

# PRICE AND COST COMPETITIVENESS

EUROPEAN COMMISSION

DIRECTORATE-GENERAL FOR ECONOMIC AND FINANCIAL AFFAIRS

ECFIN/C-1

Fourth quarter 2002

**Quarterly data on price and cost  
competitiveness of the European  
Union and its Member States**

## **DEVELOPMENTS IN THE COST COMPETITIVENESS OF THE EUROPEAN UNION, THE UNITED STATES AND JAPAN**

### **MAIN FEATURES**

#### **The euro against major international currencies:**

- Pursuing its appreciating trend over the fourth quarter, the euro gained on average 4% against the US dollar, 5% against the Japanese yen, 2% against the pound sterling and remained stable against the Swiss franc.
- All in all, the nominal effective exchange rate of the euro against the currencies of 12 industrialised countries appreciated by about 2½% during the fourth quarter of 2002. However, in December, it still stood about 4% below its inception-level (monthly data). Over the fourth quarter, the dollar, the pound sterling and the Japanese yen depreciated in effective terms by 1½%, ½% and about 3% respectively.

#### **Relative cost and price indicators: international developments**

- The appreciation of the euro exchange rate led to a deterioration of the cost competitiveness (based on ULCE) of euro area producers (against 12 industrialised countries) of about 1% in the fourth quarter of 2002. Cost competitiveness of the euro area producers deteriorated by 7% compared to one year ago but is still (9½%) above its long-term average.
- Despite its depreciation against the euro, the real effective exchange rate of the US dollar has been relatively stable over the fourth quarter. However, earlier depreciation led to a gain of 6% in terms of cost competitiveness over the year. Nevertheless, the real effective exchange rate of the US dollar is still 11% above its long-term average. The larger depreciation of the yen, notably against the euro, induced an improvement of 4% of the Japanese cost competitiveness over the last quarter. Consequently, the Japanese cost competitiveness is some 15% above its historical average.

#### **Relative cost and price indicators: intra-EMU developments**

- Over the *last two years*, the Netherlands, Spain, and Portugal saw a deterioration in cost competitiveness relative to EMU partners. In these countries, cost and price pressures are related to *inter alia* their strong cyclical position. In contrast, moderate wage increases or weaker cyclical positions led to an improvement in intra-EMU cost competitiveness in France, Germany and Austria.
- In a *longer term perspective*, intra-EMU cost competitiveness is better than its 1987-01 average in France and Austria and considerably better in Finland, but this large deviation is related to the economic shocks that occurred in the early 90s, including the collapse of trade with the former Soviet Union. The current position in Portugal, Greece, Spain and the Netherlands is considerably worse than their long-term average, partly due to a catching-up process.

#### **Relative cost and price indicators: Member States outside the euro area**

- Despite the small improvement against the euro area over the last year, the Danish price and cost competitiveness is still down compared to its 1987-01 average, partly due to less moderate wages. Although Sweden experienced a small deterioration of price and cost competitiveness over the last year, it is still in a favourable position as it stands some 10% above its historical level.
- Despite an improvement over the last two years, manufacturing cost competitiveness in the UK remains about 28% below its 1987-01 average relative to the euro area.

