Euro area competitiveness developments

"La competitivité belge. Analyses et enjeux"

Bureau fédéral du Plan

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Overview

- ✓ euro area external performance in the global economy

- ✓ evolution of intra-euro area competitiveness

- ✓ main factors driving intra-euro area imbalances and external competitiveness

- ✓ the role of the non-tradable sector

- ✓ the role of non-price competitiveness

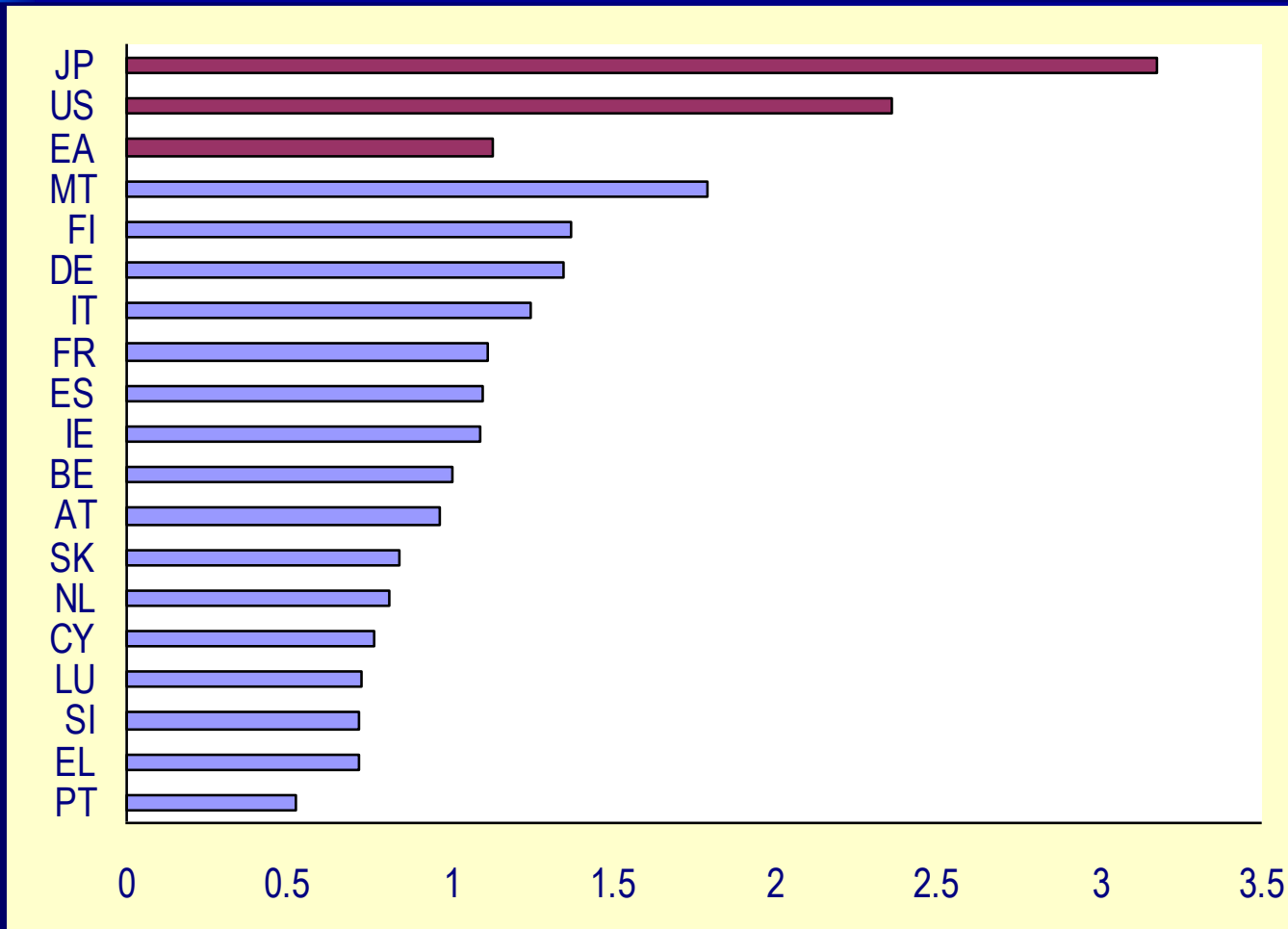- ✓ some preliminary findings on Belgium

- ✓ conclusions
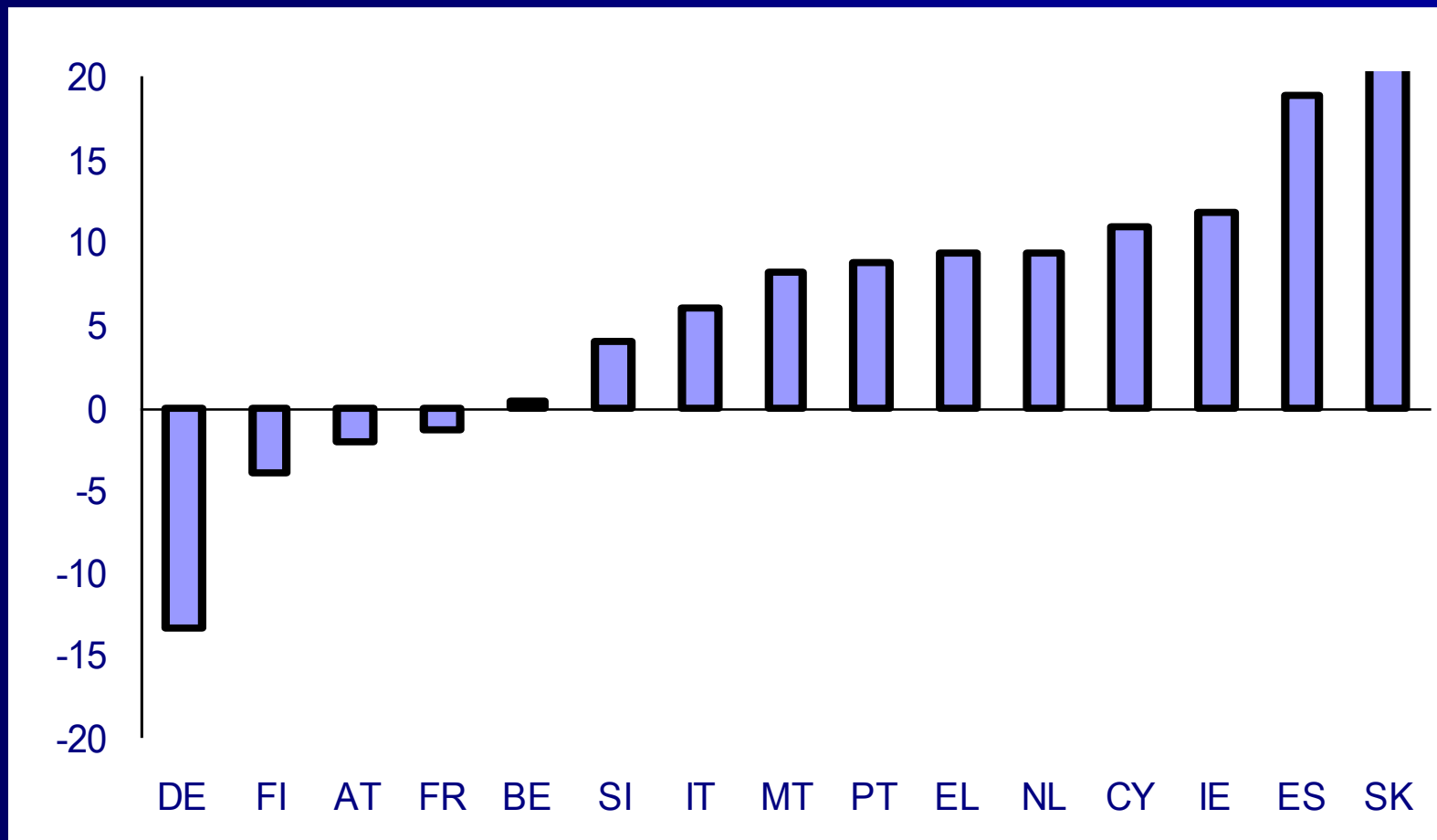
