



OECD Territorial Reviews: Madrid, Spain

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Introduction

Madrid has captured the advantages of globalisation by becoming a metropolitan region of 6 million people, which attracts foreign workers and firms. The capital region has experienced impressive dynamic economic growth in recent years, making the best of the positive business cycle in Spain. It absorbs more than half of Spain's total foreign direct investment (FDI) and has extended its economic relations with Latin American countries.

Growth has occurred largely in the service sector (financial, banking, business services) as well as in logistics (Madrid Barajas Airport is the largest employer in the region). Unemployment has fallen to a low level – 6.5% in 2006 – while the growth rate has surpassed the national average as well as the average for OECD metro-regions. This overall positive environment has generated expectations among the local community, with the city government aiming to become the “most important metropolis in Europe after Paris and London”.

There is however concern about how to sustain this positive economic path in the long run. The main challenges to be addressed include a relatively low productivity level, insufficient specialisation in high value-added manufacturing activities, a low innovation capacity, job-skills mismatches, especially for immigrants, transport congestion, and a shortage of rental housing. In the present positive environment, public authorities in Madrid will need to consider a well-rounded strategy promoting longer-term shifts in economic, labour market and spatial structures to sustain the robust growth path.

Developments in public-policy making and the governance framework in Madrid have provided the metro-region with many of the institutional resources necessary to make decisions and effectively implement public policies, yet some adaptations will be necessary to address effectively the forthcoming challenges.

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

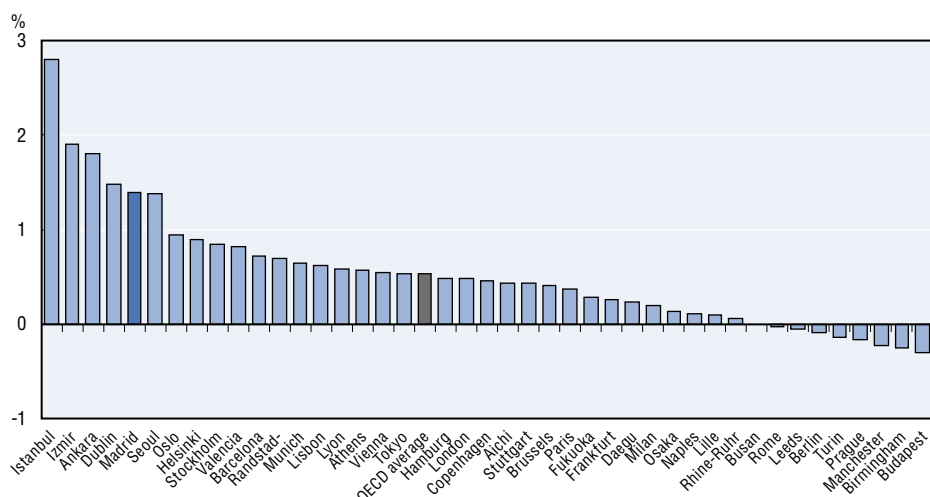
What are the main factors of success?

Since the mid-1990s, Madrid has enjoyed one of the highest expansions in population and economic growth within Europe and among OECD metropolitan areas (see Figure 1). From 1995-2005, Madrid registered an average annual growth rate of 3.7%, above Spain's 3.3%, and twice the average growth rate of the European Union for the same period. The population grew by 15.4% in 2000-2006. Over the same period, 760 000 new jobs were created and unemployment declined from 11.6% to 6.5%.

This economic boom has made the Madrid metro-region a magnet for foreign workers, mainly from Latin American countries. With an influx of 495 000 migrants between 2001 and 2006, increasing their share of the regional population to 13.3% from 5.7%, immigration has been a driving force behind Madrid's economic success. Today, the capital region is home to more than 13.5% of the national population and generates above 17% of Spain's output.

