

# German High-Tech Sector Continues to Be Buoyant

*In 2007 the number of start-ups in the high-tech sector rose to 19,200, a four percent increase compared with the previous year. The increase in the high-tech sector contrasts with the development of start-up activities across all sectors of the economy, which witnessed a two percent reduction in the number of start-ups in 2007 compared with the previous year.*



This is one of the main findings of an ongoing study into the development of high-tech start-ups in Germany, which the Centre for European Economic Research (ZEW) is conducting in collaboration with Microsoft Germany's "unternimm was. (Do something)" start-up initiative.

The rise in the number of start-ups in high-tech sectors in 2007 is due to the exceptionally good economic situation in the high-tech areas of services and industry. The high-tech sector currently accounts for slightly less than 8 percent of all start-ups in total. However, high-tech start-ups are particularly important to the competitiveness of the economy, because they ensure timely alignment of the economy with promising technological developments. In the technology-oriented services sector, the number of start-ups in 2007 was 4 percent high-

er compared with 2006. However, this is a lower increase than in the industrial high-tech sector, which saw 6 per cent more start-ups.

## Leading Edge Technology at its Turning Point?

It's pleasing that the number of start-ups in 2007 has risen in both leading-edge technology and superior technology, i.e. in both sectors of the industrial high-tech area. This is good news, because it interrupted a downwards trend in leading-edge technology which had continued for ten years (see chart next page). Leading-edge technology had around 780 start-ups in 2007. This is a 4 percent increase compared with 2006. Superior technology witnessed an increase of 7 percent on around 1,800

new companies. The healthy economic situation in 2007, particularly in sectors like mechanical engineering, electrical engineering and control and instrumentation, was crucial to this development. In spite of the upwards trend, the number of high-tech start-ups is still clearly below the level achieved ten years ago. As the macro-economic benefit of high-tech companies is due, first and foremost, to the cumulative overall effect of all the companies together, a lower level of start-up activities in the high-tech sector reduces the German economy's future achievement potential.

## High-Tech Start-Ups are Seldom Born of Necessity

Empirical findings suggest that high-tech start-ups are more rarely born of necessity than start-ups in the non-high-tech sectors. Regression analyses show that changes to start-up intensity

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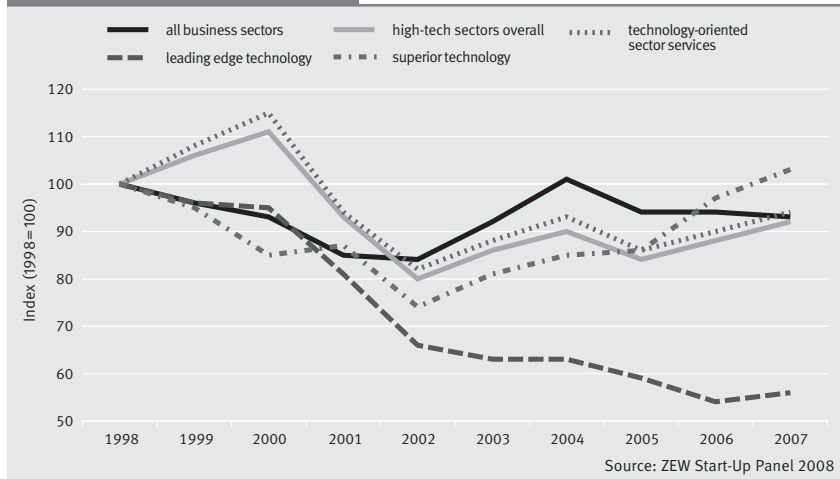
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## RESEARCH FINDINGS

across all sectors of the economy are affected by the level of the regional unemployment rate. The principle here is: the higher the unemployment rate in the

base year of the study, the higher the increase in start-up intensity. This effect is not observable in the case of start-ups in the high-tech sector.

## Start-Up Activities in Germany



Information and communication technologies (ICT) are important to the high-tech sector. The ICT sectors include software, ICT services and hardware. After severe declines in start-up activity in 2001 and 2002, start-up activity in the software sector stabilized last year, with the number of start-ups in the software sector being around 3,900, an approximately 3 percent increase compared with the previous year. ICT services saw start-up activity in 2007 rise to 5,900 new companies, an increase of 4 percent compared with 2006. After the marked decline in start-up activity in the hardware sector in 2001 and 2002 and the subsequent stagnation of start-up figures, 2007 provided the first evidence of a slight increase of 2 percent in start-up activity compared with 2006.

