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On 1st April 2005 Prof. Dr. Simon Evenett joined our Institute. He is of British nationality, studied at Cambridge University and earned his PhD in economics at Yale University. He has held academic positions at the University of Michigan, Rutgers University, University of Berne, and the Saïd Business School at the University of Oxford before coming to St. Gallen. Between 1998 and 2002 he worked with World Bank as an economist.

This is a good occasion to focus the editorial on the international orientation of the Institute. Analysing foreign trade opportunities and the evolving nature of the world economic order were prime motivations for the creation of the Institute in 1943. The reconstruction of world economic order was one of the main challenges that was foreseeable towards the end of World War II. The Institute’s main objective was to carefully observe and analyse trends in the multilateral trading system and to provide Swiss authorities with good analysis to inform their decisions. As a second main objective, the Institute was to undertake market studies in order to assess commercial opportunities for Swiss firms. Firms, and the economy in general, had to be prepared for a major shift of market forces. Scarcity of goods was, for the unprepared, to be replaced by scarcity of market opportunities.

The activities of the Institute have changed and expanded over time. First, conditions for long term growth, then, regional economics, and, finally, economic policy in general came on to our research agenda and influenced our consulting activities. Consistent with this, since many years the Institute hosts a strong group of empirical labour market researchers. Even so, the international orientation remains an important pillar of our activities. This is also reflected in the composition of our Förderungsgesellschaft (Association of Sponsoring Institutions), which comprises well-known Swiss firms with global reach. The journal *Aussenwirtschaft* has been published for more than 60 years and, with its policy orientation, creates a link between academic analysis and policy discussion in the broad area of international commerce.

Against this background, we are very pleased that Prof. Dr. Simon Evenett accepted the job offer of the University of St. Gallen and joined our Institute. He complements and reinforces our activities both with his thematic background and with his rich international network. He has very good contacts to international organisations such as the World Bank, UNCTAD, the OECD, and the WTO. Has leads a number of international research projects and networks in the area of international competition law and policy, and he is well known for his policy statements. Given today’s discussions and frictions, we particularly welcome the fact that he has done much research and consulting on the question of how to best to integrate developing countries into the world economy.

Prof. Dr. Heinz Hauser has led the International Economics Section of the Institute for over 20 years now. Besides his professional interests in international economics, he has been a driving force in internationalising teaching programmes at the University. He started establishing exchange opportunities with a large number of universities abroad in the last decade. During 1995 - 1999 he served as Chairman of a network of leading European Business Schools (Community of European Business Schools - CEMS). Together with Prof. Dr. Roland Kley he planned and implemented a new study programme *International Affairs and Governance*, and he represents the University of St. Gallen in the *Association of Professional Schools in International Affairs*, which comprises the leading schools in this field worldwide.

International orientation is not only prevalent in the International Economics Section, but is an important characteristic of the other sections too. In addition to projects for Swiss authorities, the labour market group of Prof. Dr. Michael Lechner works on substantial multi-year consulting projects for
the German Bundesagentur für Arbeit. In 2005 projects for the Austrian and the Serbian government were added to this research portfolio. The labour market group is also strongly involved in the international academic debate and collaborators present their findings at international academic conferences. Prof. Dr. Michael Lechner is member of several editorial boards of international journals in the area of labour market economics.

Prof. Dr. Gebhard Kirchgässner has focused his research on a topic which seems to be very Swiss: the economic and political impacts of different forms of direct democracy and federalism. But his research has also gained a high international profile and reputation. He has presented his research findings at various academic and non-academic conferences in Germany and elsewhere. He represents Switzerland in the project titled "The Practice of Fiscal Federalism: Comparative Perspectives" within the international network "A Global Dialogue on Federalism", which is a joint initiative of the Forum of Federations and the World Bank. He sits on the Scientific Board of the Initiative and Referendum Institute of the University of Southern California. Until May 2005 he served as president of the European Public Choice Society.

We are convinced that the strong international orientation of our institute’s activities strengthens the reputation of our university and the St. Gallen region and helps to realise benefits of an international university for the region; the latter being stated by the Rectorat as a strategic goal in implementing the University Governing Board’s Vision 2010. The Canton of St. Gallen provides us with a high degree of autonomy which facilitates our international orientation; a governing structure for which we are thankful to the authorities. Our thanks go also to the members of the Institute’s Association of Sponsoring Institutions, chaired by Erika Forster, member of the Swiss Upper Chamber, who support us financially and provide valuable suggestions and advice. Last but not least, our special thanks go to all our collaborators. Without their ongoing high commitment we could not maintain our high level of activity - in the national and international arenas.

