

Box 3

THE IMPACT OF DEVELOPMENTS IN INDIRECT TAXES AND ADMINISTERED PRICES ON INFLATION

Over recent years indirect taxes, particularly those on tobacco products, and administered prices have had an increasing upward impact on euro area HICP inflation and were one factor behind the relative stickiness of HICP inflation over the past couple of years. In the coming months some further upward impact may be expected, although there is still uncertainty about its precise timing and magnitude.

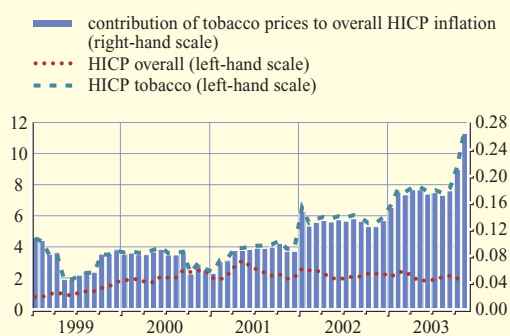
Indirect taxes

Indirect taxes are levied on many goods and services, either via value added taxes, which impact on a wide range of goods and services, or else via taxes on specific goods or services, such as energy or tobacco products. Since January 2002 taxes on tobacco products have been increased significantly, while increases in other indirect taxes have not been as pronounced.

In 2002 and 2003, there was an increase in tobacco excise duties in many euro area countries. Increases in tobacco taxes can mainly be explained as an effort to curb tobacco consumption for health reasons, but may also reflect the need for governments to raise revenues as a result of budgetary pressures. Since January 2002, the year-on-year rate of change in tobacco prices in the euro area has increased significantly (see Chart A), driven primarily by the higher taxation on tobacco products. In November 2003 the year-on-year rate of change in tobacco prices stood at 11.6%. Looking forward, in 2004 agreed and proposed increases in taxes should have a further upward impact on tobacco prices in a number of euro area countries.

Chart A Tobacco prices and overall HICP inflation

(annual percentage changes and percentage points)



Sources: Eurostat and ECB calculations.

Other indirect taxes, such as energy tax or value added tax (VAT), also impact on price developments. However, over the past two years, average VAT rates have remained broadly unchanged in the euro area. Similarly, while there has been some increase in energy taxes, these have not been as pronounced over the last two years as the increases in tobacco taxes.

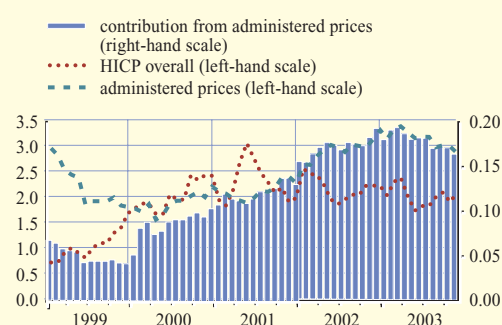
Administered prices

In addition to indirect tax changes, identifying developments in administered prices is also of interest, as they are not necessarily – at least not in the short run – driven by general macroeconomic factors such as external or internal price and cost pressures or the business cycle. However, defining administered prices is not easy, particularly at the euro area level. What is an administered price in one country could be market-determined in another. Even within countries it is not always easy to distinguish between administered prices and market-determined prices. Despite these caveats, Chart B illustrates the development of a proxy measure of administered prices within the services

component of the HICP.¹ The year-on-year rate of change in this proxy measure has been higher than overall HICP inflation since late 2001. However, the increase in the contribution of administered prices to HICP inflation has been even larger than that implied by the relative rates of change in administered prices and overall HICP. This is due to the extension since January 2001 of HICP coverage to some items relating to health, social protection and education services. It should be noted that these estimates refer only to a relatively narrow set of administered prices. There are other partly or fully administered prices in individual countries (e.g. regulated rents) that are not considered here. Looking forward, in 2004 agreed and proposed measures should have a further upward impact on administered prices, both for goods and services, in a number of euro area countries.²

Chart B Administered prices and overall HICP inflation

(annual percentage changes and percentage points)



Sources: Eurostat and ECB calculations.

Probable future developments

As already indicated, a further upward impact from tobacco taxes and administered prices may be envisaged in 2004, based on proposed or agreed measures. However, it is important to note that it is not always possible to identify or quantify these impacts in advance. Budgetary processes differ across countries, so that for some measures the implementation may be signalled in advance, whereas for others little information is made available. In addition, the data relating to the absolute prices (in euro) of specific goods and services, which would be needed to obtain a precise quantitative estimate of the impact, are not widely available. Lastly, in some cases, where prices are charged for the first time or the pricing structure is complex, it may not be clear in advance what the pass-through to or impact on the HICP will be.

For longer horizons, such as 2005 and beyond, very little information is at present available on planned changes in indirect taxes and administered prices. To the extent that such measures are often decided only shortly before implementation, they may imply revisions to previously published inflation forecasts and projections. This is because most forecasting and projection exercises, including those of the ECB, typically take into account only firmly planned or already decided fiscal measures.

1 Given differences across euro area countries only a crude and narrow proxy of administered prices may be constructed. The items included in this proxy measure are sewerage collection (HICP weight in 2003, 0.5%), refuse collection (0.5%), medical and paramedical services (0.9%), dental services (0.6%), hospital services (0.7%), passenger transport by railway (0.4%), postal services (0.2%), education (0.9%) and social protection (0.9%). Their aggregate HICP weight is 5.6%.

2 The anticipated changes in administered prices in 2004 relate to goods as well as to services prices, mainly healthcare.