Box 4

Recent developments in extra-euro area trade volumes and prices

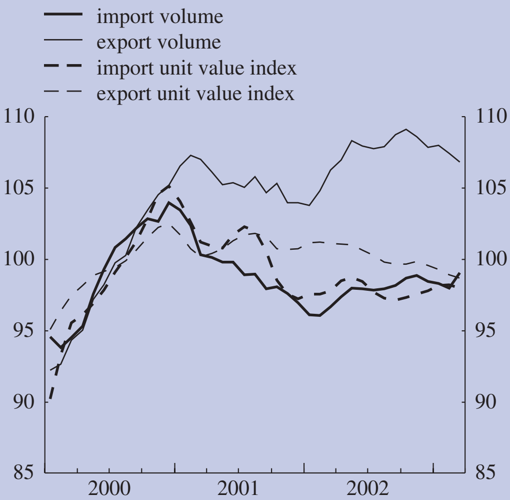
In view of the strong appreciation of the euro since the second quarter of 2002, this box takes a closer look at recent developments in the volumes and prices of extra-euro area exports and imports of *goods,* with a particular focus on the period between the beginning of 2002 and the first quarter of 2003. Trade data that have been disaggregated by both commodity category and trading partner are used to shed light on the likely factors accounting for recent movements in aggregate trade volumes and trade prices (unit value indices are used as a proxy for the latter). Overall, the appreciation of the euro has been associated with declines in both export volumes and export prices, while weak foreign demand has also affected export volumes. Thus these factors explain the recent fall in export values which, in turn, largely account for the decreases in both the goods and current account surpluses. At the same time, weak euro area demand seems to have partly offset the potential upward impact of the appreciation on import volumes, while the expected downward pressure of the strengthening of the euro on import prices seems, thus far, to have been largely counterbalanced by rising oil prices.

Chart A shows recent developments in extra-euro area trade volumes and unit value indices of goods up to the first quarter of 2003. *Export volumes,* after growing strongly in the first few months of 2002, started to flatten out before declining in both the fourth quarter of 2002 and the first quarter of 2003. This slowdown and subsequent decline in exports reflects both a weakening of foreign demand and a decline in price competitiveness arising from the appreciation of the euro, which began in the second quarter of 2002. However, compared with the decline in export volumes in 2001, which was largely due to falling foreign demand, the current fall in exports has, so far, been fairly moderate. Chart B shows that the recent downturn in export volumes was spread fairly broadly across all major export markets of the euro area. However, until the latter part of last year, exports to Asia and to the central and eastern European countries had been growing rapidly, while growth in exports to the United States was somewhat weaker and exports to the United Kingdom registered a significant decline. Taking into account the growth of total import volumes in these markets, the weakness of euro area exports to the United Kingdom and the United States in 2002 and early 2003 implies some decline in the euro area's export market share in these two countries over this period. Meanwhile, it seems that there has only been a slight loss in the euro area's export market share in Asia, with virtually no loss in its market share for exports to central and eastern European countries.

Turning to a breakdown of exports into different product categories, export volumes of capital, consumer and intermediate goods have all shown declines in recent months (see Chart C). However, exports of consumer goods have proved to be more resilient than the other two categories since the second quarter of 2002. Moreover, it should be borne in mind that, despite recent declines, export volumes remain at comparatively high levels, reflecting the significant earlier rise in the euro area's export market share associated with the previous gains in international price competitiveness resulting from the depreciation of the euro in 1999 and 2000. Furthermore, as emphasised in the article entitled "Developments in the euro area's international cost and price competitiveness" that appears in this issue of the

Chart A: Extra-euro area trade volumes and unit value indices [1]

(index: 2000 = 100; seasonally adjusted; three-month moving average)



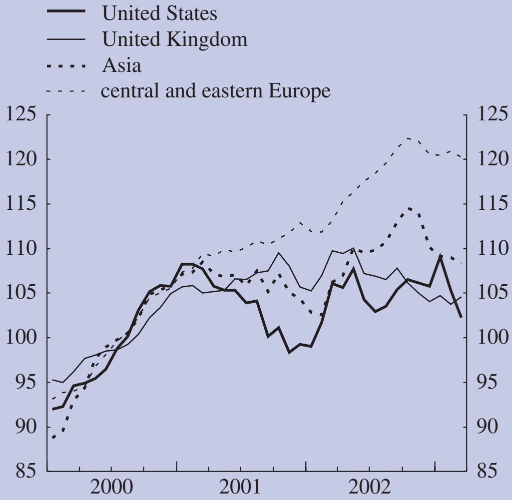
Sources: Eurostat and ECB calculations.

1) Latest observations are for March 2003.

Monthly Bulletin, the international cost and price competitiveness of the euro area is currently at levels similar to those seen at the time of the launch of the euro, and is broadly in line with historical averages.