global export market shares
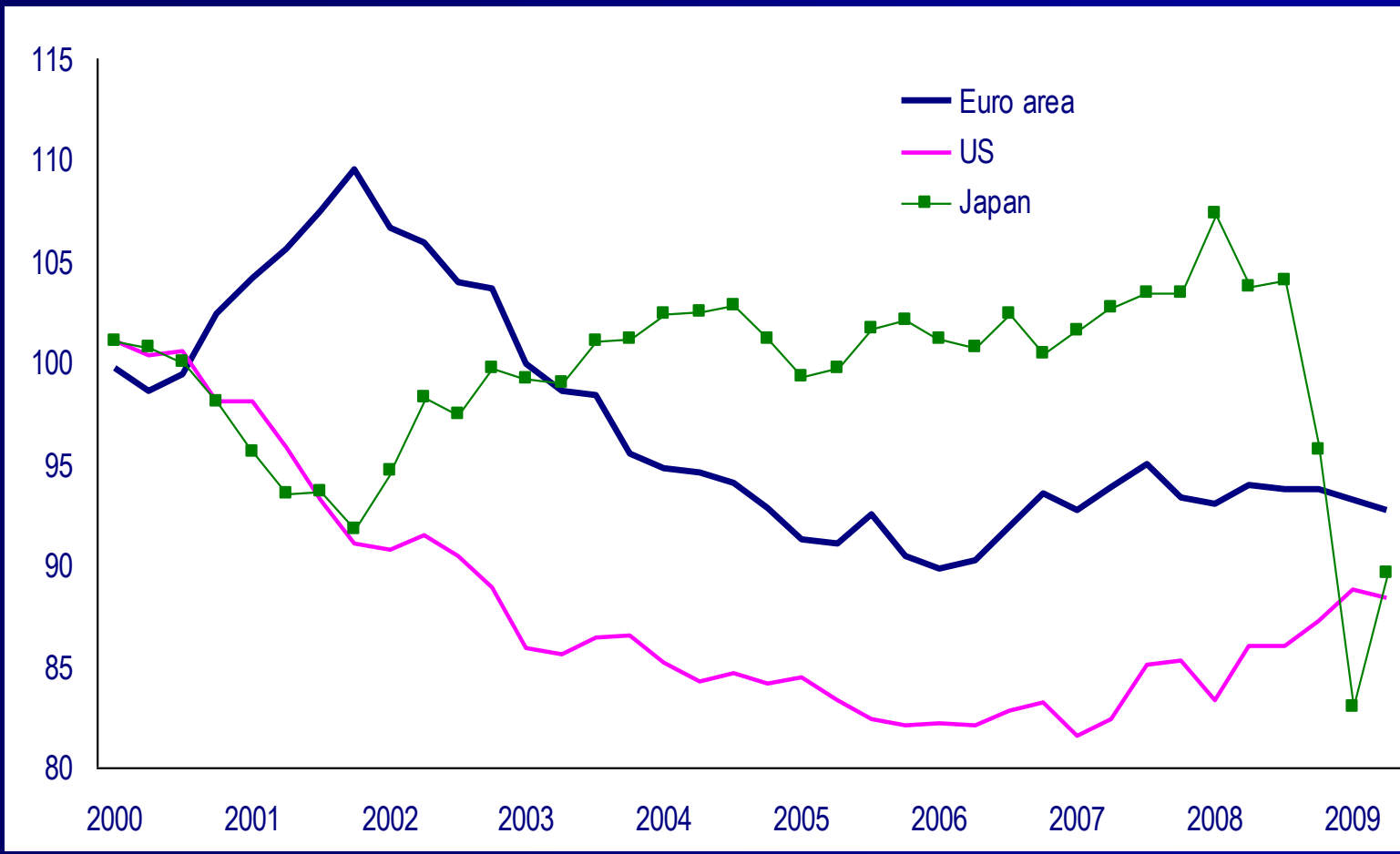
Source: Commission services. Euro area date excludes intra-euro-area trade

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Export market growth − 2010 forecast

Note: percentage change on preceding year, export weighted GDP growth of trade partners; own calculations based on IMF October 2009 forecast.

Intra euro area REER divergence
(1998-2008 - in %, based on GDP deflator)

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Appreciation in SK during 1998-2008 amounted to 66%.