Although the recent strong regional performance is partly the result of a "country effect" – driven by Spain's international openness, EU membership, macroeconomic and structural reforms – Madrid's economic success has also been sustained by a set of ambitious policy measures to enhance human, social, infrastructure and institutional resources. The region is now endowed with efficient public transport infrastructure: the railway, road and subway network have been continuously expanding – the metro network has increased on average 6% per year, and is now double the size it was in 1984 – and the radial shape of the national transport infrastructure makes Madrid a prime logistics platform in Spain. International and regional accessibility have also improved with the recent Barajas airport expansion. The airport is now the largest regional employer and Madrid ranks 5th for passenger traffic and 9th for freight in Europe. Madrid also has a well-qualified and relatively inexpensive labour force (see Figure 2). The metro-region ranks 8th among the OECD metro-regions, and second in Europe after London, for the share of the population aged 15 and more with a tertiary education. Finally, the public authorities have made consistent efforts to valorise urban cultural and natural amenities such as museums and parks, helping to boost tourism.

Figure 1.
AVERAGE ANNUAL
POPULATION GROWTH
RATES AMONG OECD
MEMBER COUNTRIES
(1995-2002)



Note: OECD average refers to the average of OECD metro-regions.

Source: OECD Metropolitan database.

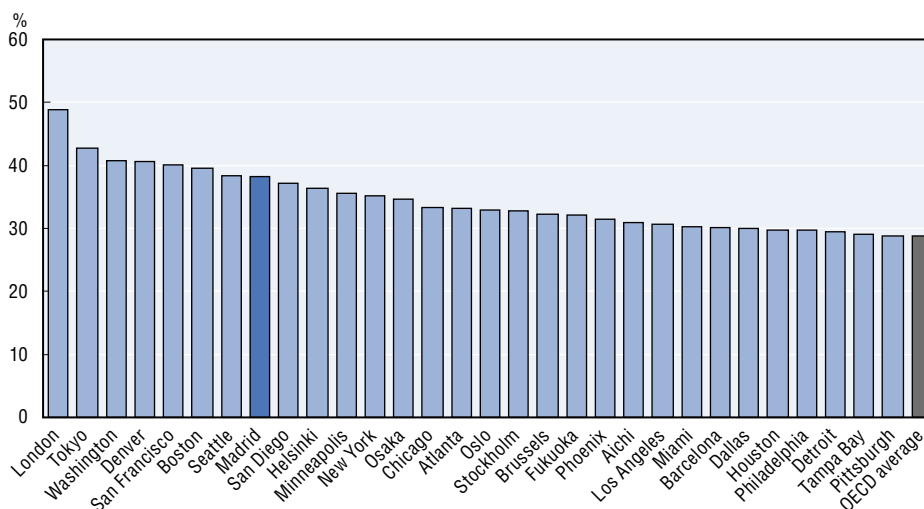
Madrid is now the 4th tourism destination in Europe after London, Paris and Rome, particularly for business trips thanks to major investment in congress and exhibition centres – the region ranks among the 10 top places worldwide for international conferences. ■

What new challenges does Madrid face?

A main challenge for Madrid is to extend its present economic growth into a long-term pattern. Madrid ranks 20th out of 31 metro-regions in Europe with 1.5 million and more inhabitants, despite having a per capita gross domestic product (GDP) above the European average. Madrid's overall economic development is burdened by structural deficiencies causing low labour productivity; Madrid's was 18% lower than the average OECD metro-region in 2002. Relatively low labour productivity is a concern throughout Spain, but Madrid has been performing below the national average for labour productivity growth since 2001 (see Figure 3). Structural bottlenecks on the labour market caused by overuse of short-term contracts, and a mismatch between education and required job skills along with insufficient specialisation in high value-added activities have limited the increase of productivity levels. Madrid has also registered greater specialisation in some productive activities, advanced financial services and medium-high tech manufacturing. Nevertheless, many new jobs were created in low value-added services such as construction, hotels and restaurants, or community services and the crisis in electronics along with insufficient research and development (R&D) expenditure have also contributed to a reduced share of high-tech manufacturing.

