

Box 3

INDUSTRIAL PRODUCER PRICES FOR SALES IN DOMESTIC AND NON-DOMESTIC MARKETS

Developments in industrial producer prices provide analysts with two types of information. On the domestic side, they provide indications of inflationary pressures in final consumer prices that may be building up along the production chain. On the non-domestic side, they provide indications of competitiveness. In the latter case, it is useful to take into account the prices for sales in both domestic markets and non-domestic markets, as from the perspective of the individual firm, the pricing structure is likely to be determined on the basis of overall sales and profitability. This box reviews trends in industrial producer prices in the euro area for domestic and non-domestic sales and compares the strength of these trends before and after the onset of the crisis in 2008.

Recent euro area-wide trends

Euro area industrial producer prices for sales in domestic markets are an aggregation of the prices for domestic sales in each euro area country, while prices for sales to other euro area countries fall under non-domestic prices. In the years preceding the crisis, euro area producer prices for domestic sales recorded a much sharper increase than those for non-domestic sales, but also recorded a larger fall in the immediate aftermath of the crisis (see Chart A). Over the past few years domestic and non-domestic prices have developed in a broadly similar fashion. Among non-domestic prices, the increase in those for intra-euro area sales was stronger than that in those for sales to countries outside the euro area before the onset of crisis, but has been weaker since.

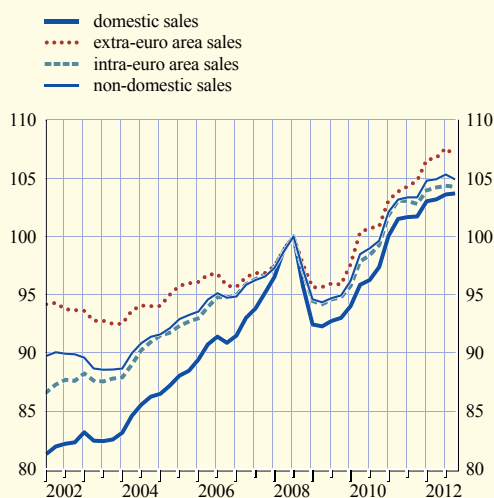
These relative trends broadly reflect the general economic developments across different regions. For example, a number of euro area countries experienced buoyant domestic demand in the pre-crisis period, which exerted upward pressure on prices for domestic sales. Conversely, in the period after the onset of the crisis, the relative strength of foreign demand outside the euro area supported more robust price increases in extra-euro area sales.

Euro area country and industry trends

In common with other euro area aggregate series, producer price developments at the euro area level conceal quite heterogeneous developments across countries. Furthermore, there are considerable differences across countries in the composition of the industrial sector in terms of intermediate, capital and

Chart A Total manufacturing producer prices for the euro area

(index: Q3 2008 = 100)



Sources: ECB calculations and Eurostat.

consumer goods production.¹ This implies, for instance, that countries with a large share of intermediate goods production can experience more pronounced movements in overall producer price inflation, owing to the more prevalent impact of fluctuations in commodity prices. It is therefore best to compare developments in domestic and non-domestic prices at both the individual country and industry level.