Chart B: Extra-euro area export volumes to selected trading partners [1]

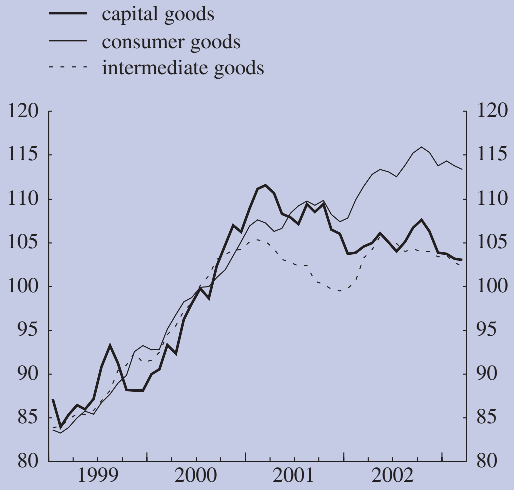
(index: 2000 = 100; seasonally adjusted; three-month moving averages)



Sources: Eurostat and ECB calculations.
1) Latest observations are for March 2003.

Chart C: Extra-euro area export volumes for selected commodities [1]

(index: 2000 = 100; seasonally adjusted; three-month moving averages)



Sources: Eurostat and ECB calculations.
1) Latest observations are for March 2003.

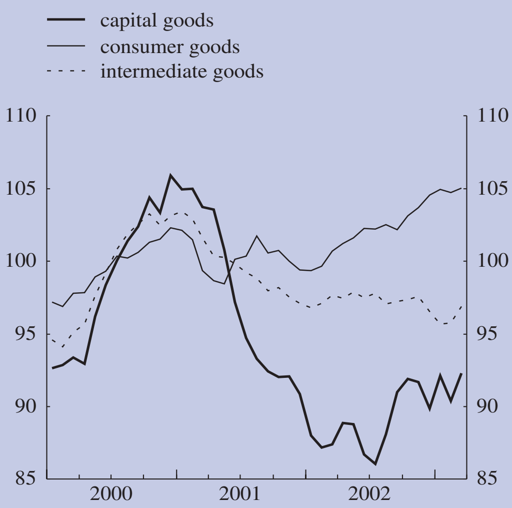
Despite rising costs – as measured by unit labour costs or producer prices – *export prices* have fallen by around 2.5% since the euro began to appreciate in the second quarter of 2002 (see Chart A). This suggests that euro area exporters are cutting profit margins in an effort to partially offset the effects of the loss in price competitiveness resulting from the appreciation of the exchange rate. The mechanisms behind this adjustment are essentially a mirror image of those at play during the earlier depreciation of the euro when euro area exporters increased their prices in excess of rising costs, thereby increasing their profit margins. However, it must be considered that changes in unit value indices, which are used as a proxy for euro area external trade prices (as the latter are unavailable), reflect not only changes in prices but also changes in the composition and product characteristics of trade at both the detailed and aggregate level.

Meanwhile, after falling throughout 2001, *import volumes* began to grow as from the beginning of 2002, but at a fairly sluggish pace, particularly when considering that the appreciation of the euro should have provided a boost to import volumes by improving their price competitiveness vis-à-vis domestic euro area producers (see Chart A). It thus seems that weak euro area demand, especially for the import-intensive categories of expenditure – such as capital expenditure and exports – may have partly offset the upward impact on import volumes that should have resulted, ceteris paribus, from the appreciation of the euro. Chart D shows that import volumes of capital goods fell sharply in 2001 and grew only sluggishly in the second half of 2002 and early 2003, in conjunction with weak euro area capital expenditure. By contrast, imports of consumer goods seem to have shown a more sustained increase in 2002 and the first quarter of 2003, which may be linked to the import-boosting effects of the appreciation of the euro. Meanwhile, over the same period, developments in euro area aggregate demand, rather than movements in the exchange rate, seem to explain the weakness of imports of intermediate goods.

Thus far, *import prices* of goods have shown little response to the appreciation of the euro (see Chart A). This is largely because the expected downward pressure on import prices resulting from the strengthening of the euro was more or less offset by rising oil prices, particularly during the build-up to the military operations in Iraq in the first quarter of 2003 (as shown in Chart E). However, import prices of manufactured goods – which are not directly affected by fluctuations in oil prices – fell by around 3.5% between the second quarter of 2002 and the first quarter of 2003, thereby reflecting the rise in the nominal effective exchange rate (NEER) of the euro.

Chart D: Extra-euro area import volumes for selected commodities [1)]

(index: 2000 = 100; seasonally adjusted; three-month moving averages)

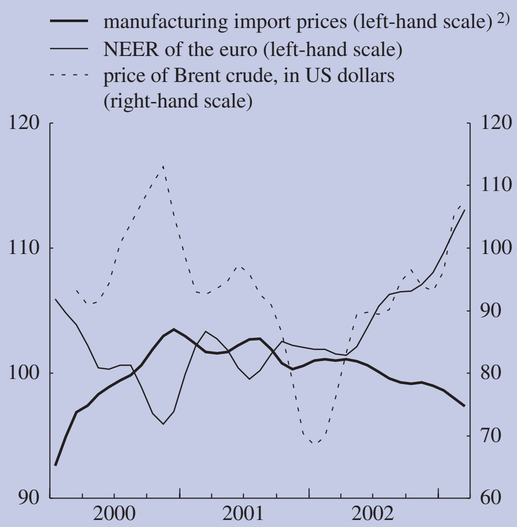


Sources: Eurostat and ECB calculations.

1) Latest observations are for March 2003.

Chart E: Extra-euro area manufacturing import prices, oil prices and NEER of the euro [1)]

(index: 2000 = 100; three-month moving averages)



Sources: Eurostat and ECB calculations.

1) Latest observations are for March 2003.

2) Seasonally adjusted data.