The share of R&D activities compared to total GDP is higher in Madrid than for Spain as a whole (1.82% versus 1.13% in 2005), but Spain itself is close to the bottom of R&D rankings among OECD member countries, with a spending to GDP ratio of 1.1% against an EU average of 2%. Madrid also produces a number of patent applications only slightly above the national average and relatively low compared to the leading European metro-regions.

Figure 2.
SHARE OF POPULATION
OF 15 YEARS AND
MORE WITH TERTIARY
EDUCATION
Metro-regions above
the OECD average (2004)



Note: OECD average refers to the average of OECD metro-regions.

Source: OECD Metropolitan database.

Madrid's recent fast urbanisation and rapid inward migration have also generated new demands. Despite a well-developed public transit system, the recent surge in private car users has generated significant congestion costs, particularly in the outskirts of the city. The land and housing markets are also under pressure which has led to significant and consistent price increases, despite a significant increase in housing provision. Consequently, housing costs represent almost 40% of annual household expenditures in Madrid. The lack of affordable housing particularly affects young people – about 22% of Madrid's 20-34 year-olds still live with their parents – and the most vulnerable groups such as immigrants. This trend can partly be explained by rigidities in the Spanish housing system, which has tended to favour home ownership. This is a positive element in that a growing percentage of the middle classes now own their homes, but has been to the detriment of rental housing where the available supply of units has declined while the number of empty units has increased (about 13% in the City of Madrid). Finally, Madrid's recent large influx of 495 000 migrants in just five years has been a driving force behind Madrid's economic success. Their integration in the labour market and in society has thus far been considered quite successful; however it has also come with a natural gentrification process and spatial/income disparities within the region, especially in the southeast and in the south although on a limited scale compared with other OECD metro-regions. ■

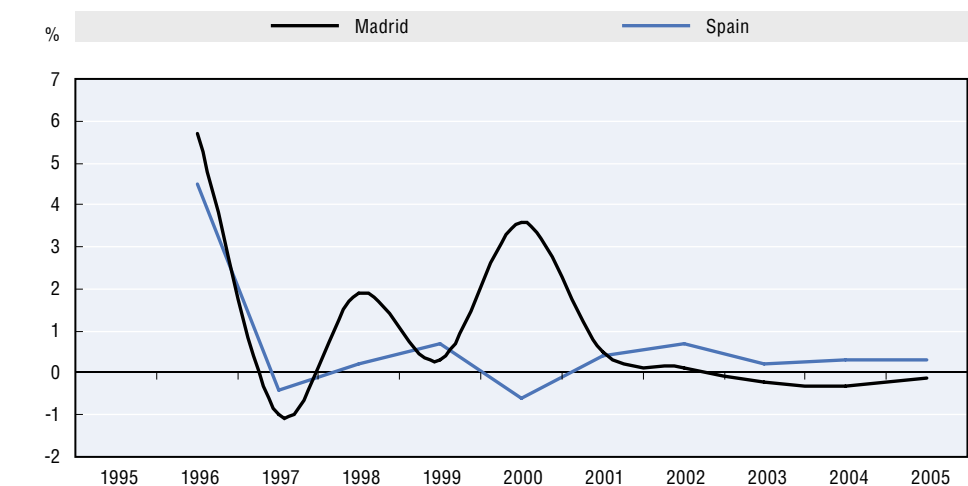
How to upgrade the economy?

Madrid could improve its specialisation in high value-added industries by increasing labour productivity, innovation capacity and local specialisation in key strategic sectors and by optimising migrants' skills.

- *Improving labour productivity* in Madrid could be tackled by reducing the overuse of short-term contracts that have encouraged the creation of low-skilled jobs and acted against strong job performance. Sub-national authorities can provide employers with incentives to reduce the use of short-term contracts for young highly-educated workers. Such policies could be conducted in partnership with local universities and professional training institutes to improve graduate integration into the labour market. This approach would also reduce the significant existing education-job mismatches.