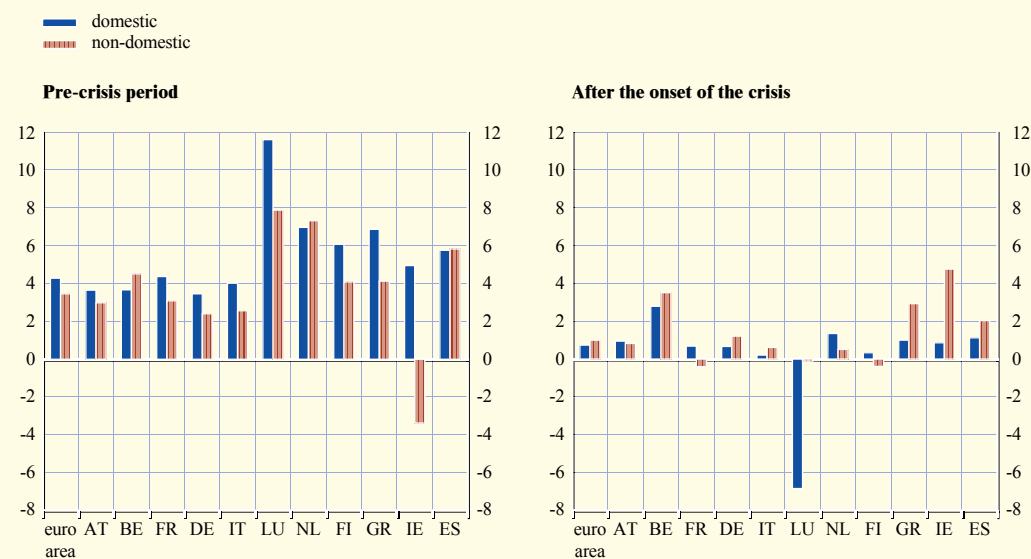
With regard to intermediate goods industries, in the four-year period prior to the crisis euro area domestic prices increased by 4.3% per annum on average and, thus, more strongly than non-domestic prices (3.5% per annum). In the period after the onset of the crisis, these relative magnitudes reversed slightly, with annual average price increases of 0.7% in domestic prices and 1.0% in non-domestic prices (see Chart B). This rebalancing between domestic and non-domestic price trends took place in the majority of euro area countries and was particularly pronounced in Greece, Ireland and Luxembourg. For instance, in Greece, the average annual increase in domestic prices in the pre-crisis period was roughly 3 percentage points higher than that in non-domestic prices, while it was about 2 percentage points lower after the onset of the crisis.

A similar picture can be observed for capital goods industries at the euro area level and in the majority of euro area countries – in particular Finland, but also Greece and Luxembourg (see Chart C). In Finland, this reversal in relative developments mainly reflects the change from

1 See also the box entitled “Update of the index and weight reference year to 2010 for short-term business statistics” in this issue of the Monthly Bulletin. For instance, the weight of non-durable consumer goods industries in the overall producer price index is relatively high in Ireland and Cyprus, while for capital goods this is the case in Germany and Finland, and for intermediate goods industries this is the case in Luxembourg and Malta.

Chart B Intermediate goods producer prices

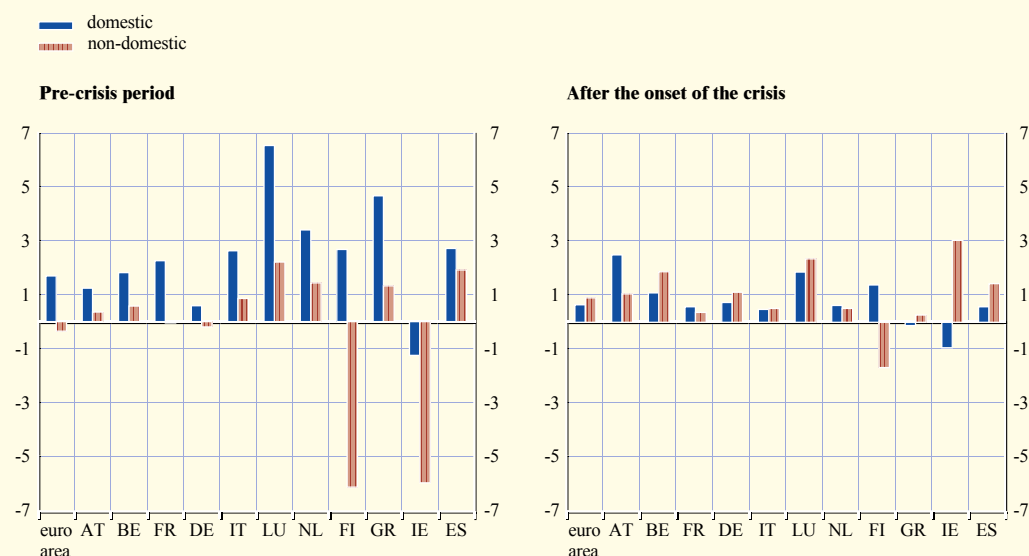
(annual average percentage changes)



Sources: ECB calculations and Eurostat.
Notes: The pre-crisis period is from the third quarter of 2004 to the third quarter of 2008. After the onset of the crisis covers the period from the third quarter of 2008 to the fourth quarter of 2012. Non-domestic price series are not available for Portugal. For presentational purposes, the countries are not listed in the EU protocol order.

Chart C Capital goods producer prices

(annual average percentage changes)



Sources: ECB calculations and Eurostat.