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## Consumers Worried about Genetically Modified Foods despite Labeling

*The labeling of genetically modified (GM) foods is mandatory in the European Union. Nevertheless, it is easy to unsettle consumers when it comes to differentiate between GM foods and non-GM foods. This is the finding of a study conducted by the Centre for European Economic Research (ZEW) in Mannheim (Discussion Paper No. 08-029), which analyses consumer behaviour by means of controlled laboratory experiments. German consumers require a price reduction of about 50 percent to purchase GM foods. The sales opportunities for GM foods in Germany and the impacts of different labeling regulations on the customer behaviour are spotlighted in the study.*

In total, 164 volunteers participated in the laboratory experiments. The participants bid in real auctions for candy bars and soy bean oil. These products either contained GM or non-GM ingredients. It was the first study in Germany in which participants had to make real purchase decisions about GM foods. In contrast to surveys in which the participants only answer hypothetical questions, auctions give participants the incentive to reveal what they are willing to pay in reality.

The study's findings indicate that consumers definitely prefer non-GM

foods. More than 80 percent of the auction participants offered higher prices for non-GM foods than for GM foods. On average participants demanded a price reduction of about 50 percent to purchase GM foods. GM foods, therefore, are only likely to sell if they are offered at a much cheaper price than non-GM foods.

Current regulations allow additional labeling of non-GM foods with labels saying "produced without genetic engineering" and products labeled "GM-free" are readily found on the German market. The study shows that this re-

dundant labeling affects consumers' trust in the current mandatory labeling scheme, shattering consumer confidence in the GM-free character of products that do not carry a label.

### Redundant Labeling Causes Distrust

As the imminent commercialisation of GM foods in the German market is likely to rise producer incentives to label their product as GM-free, consumers' lack of confidence in the regulatory scheme may worsen. Policy makers should act promptly to either increase consumers' trust in the existing labeling regulations, for example through information campaigns, or consider the possibility to change the existing regulation by banning or requiring "GM-free" labels.

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## RESEARCH FINDINGS

# Rainforest Conservation Reduces Costs of International Climate Policy

*Preserving tropical rainforests is not only important for the protection of biodiversity but represents a particularly cost-efficient instrument of climate policy. If the world's rainforests were involved in the international emissions trading to reduce climate-changing greenhouse gases, industrialised countries as well as developing countries would benefit in the long term.*

Last year's assessment report of the Intergovernmental Panel on Climate Change emphasized the urgency of combating global warming. As the primary causes of climate change the report highlights fossil fuel use and land use change, the latter accounting for roughly one fifth of total anthropogenic greenhouse gas emissions. In this context, a recent study (Discussion Paper No. 08-016) conducted by the Centre for European Economic Research (ZEW) suggests that avoiding emissions by protecting large rainforest areas is not only effective for climate protection but also cost-efficient. Integrating rainforest protection in a new climate policy agreement (after the Kyoto Protocol expiry in 2012) would thus considerably increase the effectiveness and affordability of future climate politics.

## Forests Play a Key Role in Climate Change

A new policy proposal entitled "Reducing Emissions from Deforestation and Degradation" (REDD) aims at integrating tropical rainforest conservation in international trading of emission allowances. Forests play a twofold role in climate change: while growing trees absorb carbon dioxide from the air and store carbon by the process of photosynthesis, forests can become a major emissions source when the stored carbon is released into the atmosphere by means of deforestation activities. Thus, land clearance to create agricultural areas releases the stored carbon into the earth's atmosphere as greenhouse gas and thereby contributes to climate

change. REDD would acknowledge and value carbon emissions reduced by avoiding tropical deforestation, as developing countries would be rewarded with corresponding emissions credits which could then be sold to industrialised countries. The latter could use these credits to achieve their climate protection goals.