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Exports of goods and services
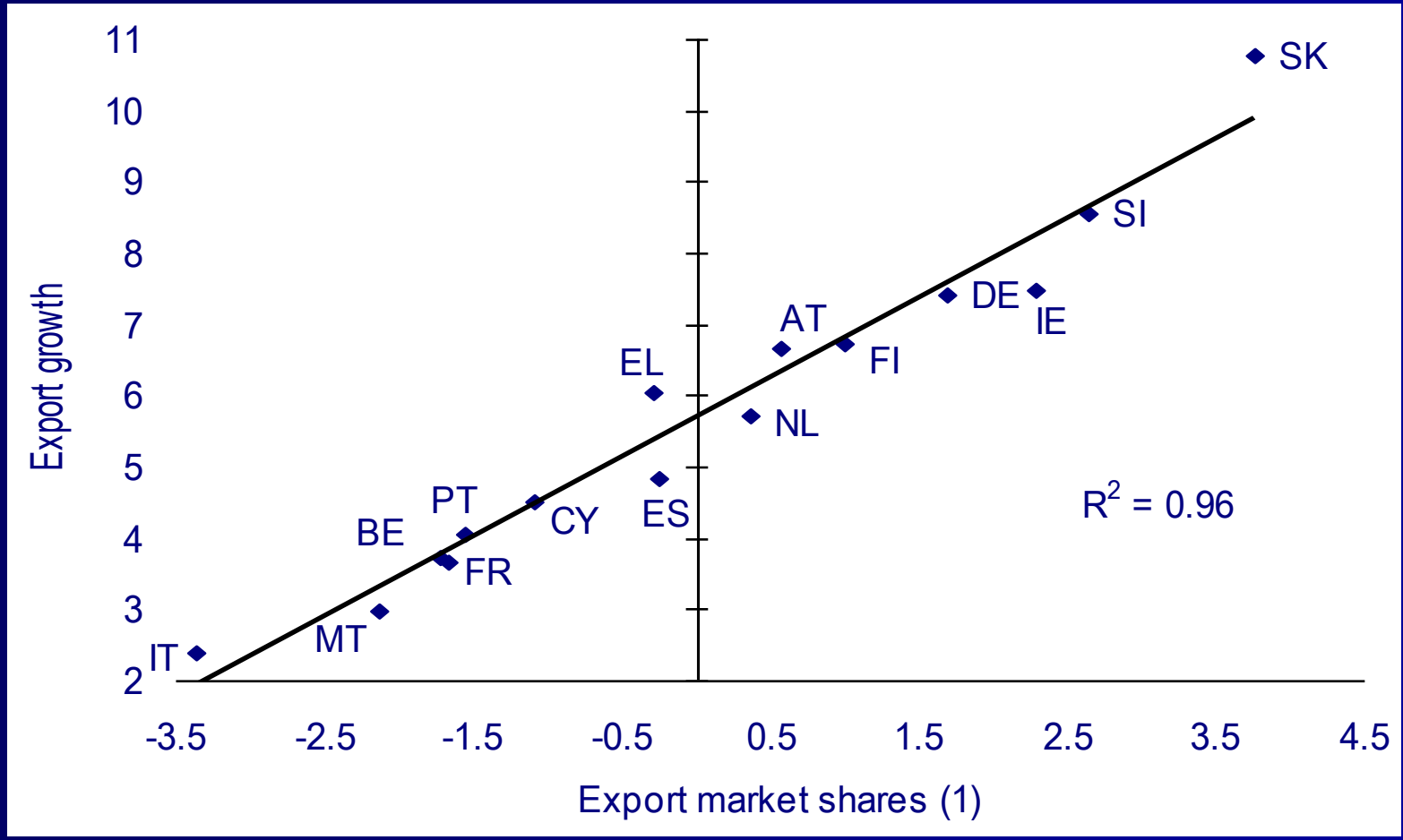## (average annual growth in % - 1999-2008)
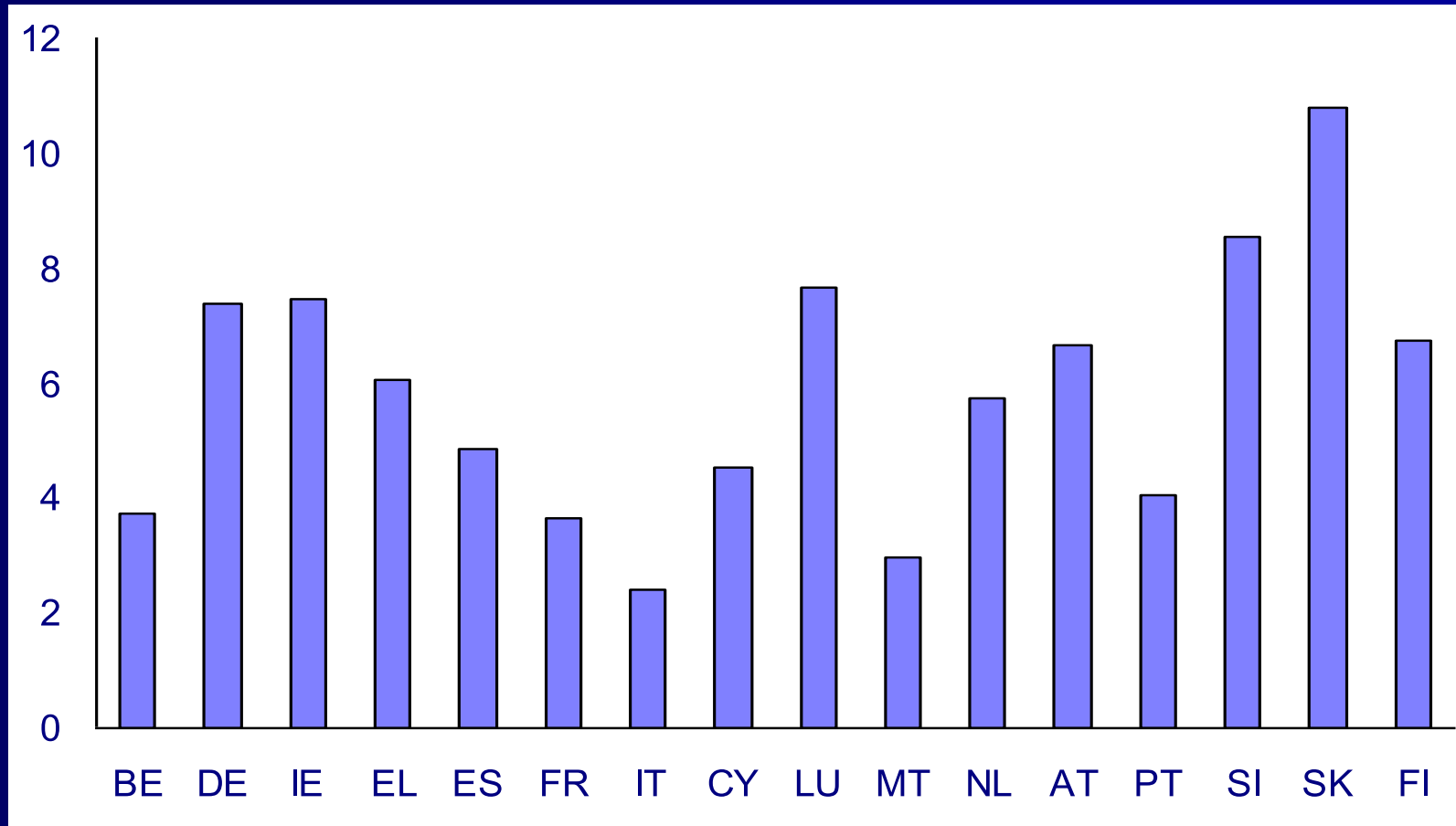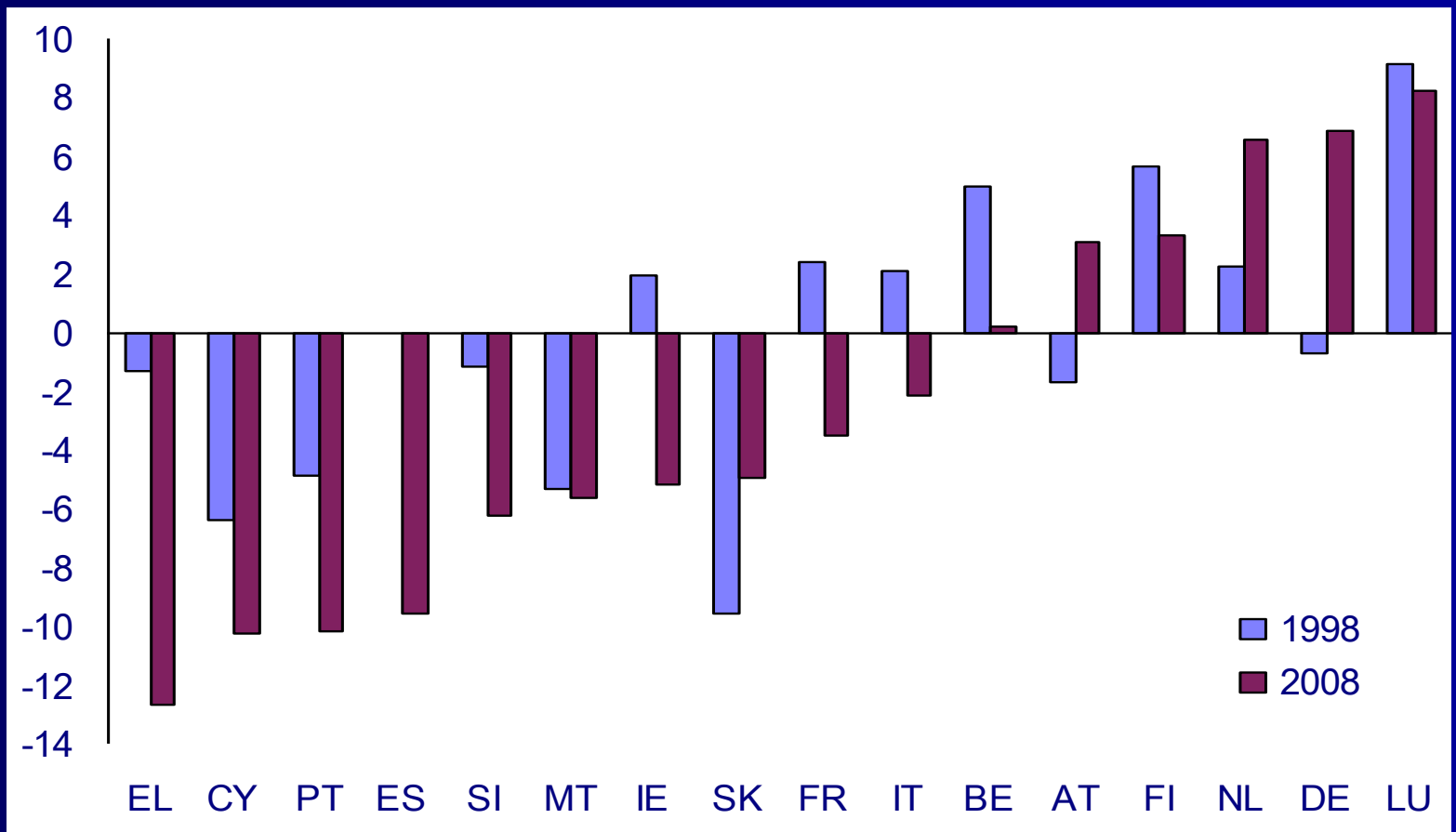
Change in export market shares and export growth