St. Gallen, 24th March 2006

Prof. Dr. Heinz Hauser
Prof. Dr. Gebhard Kirchgässner

Prof. Dr. Michael Lechner
Prof. Dr. Simon Evenett
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Prof. Dr. SIMON EVENETT

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MARTIN GEDULT VON JUNGENFELD
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FELIX BRILL (until 31 July)
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3. Research Activities

3.1 Section International Economics

Directors: Prof. Dr. Heinz Hauser

Researchers:
INGO BORCHERT
MARTIN GEDULT VON JUNGENFELD
PHILIPP JUNG (bis 30. Juni)
SANGEETA KHORANA
SHUNRONG LIAO (until 28 February)
PATRICK RUDOLPH (since 1 October)
MELANIE STAUFFER (until 30 June)

Prof. Dr. Simon J. Evenett (since 1 April)

STEPHANIE KOTHMILLER (since 1 August)
MICHAEL MEIER (since 15 July)
MARIA MAGDOLNA TARISKA (since 1 August)

Secretariat:

EDITH MEMETI-KELLER

Student Research Assistant:
ETIENNE HUBER (since 10 May)

Heinz Hauser
Simon J. Evenett

I. BORCHERT
E. HUBER
M. GEDULT
P. JUNG
S. KHORANA
S. KOTHMILLER
S. LIAO
M. MEIER
P. RUDOLPH
M. M. TARISKA
E. MEMETI-KELLER
A) General Objectives of Our Research

On 1st April 2005 Prof. Dr. SIMON EVENETT joined our Institute. Together with Prof. Dr. HEINZ HAUSER he chairs the International Economics Section and contributes in particular his rich international research and consulting network. Both share a strong belief that the Institute’s activities should be based on rigorous theory but have a strong policy orientation.

Much of our research is devoted to developing a better understanding of the multilateral trading system and its consequences for international commerce and for the wealth of nations. An important objective is to undertake research that is of interest to scholars, policymakers, and to leading business people and members of civil society who follow developments in the multilateral trading system. As a result, our research often draws upon institutional knowledge and recent policy proposals as well as using microeconomic tools and econometrics. In this respect a challenge often faced is to maintain academic rigour without losing the non-academic audience for our research. The dissemination of our research to many different fora is a complementary objective, and considerable lengths are taken to present our research at academic conferences, at international organisations such as the OECD, WTO, UNCTAD, World Bank, and regional development banks, and to non-specialist audiences. Given the diverse audiences for our research findings, it is not surprising that our writings are published in a wide range of different formats and sources.

As part of our general orientation we are convinced that dissertation projects are an important source of research at our Institute. In 2005 two SIAW-affiliated dissertations have been published by internationally renowned publishers: SACHA WUNSCH-VINCENT, The WTO, the Internet and Trade in Digital Products – EC-US Perspectives, Oxford: Hart Publishing; and THOMAS A. ZIMMERMANN, Negotiating the Review of the WTO Dispute Settlement Understanding, London: Cameron May. Congratulations to the authors.

B) The Team

PROF. DR. SIMON J. EVENETT, Ph.D. (at SIAW since 2005) took up his post of Professor of International Trade and Economic Development, Department of Economics, University of St. Gallen, on 1 April 2005 and became a Director of the SIAW at the same time. He serves on the Programme Commissions for the Department of Economics’ Ph.D. Programme for Economics and Finance and the HSG Executive School of Management, Technology and Law. He teaches in many different courses with an international orientation in HSG’s various teaching programmes. His research interests cover international trade in general, with some focus on international competition policy at the moment.

PROF. DR. HEINZ HAUSER chairs the International Economics Section since 1981 (since 2005 jointly with PROF. DR. SIMON EVENETT). He is member in the Programme Committee of the Bachelor and Master Programme in International Affairs and Governance where he mainly teaches international economics courses. He is managing editor of the journal Aussenwirtschaft and the WTO-News. In his research, he concentrates on basic institutional questions regarding the WTO and its Dispute Settlement Process.

After his departure from the Institute, DR. THOMAS ZIMMERMANN was elected Research Associate. He continues to support the publication of the WTO-News – the newsletter he initiated and developed in the following years with great care. Moreover, he teaches, on behalf of the Institute, in management seminars on the international economy.

DR. SACHA WUNSCH-VINCENT has also kept close contact to our Institute as Research Associate. He is working with the OECD in a unit on digital trade.

INGO BORCHERT is graduate of the Gerzensee doctoral programme and has joined the new PhD Programme in Economics and Finance. Starting with 1st February 2006 he received a grant from the
Swiss National Research Foundation to continue his studies at American and British Universities. Until March 2005 he was editorial assistant of the journal *Aussenwirtschaft*.

Martin Gedult von Jung enfeld’s dissertation project concentrates on the relationship between liberalisation of financial services in the WTO and liberalisation of the capital account in the balance of payments. He is editorial assistant of *WTO-News*, which in this case includes not just the usual editorial tasks but also much of the production.

Sangeeta Khorana is close to completing her dissertation on the subject of “Preferential treatment of developing countries in tariff-rate quota systems”. She has been offered a position as lecturer at a British university. Congratulations to her on this success.

Patrick Rudolph joined the Institute 1st October 2005. His dissertation interests are in the area of economic and technical development co-operation.

Stephanie Kothmiller (1st August), Michael Meier (15th July), and Maria Magdolna Tariska (1st August) support Prof. Dr. Simon Evenett in his research activities. Michael Meier’s Masters thesis on “Das Engagement der Schweiz in den Konflikten im ehemaligen Jugoslawien” was accepted for publication by Peter Lang Verlag, Bern.

Etienne Huber is editorial assistant for the journal *Aussenwirtschaft*.

During 2005, Philipp Jung, Shunrong Liao and Melanie Stauffer have left the Institute to take a position in private business. They plan to finish their dissertations in parallel to their job commitments.

