

UPDATING MEASURES OF EURO AREA FOREIGN DEMAND TO ACCOUNT FOR CHANGES IN THE GEOGRAPHICAL STRUCTURE OF EURO AREA EXPORTS

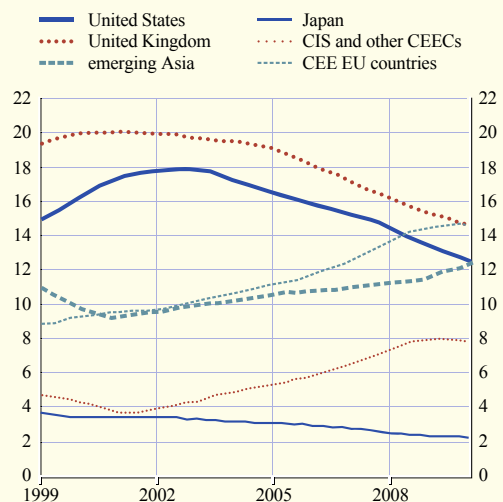
Together with changes in price and cost competitiveness, developments in foreign demand (i.e. global demand for euro area exports) are a primary determinant of euro area export growth. Accordingly, how measures of foreign demand are compiled is critically important for monitoring and forecasting extra-euro area exports as well as for evaluating the performance of euro area exporters in global export markets.¹ One integral element of these measurements is the geographical structure of euro area exports. Changes to this structure over time have implications for the measurement of euro area foreign demand and the assessment of the euro area's export performance. This box reviews recent developments in extra-euro area export shares and their impact on euro area foreign demand measures.

Euro area foreign demand is defined as a weighted average of imports of extra-euro area trade partners, using their share in extra-euro area exports of goods. Over the past few years the rapid expansion of global trade has been reflected in relatively high growth in extra-euro area exports: extra-euro area exports of goods increased in value terms by about 26% between 2005 and 2010,² compared with growth of about 35% in world trade. Moreover, the geographical structure of extra-euro area exports also changed significantly over the same period, in line with the changing pattern in world trade. In particular, the increasing integration of emerging economies into the world economy has been reflected in stronger euro area export flows to these countries, signalling that the euro area is increasingly benefiting from robust demand from these countries.

The changes in the trade structure of the euro area are also reflected in the evolution of euro area foreign demand weights, measured as a three-year moving average of extra-euro area export shares using data up to the first quarter of 2010 (see Chart A). One of the most striking features relates to the increase in the share of the central and eastern European (CEE) EU countries, reflecting the fast pace of growth in export flows to these countries following their accession to the European

Chart A Evolution of selected extra-euro area export shares

(percentages, based on three-year moving averages)



Sources: IMF Direction of Trade Statistics and ECB.

Notes: Last observation refers to the first quarter of 2010. The category CIS and other CEECs corresponds to the Commonwealth of Independent States and other central and eastern European countries; CEE EU countries comprise non-euro area countries that have joined the EU since 2004.

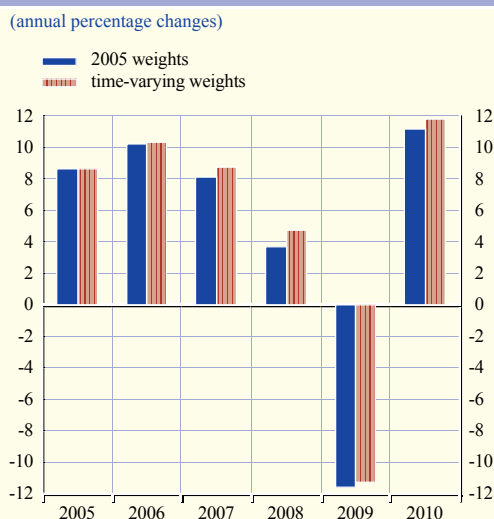
1 For more information on measuring foreign demand, see Hubrich, K. and Karlsson, T., "Trade consistency in the context of the Eurosystem projection exercises", *Occasional Paper Series*, No 108, ECB, March 2010.

2 Previous historical developments are covered in the boxes entitled "The geographical composition of euro area foreign demand", *Monthly Bulletin*, ECB, October 2004, and "Recent changes in the geographical composition of euro area foreign demand", *Monthly Bulletin*, ECB, October 2008.

Union. As a result, their weight in euro area foreign demand increased from 11.5% in 2005 to about 14.6% in 2010. Moreover, the increasing integration of economies such as China and the countries of the Commonwealth of Independent States (CIS) has also been reflected in a significant rise in export flows to these countries, and consequently in a higher share of these countries in extra-euro area exports. As a result, the weight of CIS countries (including Russia) and other CEE countries rose by 2.1 percentage points to about 8%, while the weight of emerging Asia increased by approximately 1.7 percentage points to 12.5%, mainly on account of China. By contrast, recent developments have confirmed the continuous decline in extra-euro area export shares of most advanced economies. In particular, the weight of the United Kingdom and the United States declined significantly during the period under review. In the case of the United Kingdom, traditionally the euro area's main individual trading partner, its share fell by almost 4 percentage points to about 15% in 2010. Emerging Asia now accounts for roughly the same share of extra-euro area exports as the United States.

In order to demonstrate the impact of an evolving geographical structure of extra-euro area exports in the computation of foreign demand, two different measures of foreign demand are shown in Chart B; one based on updated time-varying weights (using a three-year moving average of the shares) up to 2010 and an alternative series based on weights fixed at their 2005 average. Overall, the 2005 set of weights appears to underestimate annual growth in euro area foreign demand over the period 2006-10 by an average of around 0.5 percentage point. This highlights the importance of regularly updating the weights used to compute foreign demand so as to fully capture the effects of a changing geographical trade structure.

Chart B Two measures of euro area foreign demand



Sources: IMF Direction of Trade Statistics and ECB.