

Box 3

Euro cash changeover not expected to have a significant impact on consumer prices at the aggregate level

On 1 January 2002, the euro banknotes and coins were introduced and all prices in the euro area were converted into euro. Concerns have been raised by the public that the cash changeover could have triggered general price increases, starting already in 2001, as companies may have tried to increase profit margins by rounding up to new “attractive” euro prices. Furthermore, firms may have passed on costs related to the changeover to consumers. In recent months, consumer organisations and the media have reported examples of individual price increases interpreted as being euro-induced, i.e. resulting from the change from prices in legacy currencies to prices in euro. However, the euro cash changeover is not expected to have a significant impact on consumer prices at the aggregate level. Over a longer horizon, downward price movements should dominate, as the physical introduction of the euro will further strengthen competition in the euro area.

General considerations as well as available empirical evidence suggest that the risks of a significant upward impact on consumer prices should remain rather limited. First of all, competition in most markets in the euro area seems to be strong enough to limit any upward rounding. Moreover, downward rounding of prices is also likely. In fact, several euro area companies have taken the cash changeover as an opportunity to reduce prices in order to attract new customers and increase market shares. Second, the cyclical slowdown in euro area demand has also limited the scope for price increases. Third, consumers and consumer organisations have been vigilant and are monitoring the situation closely, also helped by the dual display of prices, making it more difficult for retailers to raise prices. Fourth, several items in the consumer price index should remain largely unaffected by any rounding, as psychological price-setting is less common for them, e.g. petrol, or they are contractually fixed, e.g. rents. Lastly, all central governments have ensured that the conversion of prices, charges and fees administered by them was price-neutral or smoothed in favour of the consumer. Local governments have been requested to follow this example.

In 2001, there were few concrete signs of generalised and sustained price increases owing to the cash changeover. Overall inflation in the euro area in terms of the Harmonised Index of Consumer Prices (HICP) has been falling steadily over recent months and there have been no noticeable movements in the main HICP components that would suggest changeover effects. This is backed up by monitoring exercises in several euro area countries, initiated by national statistical institutes, the Eurosystem and consumer organisations. By monitoring closely the price dynamics of selected consumer goods that are usually offered at attractive prices, these institutions and bodies have tried to estimate the actual impact of the conversion of prices into euro. Although these exercises have confirmed the evidence of euro-induced price increases for some specific products in individual countries, these changes have been negligible in terms of their effect on the overall HICP in the individual euro area countries and in the euro area as a whole. In this context, it should be stressed

that the identification of changeover effects is not straightforward. Any price changes might be due to either the changeover (i.e. rounding of prices or the pass-through of changeover costs), or they might reflect a change in other cost factors (e.g. wages or import prices) or a change in profit margins.

Since the start of this year, more anecdotal evidence of price increases for specific products has become available, which could be related to the cash changeover, but may also simply reflect price changes that are “normal” at the turn of the year. Further price adjustments can thus not be completely ruled out, particularly in markets characterised by a low level of competition and price-inelastic demand. However, even if these price changes were to be individually significant, it is not expected that they would have a strong impact on aggregated price developments in the coming months.

In conclusion, any upward effect on prices stemming from the cash changeover should be limited mainly owing to strong competition in euro area markets, the subdued demand situation and consumer vigilance. However, some uncertainty is still attached to this assessment and a clearer picture will emerge in the months to come. Nevertheless, any possible upward effect on prices will be of a one-off nature, while from a longer-term perspective, the introduction of the euro will increase price transparency across the euro area, which should encourage arbitrage and strengthen competition. Lastly, the permanent gains in terms of reduced transaction and information costs are expected to outweigh the one-off costs of the changeover, which should ultimately benefit consumers.