Figure 3.

ANNUAL PRODUCTIVITY GROWTH (PER WORKER)
Deflated values, 1995-2005



Source: INE – Spanish National Institute of Statistics).

- Boosting *innovation capacity* will require further R&D investment and fine-tuning of innovation policy. Actions need to be taken to address the current fragmentation of innovation policy that limits the efficiency of the already limited public funding in this area. The interaction of local firms with universities is also a challenge, partly constrained by relatively rigid regulations. Regional stakeholders could seek to transform their regional universities into centres of excellence by developing programmes aimed at creating relational capital among existing stakeholders in the innovation system.
- Efforts towards innovation and technology could be further linked with the *development of strategic clusters*. Madrid shows potential for some medium- and high-tech specialisation in biotechnology and pharmaceuticals, aerospace and in electronics, while banking and financial services are emerging as a promising advanced global services segment.
 - The *aerospace* industry localised in Madrid has benefited from a national sectoral policy and is now facing rising competition from newly emerging markets in Asia and Latin America. Regional and local stakeholders might well focus their efforts on building and improving local and international teaching, research and training networks closely linked to the specific needs of the aerospace hub, both inside and outside the direct scope of the science parks. Strategic research partnerships could also be established with major global players through specific research grants. Further specialisation in some niche markets is needed in light of the trend toward productive restructuring, though this will require a more thorough territorial diagnosis to better identify local strengths.
 - *Electronics*, the largest manufacturing sector in Madrid since the mid 1970s, has experienced a major restructuring crisis such that, even with global players like Telefónica, this sector in Madrid today plays a relatively marginal role. Madrid nonetheless retains a certain technical know-how and tradition in electronics that could be strategic for the success of complementary initiatives, such as the role of ICT within the municipal strategy, the potential for creating “educational or learning incubators” and locally supplied services for the aerospace hub.
 - *Banking and financial* services have recently undergone a rapid process of internationalization in Madrid, leading to surprising growth in the stock exchange and financial marketplace. Madrid now ranks 4th after London, Paris and Frankfurt. In addition to city government interventions aimed at creating real estate opportunities for firms, a more elaborated strategy to support the potential of this sector could be developed, especially in light of its potential to connect the financial markets and stock exchanges in Europe and Latin America.
- Several actions could be taken to *better use the assets of the immigrant labour pool*. Spanish policies regarding the immigrant population have made it easier for workers to legally join the labour market. However productivity losses from mismatches between training levels and skills requirements, partly linked with slow recognition or non-recognition of foreign credentials, still need to be addressed. Inter-governmental collaboration would give public actors from the three levels of government the opportunity to optimise a

multi-sectoral approach to immigration policy, perhaps by establishing a single “round table” to pool their resources. This “round table” could focus on the institutionalisation of mapping jobs to skills in Madrid’s metropolitan economy, in co-ordination with the business sector and the labour associations. ■

What about spatial development?

Land use and spatial planning have to adapt to new challenges raised by the recent fast urbanisation and growth in Madrid, including costs linked to transport congestion and strain on housing and real estate.

Transportation is a shared competence and is managed by the Madrid Public Transportation Consortium, a “single purpose” independent body, made up of representatives of the three layers of government, trade unions, business associations, and civil society. The Consortium is in charge of planning, implementing and managing the regional transportation infrastructure. This governance model in transportation has proved particularly efficient, contributing to the rapid positive development registered in this field. Further action is needed, however, to address the over-use of private cars and provide alternative transport in the inner belts. The ongoing experiments of public-private partnerships, with some large companies involved in investing in alternative transport for some outward lying industrial districts are an interesting option.

In the *housing* sector, national measures are needed to relieve the pressure on the rental market. Local planning standards need to be more flexible and the land development regulations need to be reconsidered, to eliminate perverse financial incentives for local governments to retain land from the market and keep prices high. ■

How to adapt governance?