# DATABASE ON PRICE AND COST COMPETITIVENESS

## QUARTERLY REPORT - FOURTH QUARTER 2002

### I. INTERNATIONAL DEVELOPMENTS

Chart 1 **The euro against USD and JPY since changeover**

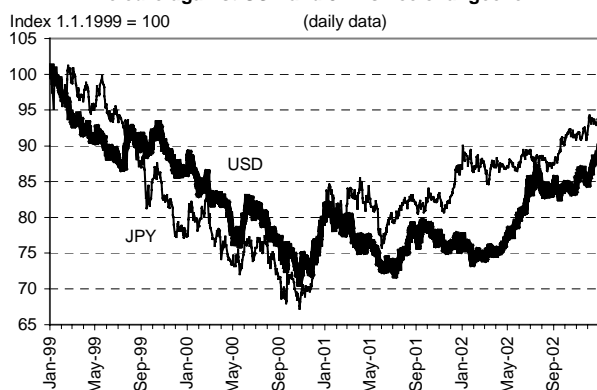


Chart 3 **The euro against GBP and CHF since changeover**

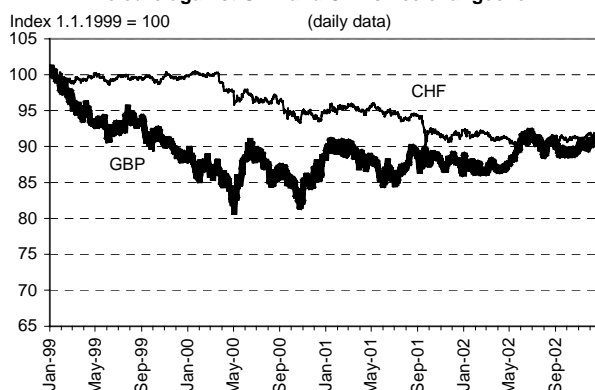
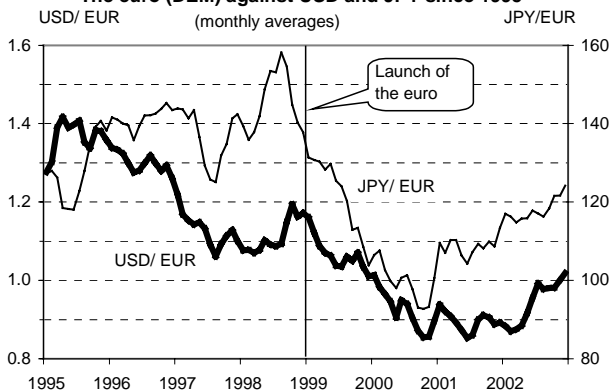
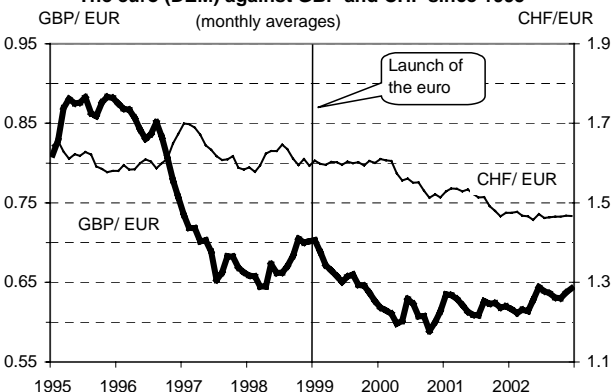


Chart 2 **The euro (DEM) against USD and JPY since 1995**



Note: EUR rates before 1999 calculated on the basis of DEM rates.

Chart 4 **The euro (DEM) against GBP and CHF since 1995**



Note: EUR rates before 1999 calculated on the basis of DEM rates.

### 1. BILATERAL EXCHANGE RATES OF THE EURO

TABLE 1: EVOLUTION OF THE MAIN BILATERAL EXCHANGE RATES

	During the fourth quarter of 2002 (monthly averages)			Relative to the previous quarter (quarterly averages)		
	Average Sep-02	Average Dec-02	% change	Average Q3-02	Average Q4-02	% change
USD/EUR	0.981	1.019	3.9%	0.984	1.000	1.7%
JPY/EUR	118.4	124.2	4.9%	117.3	122.5	4.4%
GBP/EUR	0.6306	0.6425	1.9%	0.6352	0.6365	0.2%
CHF/EUR	1.465	1.467	0.1%	1.464	1.466	0.2%

Chart 5

**Nominal effective exchange rates of the euro**

Index 1.1.1999 = 100

(daily data)