## Reduced Costs for Emission Rights for Industrialised Countries

Industrialised countries could save costs by means of REDD while reaching their climate protection goals, as reduc-

emissions trading would cut the costs for emissions certificates. Future climate protection goals could thus be reached more cost-efficiently, and more ambitious goals of reducing emissions could be realised without extra burdens for industrialised countries.

## Industrialised and Developing Countries Could Benefit

In particular, also tropical regions could benefit from the REDD mechanism. The study indicates that the revenues of selling emissions credits considerably exceed the opportunity costs of rainforest conservation in the form of foregone returns for land use (for example from selling timber or creating agricultural areas). Tropical rainforest regions could hence receive substantial net revenues from exporting carbon-off-



ing emissions by protecting tropical rainforests is more cost-efficient than avoiding emissions by technical innovations in Europe, for example. The reason is that industrialised countries already use highly developed technologies to decrease carbon emissions. To save even more emissions, the countries would thus have to invest considerably in expensive technological innovations and their implementation. Integrating tropical rainforests into international

set credits to the industrialized world. Developing countries would thereby benefit in economic terms and simultaneously preserve their forests. Furthermore, integrating rainforest protection in emissions trading could also help to win important industrialised countries as well as emerging and developing countries for a future international climate policy agreement.

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## RESEARCH FINDINGS

# EU Parliamentarians with Expertise in Economics Tend to Reject EU Tax

*The budget of the European Union (EU) has been largely financed up to now by contributions paid by member states, measured, in particular, by a country's share in the EU's gross national income. There has been a controversial debate for many years now about converting this system of contributions, at least in part, to a tax financing method and assigning the EU its own tax competence. Against this background, a survey among Members of the European Parliament (MEPs) conducted by the Centre for European Economic Research (ZEW) investigates whether they advocate an EU tax and what form such a tax should take. The survey also analyzes the extent to which the representatives' national origin or party affiliation determines their advocacy or rejection of an EU tax.*



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The ZEW Study (Discussion Paper No. 08-027) is based on its own survey of MEPs, in which 158 representatives, that is twenty percent of all EU parliamentarians, took part. The mandate holders were not only questioned about their general attitude to an EU tax, but also about the type of tax they preferred. Overall, the study shows that the parliamentarians, on average, have a slight preference for financing the EU budget via a tax system and that an environmental tax or EU value-added tax would be the preferred starting points for a project of this sort.

## Approval Ratings on EU Tax Vary Considerably across MEPs

However, approval ratings on this issue vary considerably across member states and parties. This gives rise to the main question of the study, that is whether the answers given by the representatives followed party boundaries or were motivated by other individual or national characteristics. The individual answers of those surveyed were subjected to an econometric analysis. This examined the extent to which, in addition to party membership, particular characteristics of a representative's country of origin or his individual characteristics play a role in respect of his attitude to the introduction of an EU tax.

## Long-lasting EP Membership Boosts Acceptance of EU Tax

The result shows that, while party membership exerts an important influence, the other explanatory variables are also significant. For example, representatives with a degree in business administration or economics tend to reject an EU tax. This also applies to members of the budget committee. Evidently, expert knowledge tends to nurture scepticism about an EU tax's ability to provide a real improvement. Long membership of the European Parliament (EP), by contrast, tends to be linked to an affirmative attitude to the EU tax, which may be

attributable to adjustment to the prevailing preferences in the European Parliament in the course of membership.

## New EU Members Prefer Autonomous Tax Policy

In addition to these personal characteristics, there are particular characteristics relating to the countries of origin that exert an influence. Representatives from the new EU member states, for example, tend to be negatively disposed towards an EU tax. This is a plausible result, because the countries of Eastern Europe make aggressive use of an autonomous tax policy to boost their company locations. There is also evidence of a tendency for representatives from net recipient countries to welcome an EU tax. These findings suggest that switching budget financing to a tax is regarded as helpful for increasing or at least safeguarding the transfers to the recipient countries. Finally, the study shows that approval of an EU corporate tax is particularly marked in those countries that impose high effective taxes on their companies. The representatives from high-tax countries obviously hope thereby to attenuate the tax competition that is disadvantageous to them by introducing a corporate tax in favour of the EU budget.