C) Own Publications

1. Journal *Aussenwirtschaft*

The Institute publishes the journal *Aussenwirtschaft* and had done so for over 60 years. Since its start, the journal has been devoted to bridging the gap between theory and practise. This aim manifests itself in a number of characteristics: The journal addresses with priority topics that play an important role in the economic policy discussion. The contributions should be well-founded in theory but – through their presentation – easily accessible for practitioners. It is also an important goal of the journal to present research contributions or economic policy statements made by members of the Institute to a wider public.

WTO-related topics are of special relevance also for the 2005 volume. Among the contributions addressing specific issues, papers dealing with EU-trade policy in the new constitutional contract, bilateral co-operation agreements of Japan, and employment effects of trade in intermediate inputs should be particularly noted. The following members of the Institute have written contributions: Prof. Dr. Simon Evenett (Can the WTO Rise to the Challenge of Economic Development?), Prof. Dr. Gebhard Kirchgässner (Optionen für die Armen: Eine ökonomische Perspektive) and Dr. Thomas A. Zimmermann (WTO Dispute Settlement at Ten: Evolution, Experiences and Evaluation). The expectation that the journal should provide thorough analyses of topical economic policy issues has been met.

2. *WTO-News*

In addition to the journal *Aussenwirtschaft*, our newsletter *WTO-News* is another very important instrument to position the Institute internationally. On four pages, two important issues related to the international economic order are discussed. The contributions deal with systemic WTO questions and
comment on important dispute settlement cases. Moreover, short book reviews provide information on new literature which is worth reading.

In 2005, two newsletters were published. On the occasion of the 10th anniversary of the WTO, one comment took stock of achievements and risks for the future development of this organisation. A second commentary highlighted the new proposals on aid for trade. Among the Dispute Cases discussed, the U.S. Cotton Case is of particular interest. The WTO’s Panel and Appellate Body have formulated far-reaching conclusions, not just for the case in question, but for the interpretation of central parts of the Agreement on Agriculture.

The *WTO-News* is a powerful instrument to make the voice of the Institute heard in the international discussion. Approximately 1500 individuals or institutions receive the German-language version of the newsletter – either in print or electronically. The English-language version is distributed to roughly 2500 recipients electronically. As we have included in our database only recipients with a clear interest in international trade matters, our Institute has now at its disposal an instrument that reaches a wide and well-informed audience. This fact is confirmed by the significant number of readers’ reactions and comments that reach us from around the world.

**D) A WTO-Related Research Focus**

As already noted, in the last few of years the International Economics Section has primarily been dealing with WTO-related questions. Prof. Dr. HEINZ HAUSER has published papers addressing institutional issues. Prof. Dr. SIMON EVENETT is managing a multi-year research project on the accession process of new members. But the research focus is also supported by dissertation projects of our staff members. Dr. AXEL FLASBARTH analysed empirically important questions concerning the inclusion of labour standards in the world trading order. Dr. ALEXANDER ROITINGER examined the general tension that exists between binding rules and flexibility in the WTO-order. Dr. THOMAS ZIMMERMANN looked at the proposals for the reform of the WTO dispute settlement system that have been put forward since 1995 and analysed their potential systemic implications for the WTO. Dr. SACHA WUNSCHEVINCENT provided one of the first comprehensive studies on the treatment of digital content services in the WTO.

In addition to these successfully completed works, other dissertation projects dealing with WTO issues are currently being undertaken at the Institute: The effects of GATS commitments on the Chinese banking market (MIKE IMAM), Preferential treatment of developing countries in tariff-rate quota systems (SANGEETA KHORANA), GATS liberalisation of financial services and capital account restrictions (MARTIN GEDULT VON JUNGENFELD), Reform of the WTO-dispute settlement system – The new rebalancing paradigm (SIMON SCHROPP), The protection of traditional knowledge in the world trading order (XUAN LI), Financial sector transformation in the Ukraine before WTO accession (VITALIY NOVIKOV), Regional and multilateral integration of the Euro-Asian Countries (SVETLANA NURMASHEVA).

Through focusing the dissertation projects on one common thematic area, it is possible to yield synergies and to facilitate the exchange of ideas among doctoral students. For the Institute, this supports building a research programme that is made possible largely through the self-financed work of our doctoral students.
E) Current Projects (Prof. Dr. Simon Evenett)

1. Promoting Competitive Markets in Developing Countries

This multi-year project is funded by the Canadian International Development Research Centre (IDRC) and began in 2003. The project will be completed in the middle of 2006 and this report refers to the activities in 2005. Prof. Dr. Simon Evenett leads this project which includes two types of research. The first type involves in-depth analyses of the level and determinants of competition in the markets of six large developing countries. The goal of these country studies is to better understand the impediments to competition in these emerging markets and the contribution, if any, that competition law and policy can make to promoting rivalry between firms. The second type of study examines competition-related matters that are relevant to many countries. To that end, analyses of (i) export cartel exemptions from national competition laws, (ii) rights for victims harmed by international cartels, (iii) the degree and determinants of national conformity with the merger-related recommendations of the International Competition Network, (iv) the relevance of the competition advocacy-related recommendations of the International Competition Network and the Organisation for Economic Co-operation and Development for developing countries, (v) the prevalence of anti-competitive practices in Sub-Saharan Africa, and (vi) the implications for competition agencies of case studies of prior enforcement actions were undertaken during 2005. A conference involving all of the relevant authors, plus leading international competition experts, was held in Buenos Aires in March 2005. Prof. Dr. Simon Evenett coordinates the group of researchers from ten countries that are participating in this project as well as contributing to the substantive development of each of the papers written.