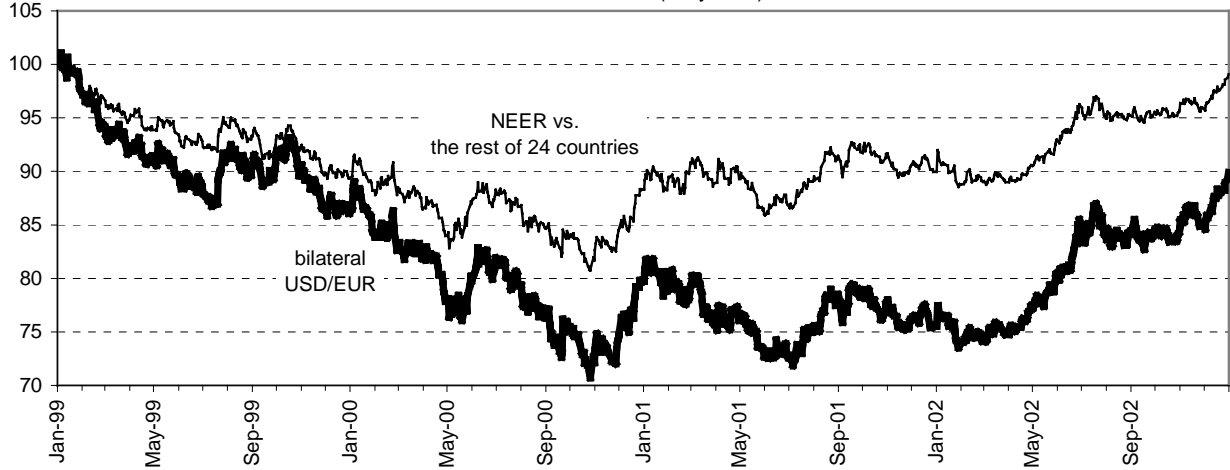
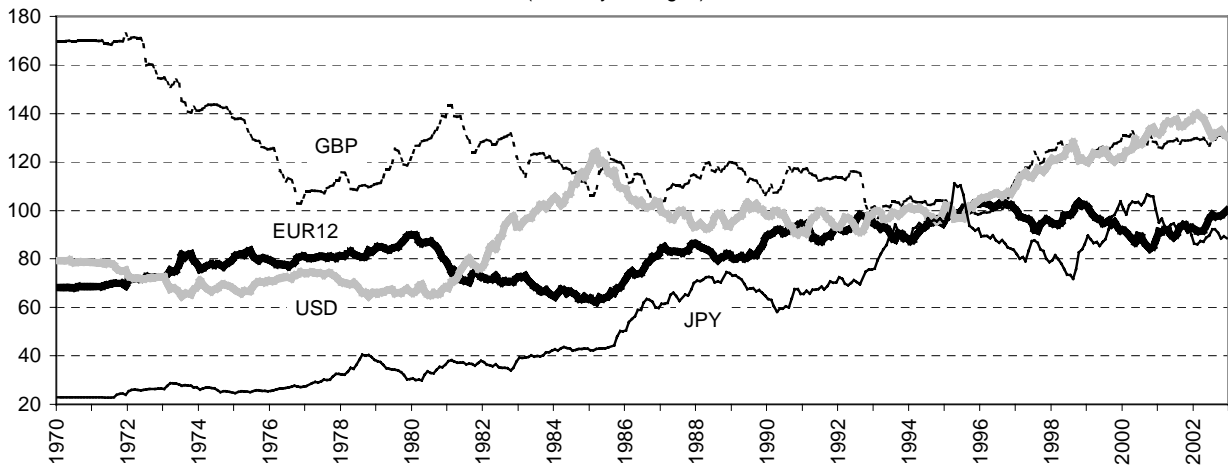


Chart 6

**Nominal effective exchange rates since 1970**

1995=100

(monthly averages)



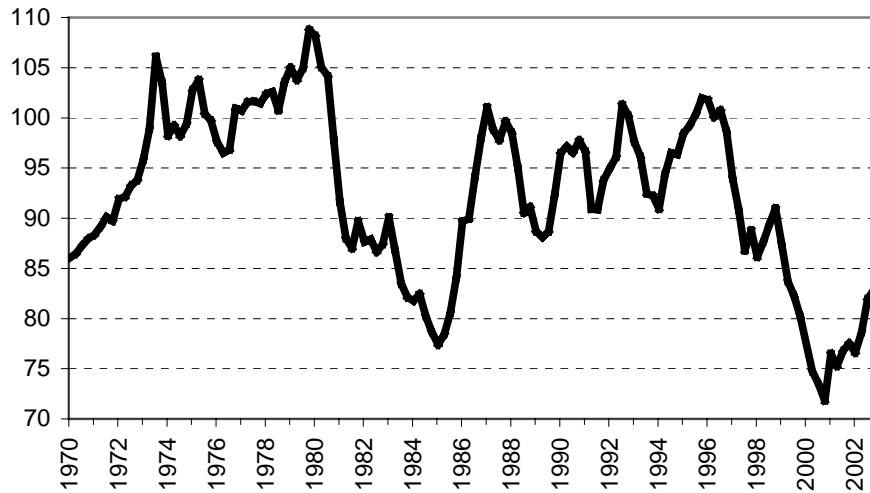
2. NOMINAL EFFECTIVE EXCHANGE RATES VS THE REST OF THE IC GROUP

**TABLE 2: NOMINAL EFFECTIVE EXCHANGE RATES**

(vs. the rest of IC, index 1995 = 100)