## Strong National Interests

Overall, the study clearly shows that national interests also have considerable influence in respect of considerations of possible reforms of the EU financial system. The hope that a European tax might one day contribute to reducing national egoisms in the budgetary debates is therefore likely to be illusory.

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## ZEW CONFERENCE

# Economics Nobel Prize Winner Heckman on “Skills, Schools and Synapses”

*Prof. Dr. Dr. h.c. mult. Wolfgang Franz, President of the Centre for European Economic Research (ZEW), welcomed the Economics Nobel Prize Winner, Prof. James J. Heckman, Ph.D., from the University of Chicago, in May for a lecture on non-cognitive skills – these refer, for example, to persistence in problem solving, discipline and concentration – and their importance for human capital formation in economies. Around 350 guests had accepted the invitation to the event, which took place at the ZEW within the “First-Hand Information on the Current Economic Policy” lecture series.*

At the beginning of his lecture entitled “Skills, Schools and Synapses”, Heckman pointed out the phenomenon of a growing new underclass which, he said, was increasingly supplanting the middle class. According to him, this phenomenon was particularly observable in the United States, but was also on the increase in many European countries. The growing underclass was, he said, characterized, first and foremost, by a high rate of school dropouts and unskilled people. Delinquency and health risks amongst its ranks were on the increase. Owing to high unemployment and decreasing productivity amongst the poorly qualified, the economies would, in his view, have to bear high costs.

## Early Childhood Moulds

While these social problems had been mainly attributed up to now to a lack of cognitive skills, such as a lack of education, the real causes, according to Heckman, lay very much deeper. Heckman argued that, even before a child completed his first school lesson, it had received (or had not received) training in certain non-cognitive competences in the parental home, which had a formative influence on his further development and hence his socio-economic success during his lifetime. In Heckman's view, these non-cognitive skills initially had nothing to do with intelligence. If anything, he said, they were character-related qualities like endurance, diligence, motivation, single-

mindedness, willpower or even self-confidence, which were already developed by parental stimulation up to the age of five.

Heckman's contention was that these non-cognitive skills provided the basis for cognitive competences to develop in later years. He argued that a child of pre-school age that learnt to pay attention to a certain matter over a certain span of

time in his home environment would subsequently find it easier to read, say, a book. This success, in his view, was motivational and opened further development doors. Another child that, had not, say, experienced a regular daily routine in the parental home would, according to Heckman, find it difficult to persevere with routine activities such as doing daily homework. Cognitive and non-cognitive skills, he said, thus had a mutual influence on one another.

of pre-school children caused society much lower costs and was moreover much more successful than any measures that did not begin until children had become youths or young adults. Furthermore, he argued that, owing to the interplay between, and the self-reinforcement effects of, non-cognitive and cognitive competences in pre-school age, educational investments in early childhood could produce high returns, measured in terms of the subsequent lifetime income of those supported.



*Prof. James J. Heckman giving his lecture at the ZEW*

*Photography: ZEW*

Social inequality, he stated, began at home, adding that, as studies con-

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## ZEW SUMMER WORKSHOP

# Economics and Econometrics of Innovation and Patenting

Every year the Centre for European Economic Research (ZEW), Mannheim, organises a Summer Workshop for young economists. This year's Summer Workshop, which took place from 9th to 12th June, focused on methods for econometric analysis of patent and innovation data. Leading experts gave an overview of specific methods in their fields, highlighting the main directions of current research.

In addition, 17 young talented researchers (selected from a total of 97 applicants) were given an opportunity to present their recent research and to discuss it with experts in their field. The young researchers were also given

ample opportunity to communicate amongst themselves, to allow them to extend their international contacts. Participants comprised young researchers from the United States, China, Italy, France, Norway, the Netherlands, Belgium and Germany.

## Research Topics

The topics covered ranged from the evaluation of public research and development programmes (R&D), to the analysis of (regional) political influences on the project selection of R&D through public R&D contests to international technology transfer. Econometri-

cally sophisticated models were used to analyse determinants of innovation strategies in selected industries such as the Chinese textile industry, the mould industry in Portugal or the German pharmaceutical industry.