2. Preparing For and Evaluating WTO Accessions

This multi-year project is funded by the Canadian International Development Research Centre (IDRC) and began in 2004. The project will be completed in the middle of 2006 and this report refers to the activities in 2005. Prof. Dr. Simon Evenett leads this project. Since the World Trade Organization (WTO) was established in 1995 twenty countries have joined. The terms upon which those countries have joined, and the time taken, are said to have become more onerous. The purpose of this research project is to examine the economic and legal consequences of several WTO accessions and to draw implications for those developing countries still seeking to join the WTO. Five developing countries were also selected for so-called process studies whereby the manner in which their respective governments prepared for WTO accession negotiations was described and assessed. In cooperation with the World Bank’s Geneva office, a conference was held at the Palais des Nations, Geneva, in January 2006 to discuss the project’s findings. The research presented at that workshop was revised afterwards and a volume is expected to be published in 2006/2007. In the middle of 2005, Prof. Dr. Simon Evenett co-authored with a senior World Bank official a “Trade Note” that received considerable attention.

3. Competition Policy For Trade and Regulatory Reform

This one year-long project took place during 2005 and was funded by the European Commission under the Sixth Framework Programme. Prof. Dr. Simon Evenett is the coordinator of this project and to date is the only HSG professor to be awarded such a grant under the Sixth Framework Programme. This substantial project involved the drafting of over twenty research papers by scholars located in Europe, South Africa, Brazil, and elsewhere. The project addresses research questions concerning the complementarities between competition policy and other policies; the factors accounting for the adoption and implementation of competition laws in developing economies; the modalities and effectiveness of bilateral agreements on cooperation on competition law-related matters; and analyses of regional approaches to trade and competition matters. During 2005 Prof. Dr. Simon Evenett organised three conferences for this project and these took place in Brussels and Paris. The findings of this re-
search were also presented at the Fifth UN Conference on Competition Policy in Antalya, Turkey, at the OECD’s Joint Group on Trade and Competition, and at the Polish Competition Office in Warsaw.

4. Competition Law and Policy in Asia

This multi-year project was funded by the Asian Development Bank and began in 2003. The project was completed in 2005 and resulted in the publication of an edited volume by Palgrave Macmillan. Prof. Dr. SIMON EVENETT was the technical advisor to this project and contributed three chapters to the edited volume. Six country studies of the determinants of competition in selected Asian economies were completed as part of this project, using a template that was similar to the one that Prof. Dr. SIMON EVENETT devised for the Promoting Competitive Markets in Developing Countries project (described above).

5. Other Projects

During 2005, Prof. Dr. SIMON EVENETT was involved in a number of other research and public policy projects. With respect to the former, he completed research papers on anti-dumping matters, so-called aid for trade, the U.S. trade policy of “Competitive Liberalization,” the competition provisions of regional trading agreements, and the relationship between anti-competitive practices and reforms in Latin America and the Caribbean. Together with BERNARD HOEKMAN he co-edited a volume on the potential contribution of the WTO to economic development, whose publication was timed to coincide with the WTO Ministerial Conference held in Hong Kong, China, in December 2005. In addition, Prof. Dr. SIMON EVENETT served as the Rapporteur of the OECD’s Global Forum on Special and Differential Treatment. He assisted the Government of Mauritius in training their officials on Non-Agricultural Market Access matters. Moreover, he acted as the International Technical Project Advisor to a SECO-funded UNCTAD project on capacity building in competition law and policy in five Latin American countries.

F) Major Publications


MICHAEL MEIER, *Das Engagement der Schweiz in den Konflikten im ehemaligen Jugoslawien*, Peter Lang Verlag, Bern et al., 2006.


3. **Research Activities**

3.2 **Section Economic Policy**

*Director:* Prof. **Gebhard Kirchgässner**

*Researchers:*
- Dr. **Justina A. V. Fischer** (until 30 September)
- **Silka Prohl**
- **Thorsten Uehlein**

*Student Research Assistants:*
- **Michael Dominic Bauer** (until 31 January)
- **Felix Brill** (until 31 July)

*Secretariat:*
- **Gabriela Schmid**
A) General Objectives of Our Research

The research undertaken in 2005 by our department can be divided into two parts. First, our research in the field of direct democracy and federalism continued. While the Swiss National Science Foundation project on the political economy of direct democracy was formally finished, research on this topic carried on. In addition, the effects of federal systems were empirically investigated, in particular in the context of the "Global Dialogue on Federalism," that is promoted by the Forum of Federations, Ottawa, and the World Bank. Prof. Dr. GEBHARD KIRCHGÄSSNER is the Swiss Country Coordinator for the sub-project titled "The Practice of Fiscal Federalism: Comparative Perspectives". Work in this field was done in cooperation with Prof. Dr. LARS P. FELD (University of Marburg) and Dr. CHRISTOPH A. SCHALTEGGER (Swiss Federal Tax Administration), two former colleagues of our department.