(average annual growth in % - 1999-2008)

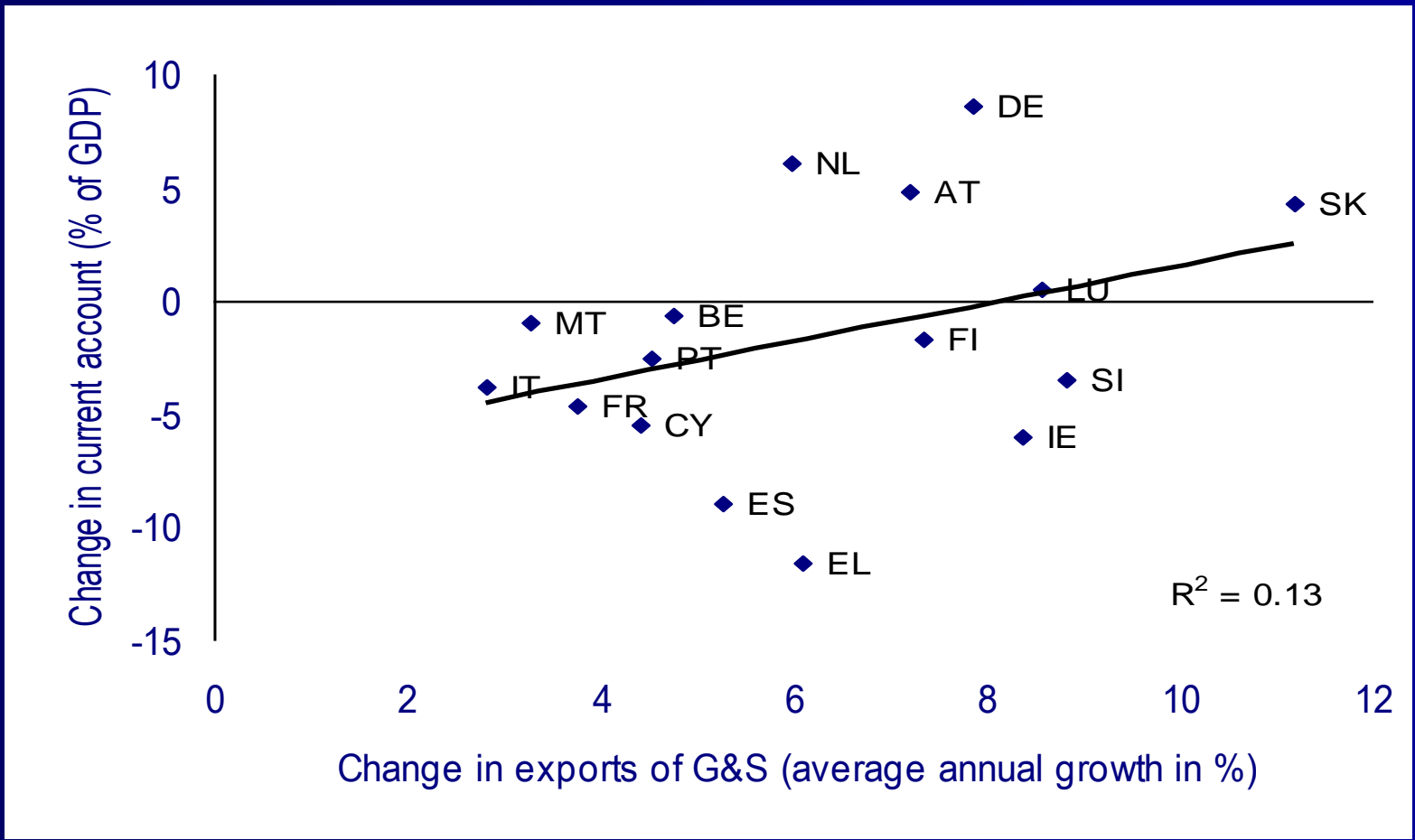# Current account positions
(in % of GDP - 1999-2008)

NLB from national accounts for all Member States, except LU (bal. of current transactions).