## Particular Emphasis on Training Component

The training component for young researchers was given particular emphasis during the ZEW Summer Workshop. Bettina Peters (ZEW) gave an introduction to econometric methods for innovation data with specific reference to the Community Innovation Surveys (CIS) of the European Union (EU). Fabio Montobio (University of Insubria, Varese) presented methods for analysing patent data. Dirk Czarnitzki (Catholic University of Leuven) summarised methods in evaluation econometrics and highlighted a selection of problems arising from the application of these econometric techniques. Jacques Mairesse (ENSAE, Paris) presented the main approaches (including their strengths and weaknesses) to estimate the private and social returns of innovation and R&D.

Methods for analysing complementarities in innovation processes were featured by Pierre Mohnen (University of Maastricht). Kornelius Kraft (University of Dortmund) and Bruno Cassiman (IESE, Barcelona) gave presentations on the interrelationship between market power, mergers and the innovation activity of companies. Following the Summer Workshop, the ZEW hosted its third conference on the economics of innovation and patenting. The conference was supported by the EU cost project "Strike" and the Anglo German Foundation's research initiative on "creating sustainable growth in Europe".

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## Carlos Santos Received the 2008 Heinz König Young Scholar Award

At the close of the ZEW Summer Workshop, the Heinz König Young Scholar Award was presented. As in the previous year, a Portuguese young scholar, this time in the shape of Carlos Santos, was awarded this prize. Carlos Santos has recently completed his doctorate at the London School of Economics. The award involving prize money of 5,000 euro, sponsored this year by MLP (Marschollek, Lautenschläger und Partner), and a residential fellowship at the ZEW commemorates Professor Heinz König, the founding director of the ZEW. The prize awards excellent empirical papers by young economists.

In his award-winning paper, Carlos Santos develops and implements a structural, microeconomic model of the decision of companies to invest in innovations. He uses data from the mould industry in Portugal to examine the explanatory power of this model. The President of the ZEW, Prof. Dr. Dr. h.c. mult. Wolfgang Franz, who



*ZEW President Wolfgang Franz congratulates Carlos Santos on his prize-winning paper.*

presented the prize also on behalf of the sponsor, paid tribute in his citation to the originality of the work of Carlos Santos, which, he said, provided an important explanatory approach to the long-term co-existence of innovative and non-innovative companies, thereby highlighting concrete starting points for a government innovation policy that aims to promote the international competitiveness of companies.

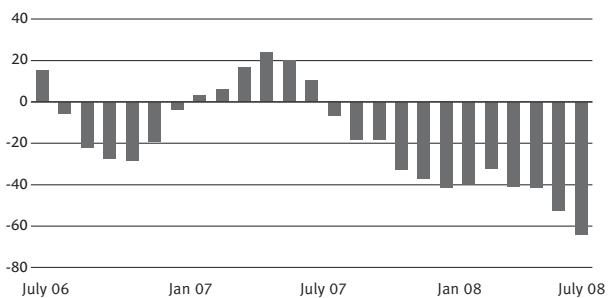
ZEW FINANCIAL MARKET DATA

## ZEW Financial Market Surveys July 2008

The ZEW conducts three monthly surveys questioning financial market experts for their expectations within six months time for essential financial market data in several European countries and the Eurozone. The questions regard the current business situation, the business outlook, interest rates, stock markets, exchange rates and inflation. Additionally, a “special question” on an interesting economic topic is asked. Up to 350 financial market experts are questioned in the Financial Market Survey for Germany. About 70 analysts participate

in the Financial Market Survey for Switzerland that is conducted in cooperation with the Swiss bank Credit Suisse. About 80 analysts contribute to the Financial Market Test for the Central and Eastern European Region (CEE) and Austria, carried out in cooperation with Erste Bank der Österreichischen Sparkassen. The CEE Region consists of Bulgaria, Croatia, the Czech Republic, Hungary, Poland, Romania, Serbia, Slovakia and Slovenia. The survey collects economic data for each of these countries but also looks at the CEE Region as a whole.

The complete results of the surveys are published every month in Financial Market Reports. The “ZEW Finanzmarktreport” ([www.zew.de/FMR](http://www.zew.de/FMR)) contains the survey's outcome for Germany. The survey results for Switzerland are published in the Financial Market Report Switzerland ([www.zew.de/FMR\\_CH](http://www.zew.de/FMR_CH)). The survey results for the CEE Region and Austria are published in the Financial Market Report CEE ([www.zew.de/FMR\\_CEE](http://www.zew.de/FMR_CEE)). Below, some selected outcomes of the July 2008 surveys are featured briefly.