Second, a substantial part of our time has been spent on the annual report of the Kommission für Konjunkturfragen (Council of Economic Experts) which last year was dedicated to the topic "Economic Effects of an Aging Society". Besides these two main strands a significant fraction of our resources was invested in completing a textbook on time series econometrics, written in collaboration with Prof. Dr. JÜRGEN WOLTERS (Free University of Berlin).

B) The Team

PROF. DR. GEBHARD KIRCHGÄSSNER is director of the Department for Economic Policy. Since January 2004, he is also the President of the Kommission für Konjunkturfragen (Council of Economic Experts) of the Swiss government. In his research he focuses on current topics in economic and especially fiscal policy, on questions of political economy, in particular in connection with the Swiss institutions of direct democracy and federalism, and on basic methodological questions of the economic and social sciences.

DR. JUSTINA A.V. FISCHER had been a member of our team since April 2002. She was mainly engaged in the project on the political economy of direct democracy whose financing ended in December 2004. Both in this project and in her dissertation, she carried out research on the societal consequences of direct democracy. After having completed her dissertation, Mrs Fischer has been awarded a fellowship by the Swiss National Science Foundation allowing her to pursue research at the London School of Economics and at the George Mason University in Fairfax (Virginia) beginning in January 2006.

SILKA PROHL has been a team member since July 2005. In the first half of 2005 she was working on a project on the sustainability of the Swiss federal government which was financed by the research commission of the University. SILKA PROHL continues empirical research on developments in the public sector finances.

THORSTEN UEHLEIN has been a team member since autumn 2003. In his doctoral thesis he deals with questions on tax competition and tax harmonization in the European Union.

MICHAEL BAUER had been a staff-member in our Department since 1 September 2004. He was a student in the MiQE/F programme of our University. At the end of January 2005 he left to take up employment at the Wegelin Bank. Since September 2005 MICHAEL BAUER pursues Ph.D. studies at the University of California, San Diego.

FELIX BRILL worked for our department as a student assistant until July 2005. He attended the MECON programme.
C) Projects

1. Direct Democracy and Federalism

At first we concluded the work relating to the project "The Political Economy of Direct Democracy" which was funded under the priority programme "Switzerland: Towards the Future" of the Swiss National Science Foundation. This project led to further publications on the relation between direct popular rights and public sector finances as well as on the effect of direct democracy on public education and crime. We have already mentioned in the last annual report that more popular rights lead – ceteris paribus – to less cantonal expenditures for education. This has negative consequences on literacy but not necessarily on capabilities relating to mathematics and natural sciences. Regarding the effect of direct democracy on the fight against crime, more democratic cantons seem to exhibit a relatively stronger preference of fighting property crime over fighting violent crime.

Another paper deals with the relation between democratic rights and subjective well-being of the citizens. There are studies which show the subjective well-being is higher in Switzerland - again ceteris paribus - the more pronounced direct democratic rights in a canton are. However, if we include variables representing the language of the citizens and, thus, cultural indicators into the regression equations, the indicator variables for the direct popular rights lose their statistical significance. Apparently the effect of culture on individual perception of well-being outweighs the effect of direct democratic rights. On the international scale however the latter effect is significant again. This indicates that while in Switzerland the extent of democratic rights does affect subjective well-being, differences between cantons are too minor to be statistically significant once cultural factors are controlled for.

It is frequently asserted that direct democracy and federalism restrict economic growth in Switzerland. In earlier work we have shown that this assertion cannot be reconciled with empirical evidence. We have looked at these arguments in detail once more while preparing a report on economic growth in Switzerland for a conference of Avenir Suisse. Again we have found that the weakness in economic growth is unlikely to be caused by direct democracy or federalism; one should rather look out for other explanations. However, the current situation is unlikely to be explained by just one single cause. A therapy should entail various measures, whereas one should not expect too much of any single measure.

2. Economic Consequences of an Aging Society

Studies in this field arose in the context of the annual report of the Council of Economic Experts which explicitly dealt with this subject in 2005. The starting point is the significant change in the age structure of the Swiss population which is caused by two distinct developments. On the one hand, the life expectancy of the population has increased, while on the other hand the number of births has strongly declined in past decades, including relative to other European countries. As a consequence the share of employed persons relative to the share of retirees declines, which raises the burden of pensions irrespective of how these are financed. At the same time the fraction of young persons is expected to decline at least temporarily. Over the next decades these developments will pose serious challenges to Swiss economic and fiscal policy.

From a societal point of view the people in the labour force have to finance consumption of all others in each period. This means that in the end only its expansion can abate the financial burden caused by an ageing society. All other measures will only shift this burden between population groups: An augmentation of social security contributions will affect employed persons, a reduction of pension payments will burden retirees, while financing by means of general taxation will affect both groups. How to optimally distribute the financial burden cannot be determined scientifically and is a political ques-
tion. Given the effects of non-wage labour costs, at least for the age and survivors insurance (AHV), additional financing via deductions on wages does not seem appropriate.

At a first glance, the distribution of this burden does not have (direct) intergenerational effects. Regarding pension funds this holds if contributions and pension payments are actuarially correct so that the individual pension depends on personal contributions. Regarding the AHV this only holds if the population structure is stable, irrespective of whether the population is increasing or decreasing. However, during the transition process of the coming years we might observe substantial shifts of the burden between generations. This might even apply to pension funds, namely if today’s provisions fall short of the requirements to pay guaranteed pensions and if in consequence contributions of the employed population are raised.