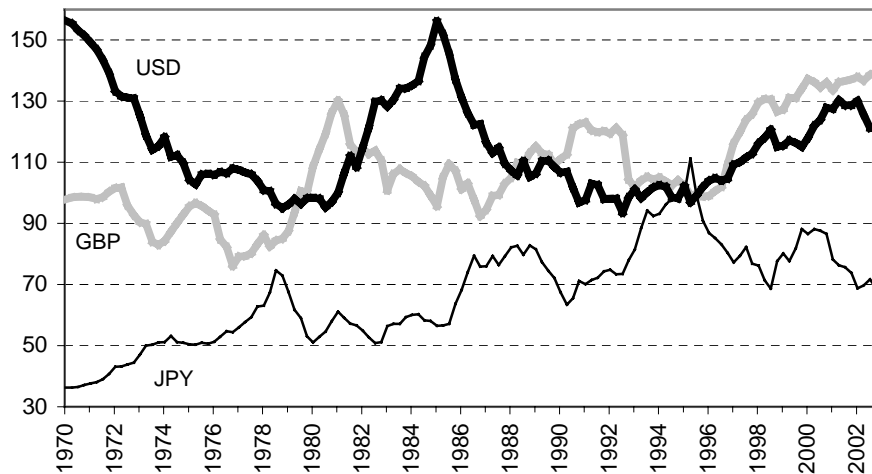
	During the fourth quarter of 2002 (monthly averages)			Relative to the previous quarter (quarterly averages)		
	Average Sep-02	Average Dec-02	% change	Average Q3-02	Average Q4-02	% change
EUR12	97.7	100.0	2.4%	97.8	98.9	1.1%
USD	132.3	130.4	-1.4%	131.4	131.6	0.2%
JPY	90.8	88.4	-2.6%	91.8	88.7	-3.4%
GBP	130.6	129.8	-0.6%	129.7	130.3	0.5%

Chart 7 **Real effective exchange rate<sup>1</sup> : eurozone since 1970**  
1995=100 (quarterly data)



<sup>1</sup> vs. rest of IC, deflated by unit labour costs in total economy

Chart 8 **Real effective exchange rates<sup>1</sup> since 1970**  
1995=100 (quarterly data)



<sup>1</sup> vs. rest of IC, deflated by unit labour costs in total economy

### 3. REAL EFFECTIVE EXCHANGE RATES VERSUS THE REST OF THE IC GROUP, BASED ON ULCE

**TABLE 3: REAL EXCHANGE RATES (ULCE)**

(vs. the rest of IC, index 1995 = 100)

	Relative to the previous quarter (quarterly data)			Rel. to the previous year (quarterly data)		Rel. to long-term average (quarterly data)	
	Q3-02	Q4-02	% change	Q4-01	% change	Average 87-01	% change
EUR12	81.9	<b>82.9</b>	1.1%	77.5	6.9%	91.5	-9.5%
USD	121.2	<b>121.1</b>	-0.1%	128.7	-5.9%	108.7	11.3%
JPY	71.7	<b>68.8</b>	-4.2%	73.8	-6.8%	81.1	-15.2%
GBP	138.6	<b>139.5</b>	0.7%	137.1	1.8%	115.9	20.4%