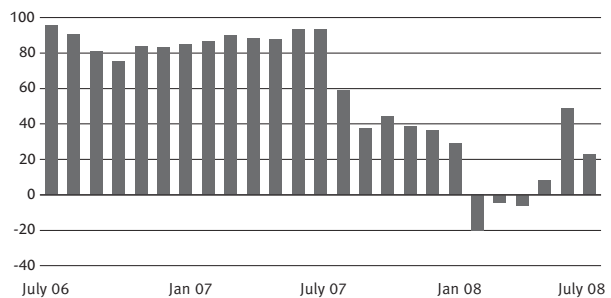


Balance of positive and negative assessment category chosen by respondents of the Financial Market Survey Germany. Source: ZEW

### Germany: Economic Expectations

The ZEW Indicator of Economic Sentiment for Germany, which reflects financial market experts' assessment of Germany's economic development within the next six months, dropped significantly in July 2008. The indicator decreased by 11.5 points and now stands at minus 63.9 points after minus 52.4 points in the previous month. This is still well below its historical average of 28.8 points. The low level of the economic sentiment indicator reflects increased world-wide risks, such as the high oil price, the strong euro and the crisis in the United States.

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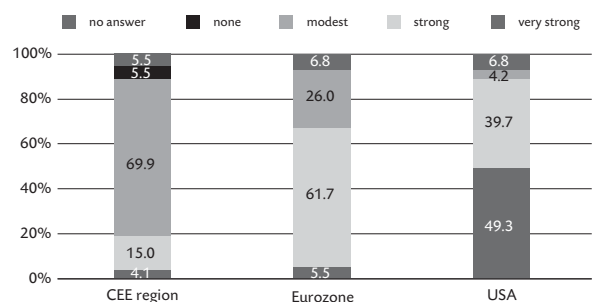


Balance of positive and negative assessment category chosen by respondents of the Financial Market Survey Switzerland. Source: ZEW

### Switzerland: Short-Term Interest Rates

Despite the trend towards rising prices, only 28.2 percent of the financial market experts anticipate that short-term interest rates for Switzerland will increase. In contrast, two-thirds of the questioned analysts foresee no change in short-term interest rate levels. Overall, the relevant indicator plunged markedly by 25.8 points to the 23.1 mark. In the wake of the recent interest rate hike by the European Central Bank to the 4.25 percent level, most of the analysts expect no change in the short-term interest rate differential between Switzerland and the Eurozone.

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Answers of the participants of the Financial Market Survey CEE. Source: ZEW

### CEE Region: Impact of the Credit Crisis

The experts were asked about the impact of the credit crisis on the CEE region, the Eurozone and the United States. 69.9 percent evaluate the impact of the credit crisis on the economies in the CEE countries as “modest”. 5.5 percent of the analysts state that the credit crunch had no bearing on the economic development in the CEE region at all. Nearly 90.0 percent of the respondents regard the influence of the credit crisis on the US economy as “strong” or “very strong”. According to the analysts, the Eurozone is caught in the maelstrom of the credit crunch as well.

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## INSIDE ZEW

## ■ ZEW Conference: Labour Economics – Theory, Empirical Methods and Current Research

From September 15 to 19, 2008, the Centre for European Economic Research (ZEW) will host an international conference on Labour Economics organized by the DFG Research Network “Flexibility in Heterogeneous Labour Markets”. The objective of the conference is to bring together PhD students, junior researchers, and senior researchers to study and discuss recent research topics in labour economics. The conference will focus for example on the theory and empirical applications of human capital, skill biased technical change and trends in wage inequality and labour force participation of older workers.

For further information visit: [www.zew.de/laboureconomics2008](http://www.zew.de/laboureconomics2008)

## ■ ZEW Conference: The Impact of Regulation on Investment and Innovation Incentives

From October 1 to 2, 2008, the Centre for European Economic Research (ZEW) will host a Conference on “The Impact of Regulation on Investment and Innovation Incentives”. A particular focus of the conference is on network-based markets, for example on telecommunications, energy, water, post and rail. The conference will focus on such topics as infrastructure regulation in alternative network-based markets, regulation and infrastructure quality as well as regulation driven research and development and its success in network-based markets.