Reducing the burden by enhancing the labour force deserves however more attention than the just distribution of the burden. Given that a substantial increase in migration is ruled out for political reasons and because its long-term effects are questionable, two alternatives remain. Firstly, one could extend general employment, secondly one could focus on extending women’s employment.

An expansion of general employment requires that the statutory retirement age of 65 is raised. Even if the retirement age does not have to be raised in the next years, it should be clearly communicated to the general public that an adjustment of the age for receiving the AHV is inevitable in the long-run. In a situation of an aging society the financial burden of the social security system can only be kept from growing if the retirement age is raised accordingly. Since the statutory retirement age is also an important benchmark for people that go into early retirement, their behaviour will be affected as well.

The augmentation of the retirement age can (and probably should) be complemented with a transition to a more flexible labour market, which e.g. allows for part-time work of the elderly population. One should also discuss introducing special provisions for occupational groups that are exposed to extraordinary physical strain (e.g. early retirement depending on the contribution period). However this should not distract from the fundamental notion that the period of employment has to be raised.

Women’s employment will rise above all if compatibility of family and work is improved. This requires both organisational and financial measures. Firstly, nursery and elementary schools should be re-designed so that both family partners can work at least half-time. Secondly, the so-called ‘marriage penalty’ of the Swiss tax system should be abolished, i.e. traditional taxation of families should be replaced by splitting between spouses or individual taxation. Thirdly, child care costs should be subsidised independently of income and/or these costs should be tax-deductible. It is not reasonable that married second-wage earners with children effectively face income losses if they work five instead of three days per week.

A better compatibility of family and work should also positively affect the birth rate. Scandinavian countries with their well developed child-care systems show that also countries with high per capita income can have relatively high birth rates. Even if the population of the Scandinavian countries is declining as well, the rate of decrease has been slower and its burden is thus more moderate.

Irrespective of the extent of social security benefits, people must be sure that they finally receive the guaranteed payments. If the AHV is to continue to guarantee a minimum living income it will likely need additional funds, even if the retirement age is lifted. The necessary funds are probably raised best by general taxation. Regarding today’s situation of pension funds the first measure to take are financial reorganisations and recapitalisations. In addition contributions and promised benefits need to be balanced. This requires that regulated parameters such as the guaranteed minimum interest rate and the conversion rate are automatically and regularly adjusted to market conditions and demography. Also, the adjustment should consider (at least implicitly) real and not nominal variables. With an
automatic adjustment it would be possible to avoid political conflicts and reduce the discretionary scope.

The aging society and the decrease in population are serious challenges to Switzerland. The faster politics reacts to these challenges and the more it is based on long-term considerations, the more likely is a satisfying solution. The problem is well defined and the essential measures are known, even if they are subject to (partly substantial) need for discussion. Politicians should actively deal with these problems even if this might be unpopular at first. Since in Switzerland’s direct democracy reforms need common consent of the citizens, they have to be approached over a long time horizon and irrespective of possible momentary failures due to lost votes.

3. Applied Econometrics

A substantial part of work in this field was spent on the completion of the German version of the textbook “Introduction to Modern Time Series Analysis”. This joint project of Prof. Dr. GEBHARD KIRCHGÄSSNER and Prof Dr. JÜRGEN WOLTERS (Free University of Berlin) is based on lectures held at the Free University of Berlin and at the University of St. Gallen. The textbook emphasises practical application of methods and is intended to serve as an introduction in particular for Master level students.

A second work in this area deals with the quality of economic forecasts of the Association of German Economic Research Institutes and the German Council of Economic Experts. Since the late sixties both institutions have regularly published forecasts in autumn on the economic development in the subsequent year. It is known that such forecasts can also be based on surveys which are conducted by the Institute for Opinion Research, Allensbach, in December. These surveys cover a representative sample of the population and capture individual expectations about the coming year. Interestingly, the forecasts based on these opinion polls, which only use information that has been already available for the forecasts of the German Council of Economic Experts, outperform the professional forecasts by several criteria. In particular information contained in short term rates does not seem to be adequately accounted for by the research institutes and the Council. Thus, the general population seems to process available information more efficiently than professional forecasters.

D) Major Publications


3. Research Activities

3.3 Section Labour Market and Econometrics

Director: Prof. Dr. Michael Lechner

Researchers:
Stefanie Behncke
Dr. Markus Frölich
Blaise Melly
Dr. Ruth Miquel
Heidi Steiger

Dr. Rosalia Vazquez-Alvarez
Stephan Werner (since 1 July)
Stephan Wiehler
Conny Wunsch

Student Research Assistant:
Michael Huber (until 31 March)

Secretariat:
Edith Memeti-Keller
Gabriela Schmid

Michael Lechner

S. Behncke  M. Frölich  B. Melly  R. Miquel  H. Steiger
R. Vazquez-Alvarez  S. Werner  S. Wiehler  C. Wunsch
A) Research Goal

The fundamental goal of our research group is to develop and improve the empirical tools commonly used in the analysis of economic data. This allows for a better understanding of economic phenomena, with the additional goal of providing high quality advice for the implementation of economic policies. To attain this goal we make extensive use of econometric methods and quantitative economic analysis, develop new estimation techniques, and assemble or employ new data sources in the process using, for example, administrative data at the micro-economic level provided by national authorities. We have designed and implemented pilot applications, either independently or in co-operation with various other institutions. Once the usefulness of some new tools and data has been established, non-university institutions should be able to employ them in routine applications. We require that all projects add to the scientific knowledge base as defined by the standards of the scientific community. With that aim in mind we expect that each individual project will produce at least one, if not more, publications in good peer-reviewed scientific journals. In addition, the members of our research group have contributed to, and will continue to contribute to, national and international scientific workshops and conferences. At present, the main focus of our policy-relevant work relates to labour markets, education, and public health policy. However, this list of research topics is not exhaustive as we are constantly expanding our field of research activities when interesting issues arise.