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export performance and the current account (1999-2007)

Domestic demand and the current account (1999-2007)
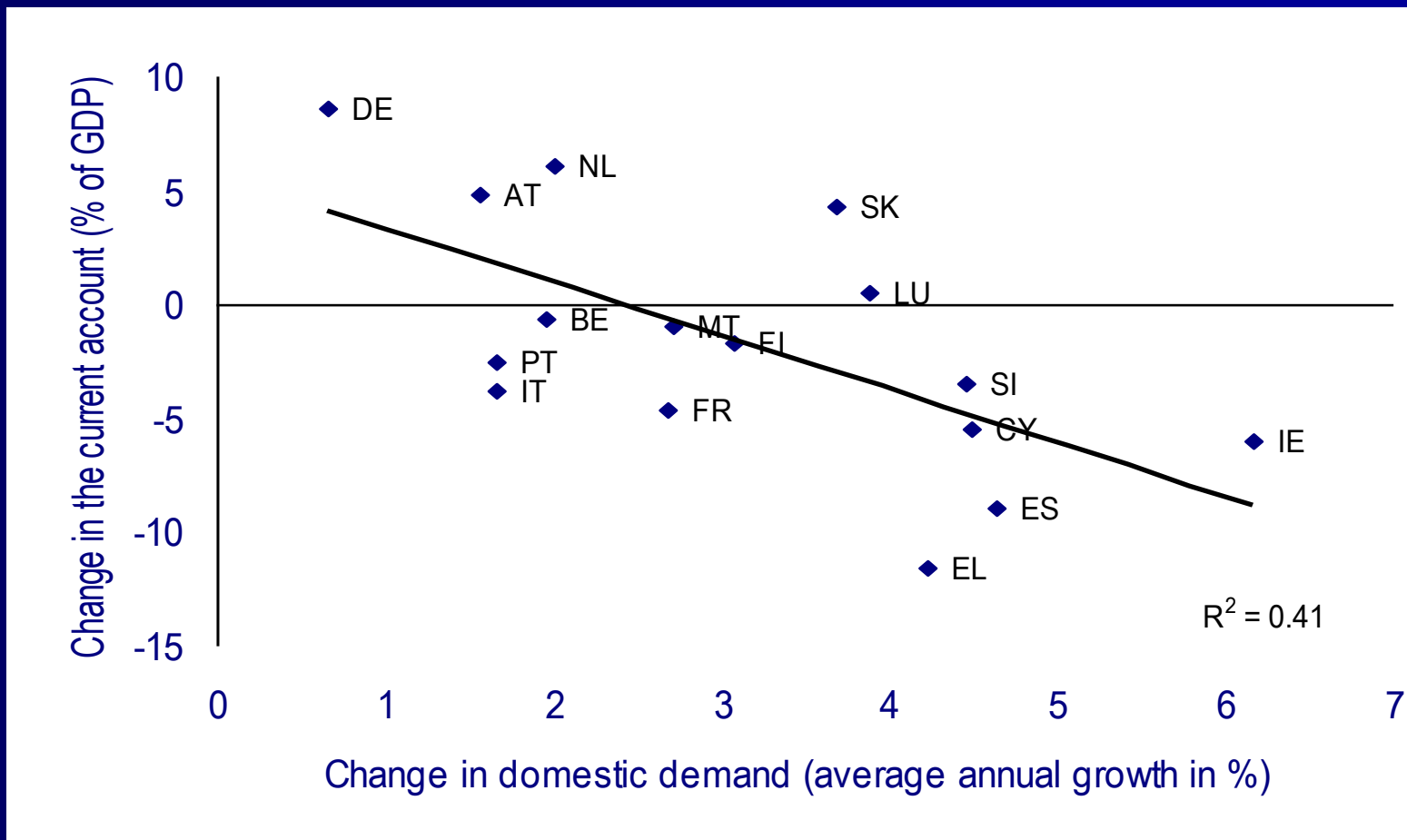
Exports of goods and services
(average annual growth in % - 1999-2008)
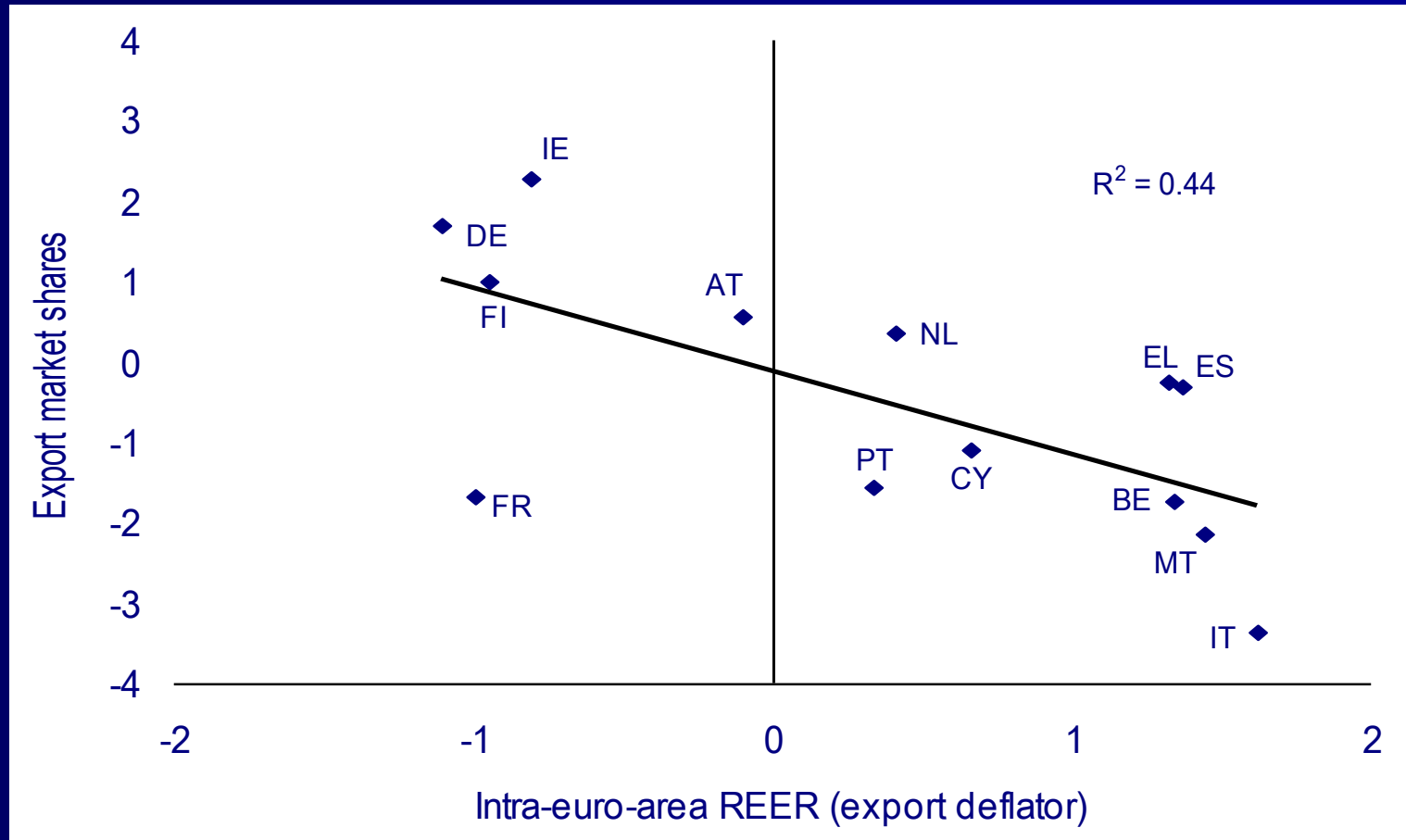
Correlations between various measures of the REER and export growth or current account
(cross-sectional correlations in %)