Notes: The pre-crisis period is from the third quarter of 2004 to the third quarter of 2008. After the onset of the crisis covers the period from the third quarter of 2008 to the fourth quarter of 2012. Non-domestic price series are not available for Portugal. For presentational purposes, the countries are not listed in the EU protocol order.

a pronounced average annual decline of 6.2% in non-domestic prices in the pre-crisis period to an average annual decrease of 1.7% after the onset of the crisis.

Finally, for non-durable consumer goods industries² in the euro area as a whole, there was again a stronger average increase in domestic prices than in non-domestic prices in the pre-crisis period and some reversal afterwards (see Chart D). This pattern was replicated across a number of countries, in particular France, Greece and Spain. However, it was not quite as consistent across countries as in the case of intermediate and capital goods industries. For instance, in Belgium, average increases in non-domestic prices were lower than those in domestic prices in both periods, while in Germany, they were higher in both periods.

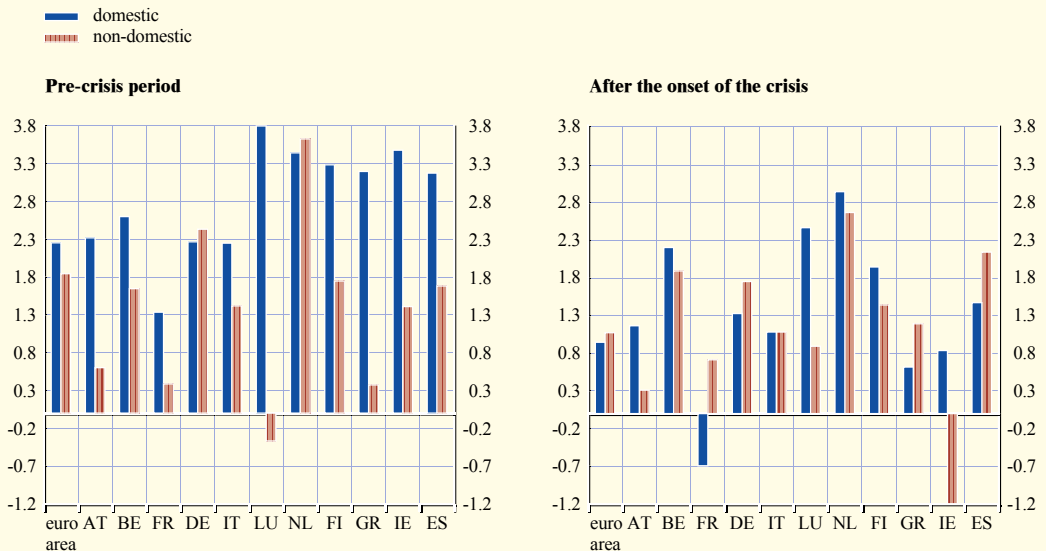
Changes in trends of domestic and non-domestic prices seem to be more pronounced in the smaller euro area countries. This may reflect the often more specialised nature of industries in these countries and the possibility that the industries are dominated by a small number of large and globally operating firms. In such cases, if a dominant firm comes under, for instance, strong pressure to adjust prices in international markets, or if it rapidly loses weight in the domestic industry by relocating its production elsewhere, this will be visibly evident in producer price developments for the industry as a whole.

Overall, the adjustment from relatively strong domestic price trends in the pre-crisis period to relatively strong non-domestic price trends after the onset of the crisis can be observed across sectors in the euro area countries. In a number of cases, this may reflect that in the pre-crisis period firms kept prices for non-domestic sales low and gained market shares by using profit

² The focus here is on non-durable consumer goods industries, as durable goods only account for a very small weight in the overall producer price index for manufacturing and industry.

Chart D Non-durable consumer goods producer prices

(annual average percentage changes)



Sources: ECB calculations and Eurostat.

Notes: The pre-crisis period is from the third quarter of 2004 to the third quarter of 2008. After the onset of the crisis covers the period from the third quarter of 2008 to the fourth quarter of 2012. Non-domestic price series are not available for Portugal. For presentational purposes, the countries are not listed in the EU protocol order.

margins realised in buoyant domestic markets. Since the onset of the crisis there has clearly been less scope for such pricing behaviour given the substantial deterioration in domestic demand conditions. However, in view of these conditions, the relative downward adjustment of domestic prices thus far seems to have been modest in a number of euro area countries, particularly those under financial stress. A conclusive assessment of pricing behaviour would need to draw on even more disaggregated data, especially in view of the highly specialised nature of the manufacturing sectors in the smaller economies.