B) The Team

During 2005 the members of our research team were active participants in the scientific community. The team produced a variety of discussion papers, technical reports, and published articles as well as participating in various scientific conferences. In addition, the group was also engaged in the teaching activities at the Department of Economics of the University (HSG). In terms of teaching-related activities the group is involved in the creation and implementation of new graduate study programmes. Details of all of these activities (both publications and conferences attended) are listed below. In what follows further detailed information on each member of the team is provided.

PROF. DR. MICHAEL LECHNER (at the SIAW since 1998), Professor of Econometrics, became chairman of the Programme Commission of the PhD Programme in Quantitative Economics and Finance (PEF) and handed over the directorship of the Masters in Economics and Finance (MIQE/F) to Professor Dr. Gebhard Kirchgässner.

DR. MARKUS FRÖLICH (since 1998) is a lecturer and adviser on Empirical Research in the Department of Economics (HSG). This position involves responsibility for providing advice on empirical economic research and on the analysis of economic data. The position is instrumental for the Department of Economics and is under the auspices of our Institute (SIAW) and is thus part of our group’s teaching activity. He also lectures in the PEF programme.

DR. RUTH MIQUEL (since 1998) took the responsibility for three large-scale research projects we conduct for the German and Austrian Employment Services. Sadly, after a long and successful period with the group, she will be leaving us in the first quarter of 2006.

DR. ROSALIA VAZQUEZ-ALVAREZ (since 2003), is a lecturer at the Department of Economics in the Bachelor, MIQE/F, and PEF programmes. In August 2005 she began to co-operate with the epidemiological research department of the World Health Organization (WHO) in Geneva.

HEIDI STEIGER (since 2000) finalised her doctoral thesis work within the new framework of the PEF programme and left us at the end of 2005.
BLAISE MELLY (since 2001), and CONNY WUNSCH (since 2002), are currently graduate students in the new PEF programme. During this last year they have made further progress towards completing their doctoral theses.

STEPHAN WIEHLER (since 2003) is in the process of developing his thesis project after successfully completing his graduate studies.

STEFANIE BEHNCKE (since 2004) has focused on the courses within the PEF programme and at the Gerzensee Study Centre.

STEPHAN WERNER (since 2005) was admitted to the PEF programme and has since started his graduate studies at the Gerzensee Study Centre.

C) Current Projects

1. Active Labour Market Policies in Switzerland

During the last two years (2004-2005) the research group started with two large-scale research projects on the effectiveness of Active Labour Market Policy in Switzerland. These projects are being conducted on behalf of The Office of the Secretary of State for Economics (seco). Both projects have as their goal finding means to encourage the unemployed back into active labour market participation. The participants in both projects are STEFANIE BEHNCKE, MARKUS FRÖLICH, MICHAEL LECHNER, and HEIDI STEIGER.

In the first project the efficiency of The Public Employment Agency in Switzerland is being examined with the aim of developing suggestions to increase its effectiveness. The Public Employment Agency was created in the mid-1990s by the Regional Employment Agencies (RAV). Each Regional Agency differs with regard to its structures, strategies, and procedures. These differences as well as changes over time are exploited in order to compare the reintegration of the unemployed across different RAVs, as well as to better understand any linkages to the organisational structures of RAVs. The different characteristics of these regional organisations are, for example, employer orientation, specialisation in terms of the advice offered by their caseworkers, the qualification structure of these advisors, and the strategies and procedures of both the regional leaders and the advisors.

Micro-econometric estimation methods can provide evidence on the comparative effectiveness of the consulting strategies of caseworkers and, consequently, a better understanding of the potential improvement in their organisational structure and their consulting strategies. At the end of 2004, all advisors and team leaders working at every RAV office were asked to participate in a written questionnaire: 84% of those who were asked to participate in the survey returned completed answers! The information from this questionnaire was combined with administrative data on all unemployed individuals (AVAM/ASAL) and data on unemployment insurance (AHV), both sets providing information going as far as ten years back. By linking data from each job-seeker with data from his or her employment advisor, it is possible to understand the effect of the characteristics and strategies of the advisors on the job-seeker’s employment chances, isolating these from the characteristics of the RAV organisation. This empirical study may yield future advice on the improvement in the effective placement of job-seeking workers. The first empirical results are expected at the beginning of 2006.

