologies. Digital technologies, for instance, can boost productivity. Take-up is around the OECD average, with many firms slower to adopt digital technologies than in leading countries.

Skills shortages in IT-related fields are hampering expansion of firms and the absorption of new technologies. IT competencies have not kept pace with leaders (Figure 4). Easing procedures for immigration from outside of Europe would assuage skill shortages. Promoting scientific and technical courses, particularly among women, would add to supply in the medium term.

Promoting a more dynamic business environment can spur adoption of digital technologies. Barriers to entry, including obstacles to inter-cantonal trade, dampen competitive pressures. Government involvement in sectors such as telecommunications is significant and sector regulators have weaker powers than elsewhere. Restrictions on services trade remain substantial. Stronger privacy protection and encouraging better management of digital security risks can help cultivate trust.

Figure 4. Swiss adults' digital skills lag the top performers

Share of adults with advanced digital skills



Source: Eurostat, *Digital Skills* database.

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Re-skilling and upgrading skills is vital to ensuring that workers are not left behind in the digital transformation. This will also improve retirement incomes. Lifelong learning is well-established in Switzerland but less-educated workers and those outside the labour force are less likely to participate. Recent measures to promote training are welcome. Targeted assistance to vulnerable workers, through vouchers for example, could further raise take-up. Spending on targeted training programmes should be ramped up. Conversely, planned measures to provide cash benefits to jobseekers aged over 60 risk lowering employment rates of older workers.

Expanding digital government can increase productivity and enhance services. The planned introduction of an electronic identification will overcome a major barrier to e-government. Policy-making is also hampered by data availability. Implementing the OECD Going Digital roadmap for measuring the digital transformation, with a priority on more timely and internationally comparable data, would provide a strong foundation for policy.

New technologies such as electric vehicles and ride-sharing platforms can lower Switzerland's carbon emissions. Cars purchased in 2018 emit 14% more CO_2 than the EU average. The government aims to raise the share of electric vehicles in new purchases to 15% by 2022, from 3% in 2018. Linking the tax rate on vehicle purchases to emissions would strengthen price incentives to purchase low-emission vehicles. This structure could help more cantons link their annual taxes to cleaner cars. Mandating the provision of charging stations in new buildings would support the roll-out.

MAIN FINDINGS	KEY RECOMMENDATIONS
Macroeconomic policies to support growth and maintain low inflation	
Debt is low and the fiscal position is sound. Structural surpluses have been larger than expected at the federal level. The monetary policy rate is negative and one of the lowest OECD-wide.	Take advantage of available fiscal space as needed, including by making fuller use of the margins under the spending limits of the fiscal framework (or "debt-brake rule"). When inflation is firmly rising start to remove monetary accommodation.
Addressing challenges in the financial sector	
Risk related to the housing market have grown due to the search for yield. Mortgages for investment properties have become more risky but stronger lending standards for investor mortgages will be introduced in 2020.	Establish a formal framework for setting mortgage lending limits that takes affordability into account and is enforced on a comply-or-explain basis.
Switzerland's large international financial sector is exposed to risks and opportunities from climate change and climate change mitigation policies globally. Providing investors and policy-holders with more information would improve resource allocation.	Strengthen disclosure of climate-related risks by financial intermediaries in line with recommendations of the Task Force on Climate-related Financial Disclosures.
Preparing for faster population ageing	
The lack of change in the statutory retirement age despite rising life expectancy will contribute to a rapid rise in the ratio of retirees to employment.The capital of the public first-pillar pension scheme is expected to be exhausted in the mid-2030s.	Fix the retirement age at 65 for both sexes as planned, then raise it gradually to 67 and thereafter link it to life expectancy.
Replacement rates from the mandatory pension system are currently high. However, 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.	Lower the parameter used to calculate annuities ("minimum conversion rate") and make it a more flexible technical parameter set by ordinance.
All levels of government rely on labour-related taxation for revenue but this creates disincentives to work and is more likely to come under pressure from ageing.	Reduce personal income taxation (at all levels of government) by lowering tax rates at low incomes and removing the disincentive for second-earners, financed by greater use of value-added tax, recurrent tax on immovable property and environmental taxes.
Few Swiss work beyond the statutory retirement age, in part due to strong financial disincentives for employers and employees. Older jobseekers have more difficulty finding work.	Use the existing annual conference on older workers to find ways to introduce greater flexibility into the wage-setting system and reduce seniority wages. Flatten the age-related progressivity in pension contribution rates. Prohibit age discrimination and establish enforcement mechanisms. Allow workers to compensate for gaps in their pension rights through contributions after age 65.
Ageing will increase health-related expenditure, which is already high. Through mandatory health insurance and out-of-pocket expenses, rising costs also pressure household budgets.	Proceed with cost containment programmes, particularly for curative care and pharmaceuticals. Introduce financial incentives and penalties to encourage the take-up of electronic patient health dossiers by health professionals and the input of quality data.
Demand for long-term care is high and will rise as the population ages. However, affordability of home-based care varies across cantons. Eligibility rules for financial support can push patients with low needs into nursing homes.	Use innovative tools such as vouchers or individual budgets based on a level of care needs, with co-ordinators helping to navigate the system, to develop the system in a cost-effective way.
Embracing digitalisation and new technologies	
Take-up of digital technologies has not kept pace with leading countries, particularly in small and medium-sized firms. IT-related skills shortages have increased. Insufficient competitive pressures and a lack of trust may also be hampering adoption.	Facilitate high-skilled immigration from non-EU countries to meet current labour market needs. Reduce barriers to entry, including by removing restrictions on the number of competitors and simplifying occupational licensing across cantons.
Participation in lifelong learning is high. But participation falls below leading countries for workers with low educational attainment and those who are not employed.	Expand spending on training for jobseekers, including those on social benefits. Use subsidies to encourage continuing education and training for groups who are most at risk from the effects of digitalisation.
E-government services are improving. Further digitalisation can reduce administrative burden and raise productivity.	Expand the use of digital tools to enhance services and simplify procedures at all levels of government.
A lack of data hinders the development of policies related to the digital economy.	Implement the OECD Going Digital roadmap for measuring the digital transformation, with a priority on more timely and internationally comparable data.
New technologies offer the opportunity to decarbonise transport, which is a key source of Swiss carbon emissions.	Redesign the federal vehicle tax to strengthen price incentives to purchase low-emission vehicles.

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