#### 4. COST COMPETITIVENESS OF THE USA AND JAPAN RELATIVE TO THE EURO AREA

Chart 9

#### Real exchange rates<sup>1</sup> : USD and JPY vs. EUR12

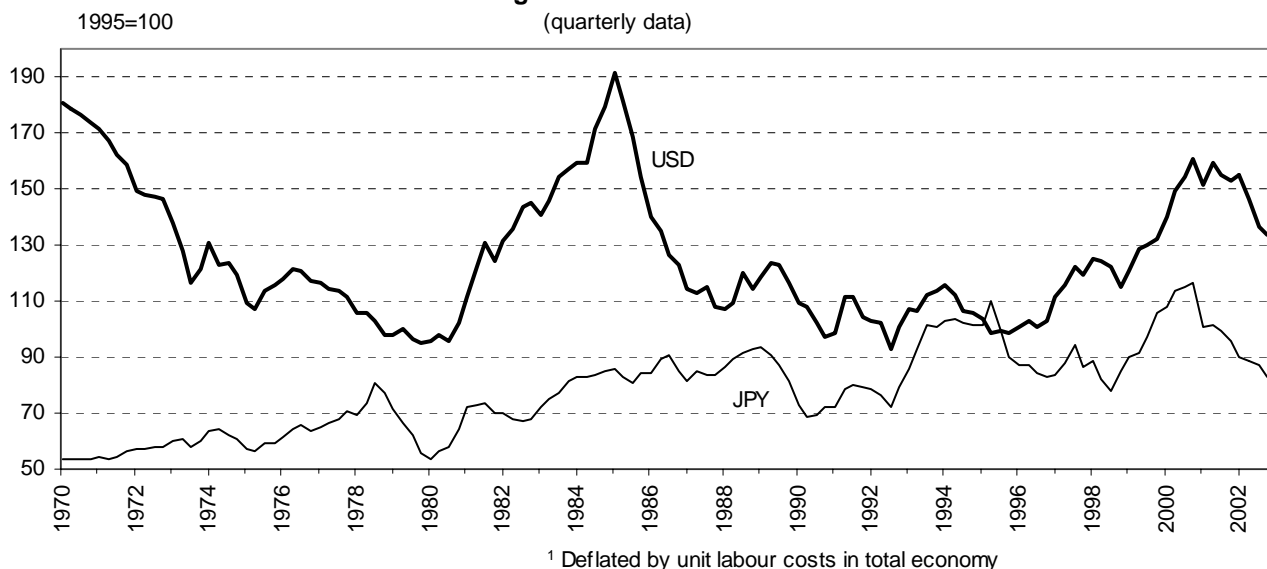


TABLE 4 A : RELATIVE COST AND PRICE INDICATORS OF INDIVIDUAL COUNTRIES RELATIVE TO EUR12

% Change	Over the last year (Q4-02 / Q4-01)			Over the last two years (Q4-02 / Q4-00)			Relative to 1987-2001 average (Q4-02 / Average 87-01)		
	ULCE	ULCM	PGDP	ULCE	ULCM	PGDP	ULCE	ULCM	PGDP
USA	-12.9	-11.5	-11.5	-17.2	-17.6	-14.5	14.3	4.4	12.8
Japan	-13.6	-14.8	-12.1	-28.9	-25.3	-26.9	-8.1	-3.9	-8.5

TABLE 4B: EVOLUTION OF REAL EFFECTIVE EXCHANGE RATES (ULCE)  
(vs. EUR12; index 1995 = 100)

	Relative to the previous quarter (quarterly data)			Rel. to the previous year (quarterly data)		Rel. to long-term average (quarterly data)	
	Q3-02	<b>Q4-02</b>	% change	Q4-01	% change	Average 87-01	% change
USD	136.1	<b>133.3</b>	-2.1%	153.1	-12.9%	116.6	14.3%
JPY	88.8	<b>87.2</b>	-1.8%	99.0	-11.9%	90.0	-3.1%

## II. DEVELOPMENTS WITHIN THE EUROPEAN UNION

Within the euro area, diverging movements in costs and prices may change the relative cost competitiveness positions of euro area Member States. Table 5 and Chart 10 show three measures of the real effective exchange rate of individual Member States against EUR12. The different measures do not always give a uniform picture of the movement over time in the real effective exchange rate of a given country against its partners and, as such, the indicators of cost and price competitiveness need to be interpreted carefully.

In some cases, deviating price and cost trends among euro area Member States could lead to a build-up of competitive imbalances which might ultimately hamper economic growth and cause unemployment in individual Member States. In other cases, however, longer-term changes in relative prices and costs may be justified by changes in economic fundamentals related e.g. to a catching-up in the level of economic development, changes in non-price competitiveness factors, or changes in underlying savings and investment patterns. Moreover, differences in cyclical positions may cause movements in relative costs and prices in the short term. An in-depth assessment of movements in real exchange rates therefore requires a comprehensive analysis of the economic situation in each country seen in a longer term perspective. This report merely provides a descriptive overview of movements in intra-euro area cost and price competitiveness indicators.