The second project, the Statistical Assisted Programme Selection (SAPS), aims at helping advisors in the Regional Employment Agencies (RAV) to place job-seekers in the appropriate programme. In 2005 a pilot study was conducted in 21 RAV offices. Randomly selected advisors received programme and
individual-specific expected employment outcomes for their clients via an internet based expert system, which had been developed by us. This pilot study was continuing through to December 2005. In early 2007, about one year later, we will investigate whether clients with an advisor who received our support were more successful in finding a job than those with advisors who did not receive that support. The basis of this pilot project is to study the success of “profiling” versus “targeting”, a strategy that was already presented in the SECO performance during 2002, as well as having received large attention in other countries.

2. Active Labour Market Policies in Germany

MICHAEL LECHNER, RUTH MIQUEL, and CONNY WUNSCH conducted two relatively large research projects on behalf of the Institute for Employment Research, which is part of the German Federal Employment Agency. Using micro-econometric techniques these projects studied the effects of various nationwide vocational education measures on the success of finding employment in Germany for those who participate in such programmes. These types of measures represent one of the most important components of Active Labour Market Policies in Germany. The aim of these two research projects is to better understand the effectiveness of such labour market measures. Both research projects rely on extensive administrative micro data sets. These data are very rich and informative which makes it possible to study the potential effects of heterogeneity with regard to both the labour market measures and the participants in these programmes.

The results for West Germany, which cover programmes conducted in 1993-1994, show that in the short-run for all of the labour market measures examined, the programmes had negative effects in terms of job creation (corresponding to the often found ‘Lock-in’ effects of such programmes). However, four years after their implementation the results suggest that most programmes have a positive effect on employment chances. Estimates for East Germany for the same period are somewhat similar: the initial effects of all programmes are negative but in the long-run the programmes have a positive employment effect. The main difference is that the employment services misjudged the development of the East Germany economy which had severe consequences for all those unemployed. Many people were retrained for the construction sector, a sector that was booming initially but was then hit by a substantial recession.

3. Active Labour Market Policies in Austria

The third country for which we conducted evaluations of active labour market policies is Austria. The project started in May 2005 and is in direct co-operation with the Austrian Federal Ministry for Economics and Labour (BMWA). This project is under the direction of MICHAEL LECHNER. Using administrative data and modern micro-econometric methods the analysis focuses on the effect of heterogeneity on the different programmes. Other members of this research group are RUTH MIQUEL, STEPHAN WERNER, and STEPHAN WIEHLER. The project is expected to end in February 2007.

4. Econometric Methods

Unemployed individuals are often subject to a sequence of labour market measures during an unemployment spell, which suggests a dynamic rather than a static treatment is more appropriate. These cases are particularly common in European countries. Static econometric evaluation methods cannot be applied that easily to these dynamic problems. MICHAEL LECHNER and RUTH MIQUEL have developed dynamic causal models that allow for an analysis of dynamic sequential programmes. MICHAEL LECHNER proposed estimation methods for this dynamic model and applied them to both simulated and actual job market data from both Germany and Switzerland.

BLAISE MELLY further developed quantile regression methods. Quantile regression can be regarded as an extension of the classical least squares method to take account of conditional expectations so as to estimate a variety of models using conditional quantile functions. In his new paper “Estimation of coun-
"terfactual distributions using quantile regression" he proposes two new methods for estimating the effect of a treatment on the independent distributions of the variables under study. The first method is based on parametric assumptions and the second is based on a completely nonparametric identification strategy. The asymptotic characteristics of both approaches were developed analytically and procedures suggested for the estimation of the relevant variances. Monte Carlo simulations show that these approaches behave well in small and middle-sized samples. The methods have been applied to actual data on potential racial discrimination in the USA.

5. Other Research Projects

Ongoing research continues in the context of the research programme "Education, Training and Job Market Search: Policy Analysis in the Context of a General Equilibrium Model for Switzerland (2003-2005)" financed by the Swiss National Fund and conducted by MICHAEL LECHNER and ROSALIA VAZQUEZ-ALVAREZ. This programme includes the theoretical and empirical development of life-cycle models of employment, as well as income and human capital formation models that can shed light on the effect of active labour market policies on labour market choices and accumulation of human capital. These models yield improved methods for evaluating the different active labour measures available to the unemployed. Swiss panel data like the Swiss Labour Force Survey (SAKE) were used in the first empirical implementations of the model.

MARKUS FRÖLICH has started research on the quality of education in developing countries with a first stage of research on primary schools in Africa. In the first project he examined the effect of having school books for studying French and Mathematics on the quality of schooling. His first results show positive effects on learning success. However, the results show some externality effects of school books held by peers. In other words, a pupil's learning success does not only depend on whether he or she has a book, but also on the total number of books available to the class. The reasons for this externality are probably to a large extent attributable to changes in terms of teaching methods. The potential consequence of these externalities is that the private incentives result in too few school books being bought in comparison to the social optimum, since the school children free-ride to a large extent on the availability of books owned by peers.

A second research project addresses the effect of reforms on school-teachers contracts in some African countries. A couple of years ago many of these countries started to offer school-teachers limited term contracts with durations of only a few years, with substantially lower salaries, as well as significantly reduced educational requirements. Such a step seemed necessary since the public expenditures for education increased due to the very high population growth while a variety of public services were no longer eligible for financing. Thus, the aim of this research project is to examine whether the reform, which led to large savings in public expenditures for education, has also led to a degradation in the quality of education. Initial results seem to suggest that this is not necessarily the case.

D) Major Publications