REER based on:	Export growth	Changes in the current account
REER based on:	1998-2008	1998-2008
GDP deflators	-30.4	-59.7
Export prices	-63.3	-33.3

A preliminary look at non-price competitiveness

✓ Non-price competitiveness includes a broad range of aspects. Preliminary ECFIN work focuses on:

- **Technological aspects**. Innovation is crucial in the development of new varieties of products as well as in producing products of higher quality (proxy: R&D intensity, patents, exports deflator)

- **Services**. Services are an important intermediate input and are increasingly being used to obtain product differentiation (proxy: TFP in selected services sectors)

- **Business environment**. Framework conditions related to the business environment (proxy: procedures, time and cost of enforcing contracts).

External competitiveness of Belgium – some tentative views

Reasons for deterioration of current account in recent years:

✓ Sustained domestic (import) demand;

✓ rising oil prices;

✓ sluggish export performance

Factors shaping export performance:

✓ geographical distribution of exports

✓ Product composition of exports (share of high-tech lower than EA average)

✓ Adverse cost developments

✓ Weaknesses in business environment

✓ SME structure less conducive to export

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Conclusions

1. Euro-area's external trade performance strongly determined by geographical distribution of exports

2. Significant divergence in REER, trade performance and current accounts across EA Member States (1999-2007)

3. In many cases, divergence was driven by domestic imbalances:

   House market bubble; overshooting of private sector debt; little productive use of capital inflows; insufficient fiscal consolidation in some MS

4. External performance is not just an exporter's story – the productivity and relative prices of the non-tradable sectors matters, too

5. Non-price factors are an important determinant of external trade performance

6. Overall, formidable adjustment challenges for Euro Area in less benign post-crisis global economic environment

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Thank you very much for your attention

For information on the economy of the Euro Area:

✓ Quarterly Report on the euro area, No 1, 2009

http://ec.europa.eu/economy_finance/publications/publication_summary14648_en.htm

✓ 2009 Annual Statement and Annual Report on the Euro Area:

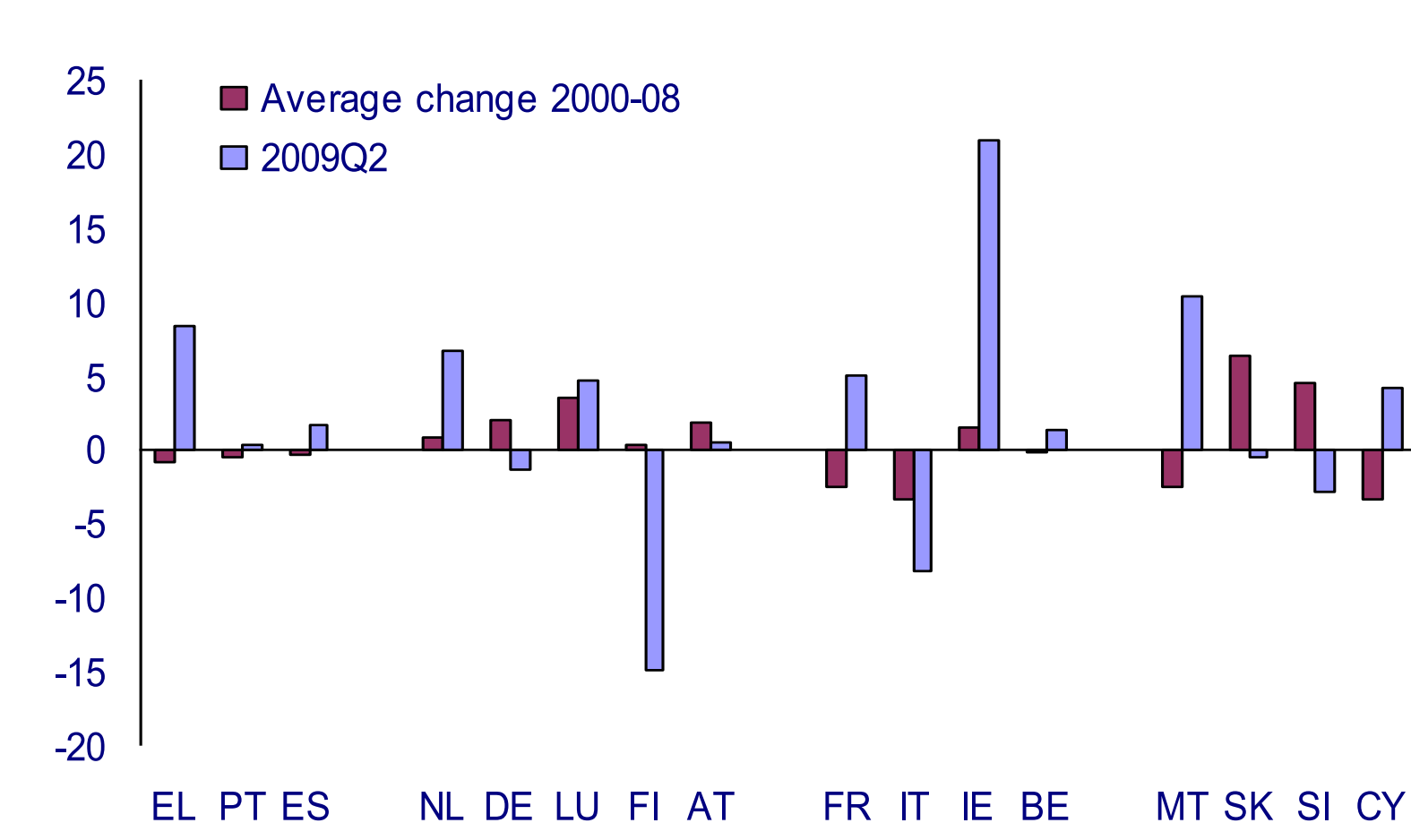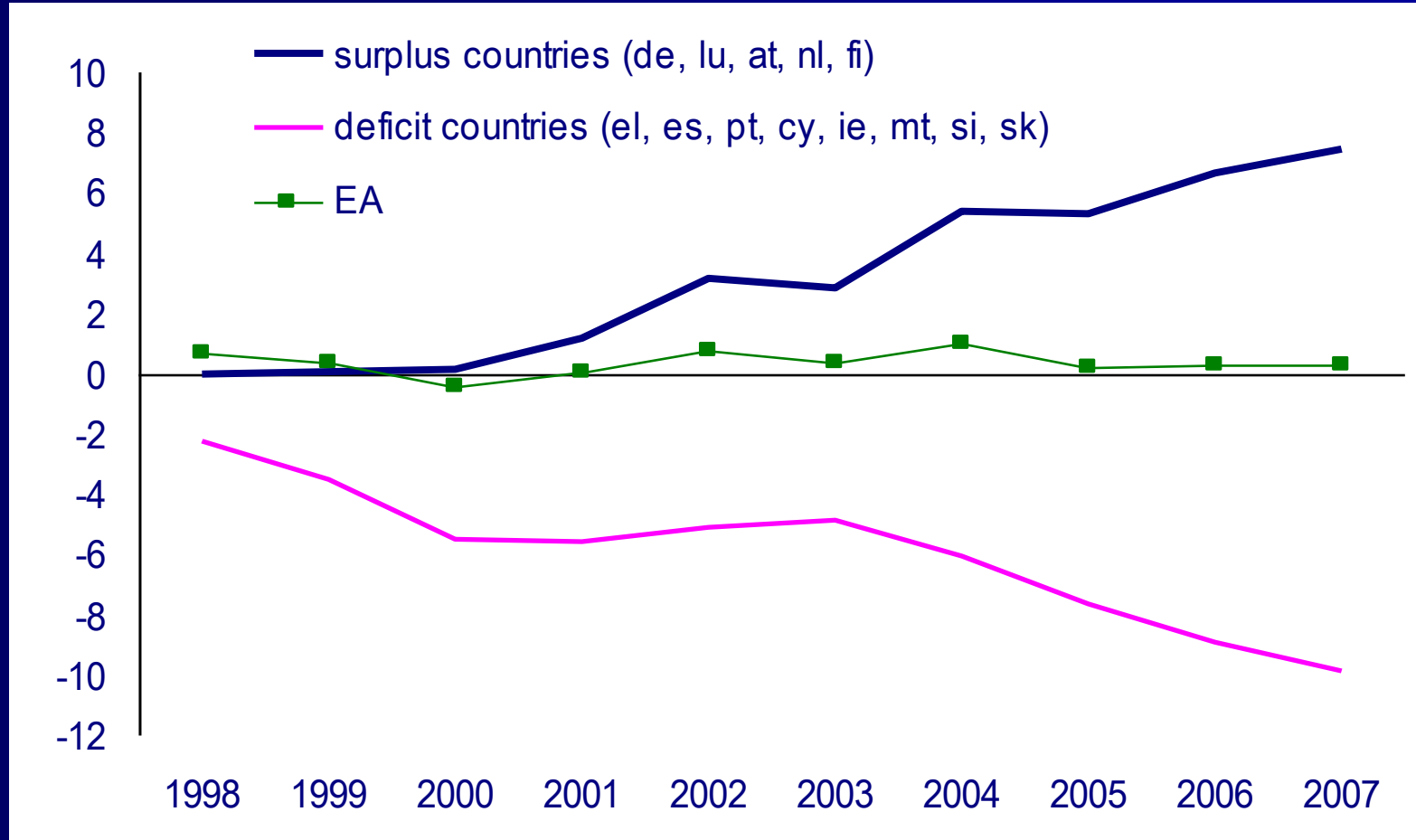http://ec.europa.eu/economy_finance/thematic_articles/article15859_en.htm

✓ Slides not shown…

Export market shares (2)

1.   Divergence
Current account divergence in % of GDP

- surplus countries (de, lu, at, nl, fi)
- deficit countries (el, es, pt, cy, ie, mt, si, sk)
- EA

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Determinants of real exports in euro-area countries – estimation results

	Long-run elasticities		Adjustment coefficient (α)	R^2
	fdem	*reer*		
Austria	1.03	-0.82	-0.15	0.53
Germany	1.02	-0.71	-0.26	0.69
Spain	1.35	-1.23	-0.12	0.41
France	0.86	-1.18	-0.31	0.38
Italy	1.07	-1.68	-0.20	0.48
The Netherlands	1.00	-0.25	-	0.69

Notes:
Sample is 1980Q1-2007Q4 except Italy: 1980Q1-2007Q4 and France: 1980Q1-2000Q1
For Netherlands the estimates presented are OLS coefficients estimated on detrended series
All coefficients are significant at 5%.

A case for policy intervention?

1. Divergence is not bad per se

   ✓ Catching-up growth

   ✓ Consumption smoothing

2. Source of imbalances need to be identified

   ✓ Market failure (e.g. bubbles) ?

   ✓ Policy failure ?