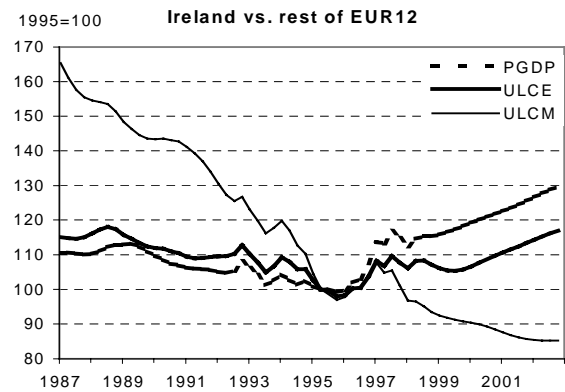
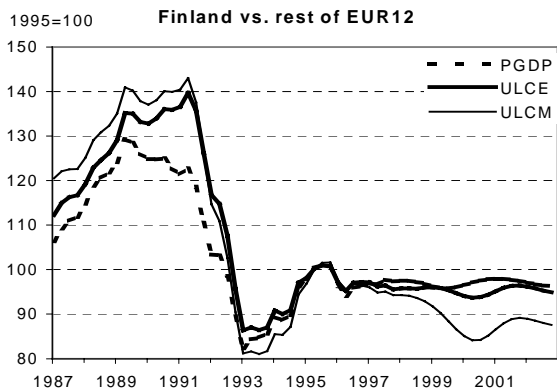
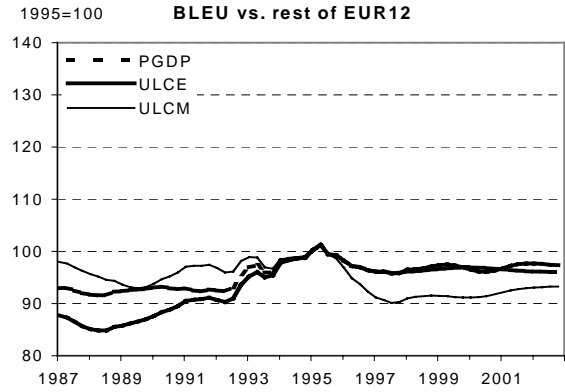
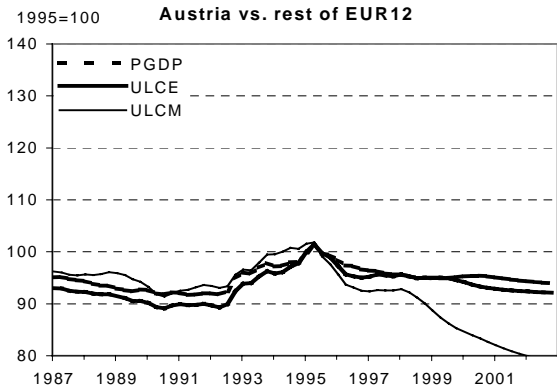
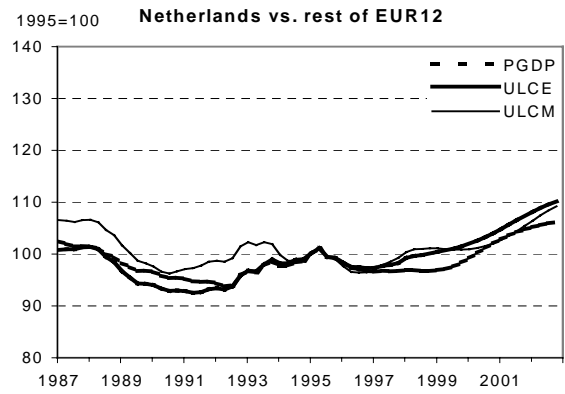
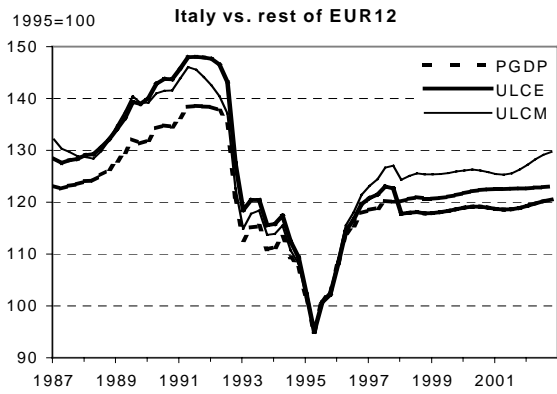
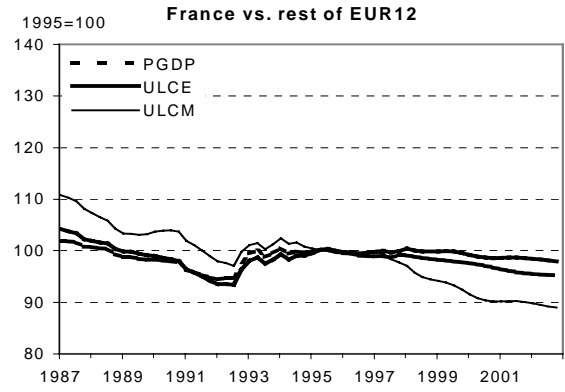
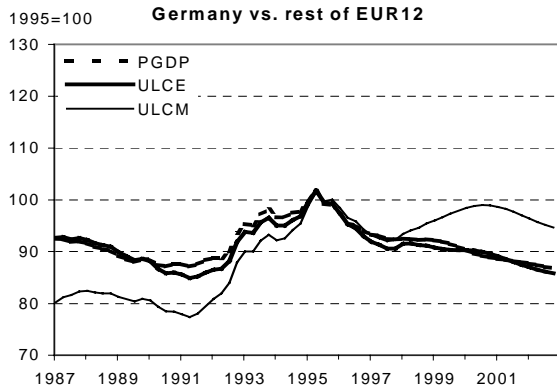
TABLE 5: RELATIVE COST AND PRICE INDICATORS OF INDIVIDUAL COUNTRIES RELATIVE TO THE EURO AREA (EUR12)