Madrid’s economic success has been due in part to a well-functioning governance framework. The successive waves of decentralisation implemented in Spain have contributed to Madrid’s local and regional governments becoming more pro-active sub-national authorities, delivering more efficient public services and developing important public policies for urban development. Moreover, Madrid has benefited from exceptional conditions compared to most other OECD metro-regions as the region fits approximately with the functional metropolitan area. As such, the region has played *de facto* the role of a metropolitan government with strong political legitimacy and resources, implementing public policies in the virtual absence of social conflict thanks to the development of a neo-corporatist system based on strong linkages with social and economic forces, especially trade unions and business associations.

The metro-region governance will however necessitate some adaptations of its current governance framework, including: i) *Streamlining intergovernmental relationships* within the metro-region and ii) *Fostering city governance* through greater involvement of civil society in urban policy-making.

i) The system of governance in Madrid is evolving towards a more balanced role among the two layers of government, with the city increasingly involved in some fields once only occupied by the regional government. It is therefore important to avoid creating a zero-sum game of competition amongst

public actors by creating linkages between the different layers. The current *decentralisation* process might help to streamline and clarify the relationships among the local and the regional authorities. Developing *innovative and flexible co-operation arrangements* is also needed. A wide range of such instruments are already provided by the Community of Madrid's institutional system. They include contractual arrangements (*convenios*) among layers of government to establish co-operation funds for the delivery of social and economic services, for large infrastructure projects like the Barajas airport expansion and for the organisation of the Olympic bid. There are also examples of *ad hoc* intergovernmental bodies, like the Regional Transport Consortium.

An innovative and flexible co-operative framework is particularly needed for *economic development* where the City of Madrid has taken a more pro-active role, implementing policies to support science and technology and entrepreneurship, and to promote internationalisation. The creation of an independent economic innovation agency in the Madrid Metro-region could help to avoid overlapping and duplication of programmes and projects, and guarantee a strategic view over the sector and the necessary scale of initiatives. This agency could well follow the model of the Public Transportation Consortium, working as an autonomous technical body involving a wide range of public and private stakeholders (including the different local economic development agencies). Synergies among actors and integration of policies could also be developed in the area of *strategic planning*. Co-operation could be induced by creating formalized places and procedures for dialogue and mediation between the two levels, for instance by developing a master plan that would embody a collective multi-stakeholder vision.

ii) The City of Madrid has undertaken important *reforms of its urban governance*, including wide modernisation of its internal organisation, with initiatives like an integrated system for economic, financial and human resources management, a service charter (*Carta de Servicios*) aimed at improving the responsiveness of public services to users and the development of electronic administration. The Madrid City Council is also implementing a process of territorial decentralisation towards the 21 Districts that are in charge of many administrative functions delegated by the mayor or the governing council in a wide range of fields. One step for the City of Madrid to improve its urban governance is to foster the participation of *civil society in urban policy-making*. New participatory approaches have recently been developed through a rather homogenous and formalised policy managed by a single municipal department that combines both economic development and civil participation. Further improvements could be reached, for instance by increasing the number of members of associations on the representative councils. Some decisions could be made by civil society, like participatory budgets, a process that allows citizens to decide how to use part of the financial resources available for investment within the local government's budget. ■

For further information

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For further reading

OECD (2007), **Economic Survey of Spain 2007**,
ISBN 92-64-02920-6, € 34, 178 pages.

OECD (2007), **OECD Territorial Review: Madrid, Spain**,
ISBN 978-92-64-03847-9, € 40, 259 pages.

OECD (2006), **Competitive Cities in the Global Economy**,
ISBN 92-64-02708-4, € 25, 450 pages.

OECD (2006), **OECD Territorial Review: Stockholm, Sweden**,
ISBN 92-64-02252-2, 218 pages.

OECD (2004), **OECD Territorial Review: Montreal, Canada**,
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OECD (2005), **Regions at a Glance 2005**,
ISBN 92-64-01863-8, € 40, 249 pages.

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