2. Underlying imbalances
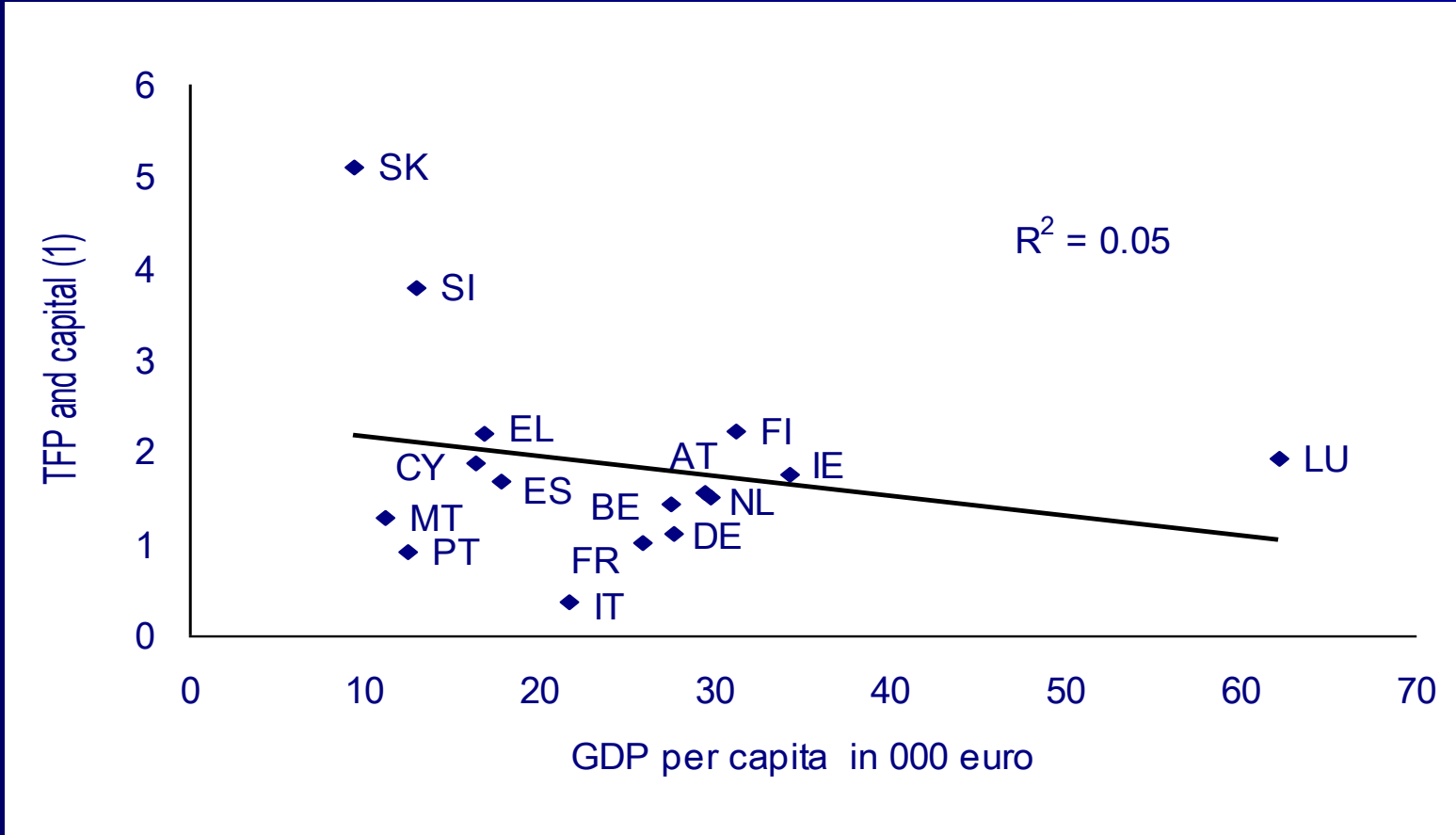## House price and current account
(changes in % - 1999-2007)

$R^2 = 0.51$

Changes in current account (in % of GDP)

Houseprice increase (in percent)
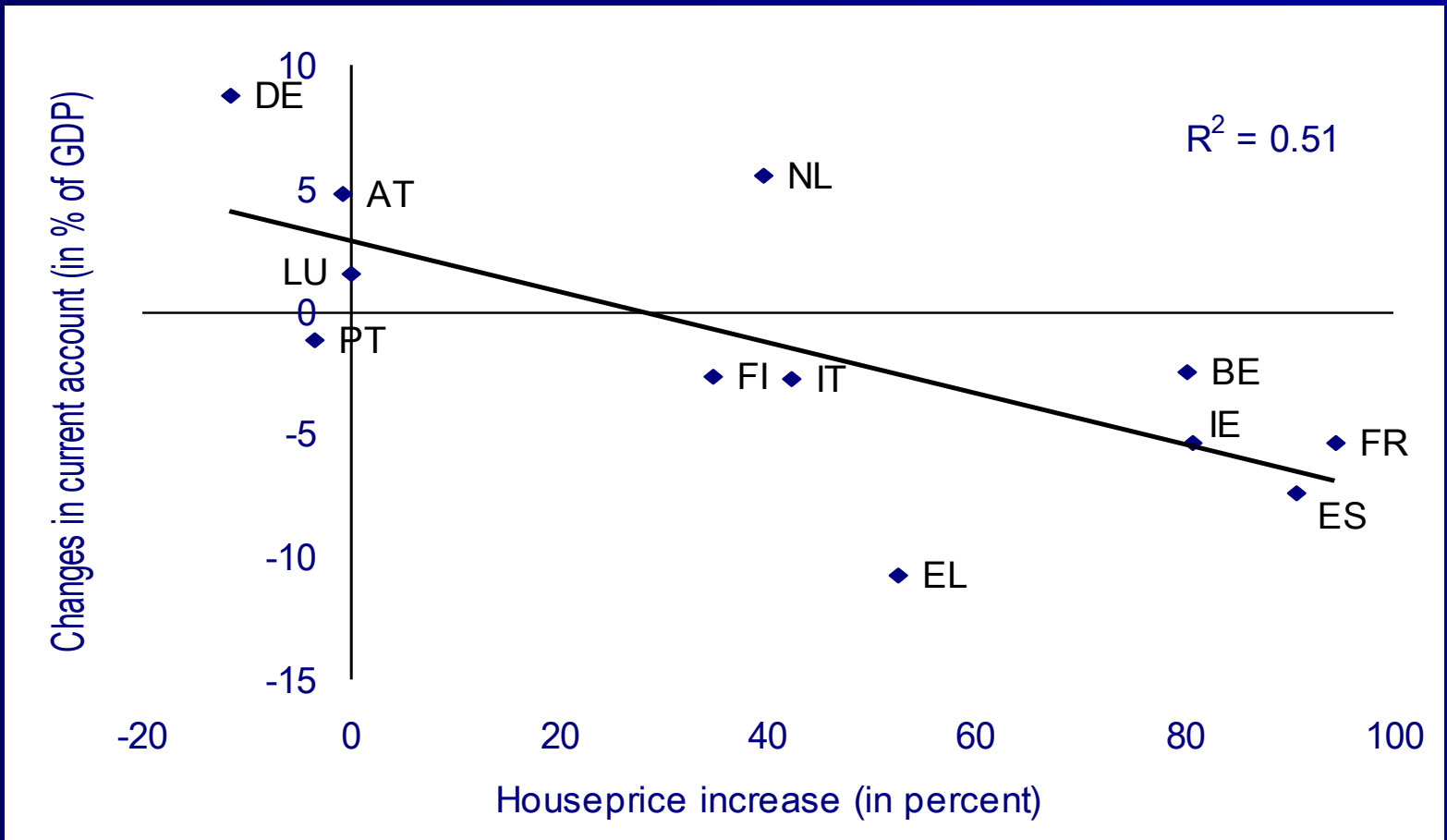
2. Underlying imbalances
Capital flow often not used for catching-up
(average 1998-2008)

(1) Sum of contribution of capital and trend TFP to potential growth.