	Over the last year (Q4-02 / Q4-01)			Over the last two years (Q4-02 / Q4-00)			Relative to 1987-2001 average (Q4-02 / Average 87-01)		
<b>Euro area Member States</b>									
% Change	ULCE	ULCM	PGDP	ULCE	ULCM	PGDP	ULCE	ULCM	PGDP
BLEU	-0.3	0.4	-0.2	1.0	1.7	-0.6	4.0	-1.6	0.7
Germany	-1.9	-2.4	-1.3	-4.2	-4.3	-2.3	-6.0	5.4	-5.7
Greece	1.7	-0.4	1.3	-0.2	-1.4	1.8	8.6	8.3	11.8
Spain	1.2	3.1	1.5	1.7	5.7	3.1	3.8	15.4	4.0
France	-0.7	-1.1	-0.4	-0.7	-1.3	-1.6	-1.2	-10.5	-3.3
Ireland	3.1	-0.6	3.3	6.6	-3.7	6.5	7.4	-27.8	17.6
Italy	1.3	2.7	0.4	1.3	3.1	0.5	-3.3	2.9	1.1
Netherlands	2.6	3.6	1.4	5.9	7.0	4.1	11.8	8.6	8.1
Austria	-0.4	-2.0	-0.6	-1.0	-4.7	-1.4	-1.6	-15.2	-1.2
Portugal	1.8	1.9	2.2	4.2	1.0	4.9	26.7	5.9	18.8
Finland	-1.6	-1.8	-1.2	0.5	2.9	-1.6	-11.2	-17.2	-7.0
<b>Non-euro area Member States</b>									
% Change	ULCE	ULCM	PGDP	ULCE	ULCM	PGDP	ULCE	ULCM	PGDP
Denmark	-0.3	-0.7	-0.3	0.5	-1.6	-0.4	6.1	2.0	5.3
Sweden	4.2	3.4	4.5	-5.3	-5.7	-5.2	-1.7	-12.8	-8.2
UK	-2.5	-0.4	-1.6	-5.2	-2.8	-5.2	22.4	28.0	17.9

Note: relative ULCE and ULCM for Italy relative to any period before 1998 are distorted by the 1998 tax reform which shifted taxation from labour costs to value added but did not significantly change competitiveness.

A minus means an improvement in cost competitiveness.

**Chart 10 : Price and cost indicators for individual countries relative to EUR12**





**Chart 10 contd.: Price and cost indicators for individual countries relative to EUR12**