For further information visit: [www.zew.de/regulation2008](http://www.zew.de/regulation2008)

## PUBLICATIONS

## ■ ZEW Discussion Papers

No. 08-041, Thomas Zwick: Earnings Losses After Non-Employment Increase With Age.

No. 08-040, Nikolas Wölfling: Asymmetric Price Transmission in Supply Function Equilibrium, Carbon Prices and the German Electricity Spot Market.

No. 08-039, Thomas Zwick: The Employment Consequences of Seniority Wages.

No. 08-038, Bernd Fitzenberger, Olga Orlyanskaya, Aderonke Osikominu, Marie Waller: Deja Vu? Short-Term Training in Germany 1980-1992 and 2000-2003.

No. 08-037, Christoph Grimpe, Katrin Hussinger: Market and Technology Access Through Firm Acquisitions: Beyond One Size Fits All.

No. 08-036, Horst Entorf, Florian Gattung, Jochen Möbert, Immanuel Pahlke: Aufsichtsratsverflechtungen und ihr Einfluss auf die Vorstandsbezüge von DAX-Unternehmen. (only in German)

No. 08-035, Christian Rammer, Anja Schmiele: Drivers and Effects of Internationalising Innovation by SMEs.

No. 08-034, Kathrin Müller: University

Spin-Off's Transfer Speed – Analyzing the Time from Leaving University to Venture.

No. 08-033, Birgit Aschhoff, Wolfgang Sofka: Successful Patterns of Scientific Knowledge Sourcing – Mix and Match.

No. 08-032, Sandra Gottschalk, Sebastian Theuer: Die Auswirkungen des demografischen Wandels auf das Gründungsgeschehen in Deutschland. (only in German)

No. 08-031, Ivo Bischoff: Conditional Grants, Grant-Seeking and Welfare when there is Government Failure on the Subordinate Level.

No. 08-030, Pedro Faria, Wolfgang Sofka: Formal and Strategic Appropriability Strategies of Multinational Firms – A Cross Country Comparison.

No.08-029, Astrid Dannenberg, Sara Scatata, Bodo Sturm: Does Mandatory Labeling of Genetically Modified Food Grant Consumers the Right to Know? Evidence from an Economic Experiment.

No. 08-028, Friedrich Heinemann, Michael Overesch, Johannes Rincke:

Rate Cutting Tax Reforms and Corporate Tax Competition in Europe.

No. 08-027, Friedrich Heinemann, Philipp Mohl, Steffen Osterloh: Who's Afraid of an EU Tax and Why? – Revenue System Preferences in the European Parliament.

No. 08-026, Ulf Moslener, Bodo Sturm: A European Perspective on Recent Trends in U.S. Climate Policy.

No. 08-025, Dieter Nautz, Sandra Schmidt: Monetary Policy Implementation and the Federal Funds Rate.

No. 08-024, Benny Geys, Friedrich Heinemann, Alexander Kalb: Voter Involvement, Fiscal Autonomy and Public Sector Efficiency: Evidence from German Municipalities.

No. 08-023, Niels Anger, Christoph Böhringer, Ulrich Oberndorfer: Public Interest vs. Interest Groups: Allowance Allocation in the EU Emissions Trading Scheme.

No. 08-022, Johannes Germandt, Friedrich Pfeiffer: Wage Convergence and Inequality after Unification: (East) Germany in Transition.



Zentrum für Europäische  
Wirtschaftsforschung GmbH

I M P R I N T

ZEW news English edition – published quarterly

**Publisher:** Centre for European Economic Research (ZEW) Mannheim,  
L 7, 1 · D-68161 Mannheim · P.O. Box 10 34 43 · D-68034 Mannheim · Internet: [www.zew.de](http://www.zew.de) · [www.zew.eu](http://www.zew.eu)  
President: Prof. Dr. Dr. h.c. mult. Wolfgang Franz · Business and Administration Director: Thomas Kohl

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