

PART 1

MAIN DEVELOPMENTS

Methodological note

Since the issue for the second quarter of 2004, nominal and real effective exchange rates presented in this report are calculated based on a reference group of 41 countries. By extending the group of reference countries from 24 countries to 41 countries, over 80 percent of extra-EU12 exports instead of 58 percent are covered. The effective exchange rate calculations consequently better reflect trade patterns.

The new reference group has been constructed by extending the former IC24 group (which includes the initial 15 EU countries, Norway, Switzerland, Australia, the United States, Canada, Japan, Mexico, New Zealand and Turkey) with the ten recently acceded Member States, Bulgaria, Romania, Russia, China, Brazil, Korea and Hong Kong. Due to data constraints, real effective exchange rates based on unit labour costs cannot be calculated for this group. Therefore, for the time being, only real effective exchange rates calculated to measure *price competitiveness* (i.e., based on consumer price indices) are based on this new reference group (“broad group”). Real effective exchange rates calculated to measure *cost competitiveness* are based on a reference group of 34 countries (the former IC24 group plus the ten new Member States).

The “broad group” is included in the tables and charts where appropriate. In the tables and charts on pages 1 to 70 of part 2, each country’s relative position is assessed with respect to the rest of 34 countries (the EU25 countries, Norway, Australia, Canada, Japan, the United States, Mexico, New Zealand, Turkey and Switzerland), with the European Union and with the euro area.

Diverging movements in costs and prices may change the relative competitiveness positions of Member States. This report presents five measures of the real effective exchange rate of individual countries, EU25 and EU12 (abbreviations for the deflators are explained in the Annex). The different measures do not always give a uniform picture of the movement over time in the real effective exchange rate of a given country against its partners and, as such, the indicators of cost and price competitiveness need to be interpreted carefully.

DEVELOPMENTS OF PRICE AND COST COMPETITIVENESS IN THE EUROPEAN UNION, THE UNITED STATES AND JAPAN

MAIN FEATURES

The euro against major international currencies

- The euro continued its appreciation against most major currencies in the third quarter of 2006. The strongest appreciation of the euro exchange rate between the second and the third quarter of 2006 was recorded against the Japanese yen (3.0 percent). The appreciation against other major currencies was smaller (1.3 percent against the US dollar and 0.9 percent against the Swiss franc). On the other hand, the euro depreciated against the British pound sterling (1.2 percent) and the Swedish krona (0.7 percent). While the euro exchange rate stood roughly 15 percent above its 1995 to 2005 average against the US dollar and the Japanese yen in the third quarter of 2006, it was still below its medium-term average against the British pound sterling.
- All in all, the euro appreciated by 0.9 percent in nominal effective terms against the currencies of 29 countries between the second and the third quarter of 2006 and stood more than 14 percent above its 1995 to 2005 average.

Relative cost and price indicators: international developments

- Mainly driven by the nominal appreciation of the exchange rate, the international price and cost competitiveness of the euro area deteriorated further in the third quarter of 2006. Between the second and the third quarter of 2006, the real effective exchange rate appreciated by between 0.3 percent and 0.6 percent. As a result, the real effective exchange rate continued the diverging trend from its 1995 to 2005 average.
- In the US, a nominal effective depreciation of the US dollar by 0.7 percent led to a further improvement of price and cost competitiveness indicators in the third quarter of 2006, despite some worsening of the relative price and cost deflators. Price and cost competitiveness positions also improved in Japan between the second and the third quarter of 2006 but worsened in the UK.

Relative cost and price indicators: intra-euro area developments

- Cost competitiveness positions relative to the other euro area countries continued to improve in Germany, Finland, the Netherlands and Belgium/Luxemburg. Of the other Member States, Greece and Spain recorded the strongest losses in cost competitiveness, continuing the trend of previous quarters. As regards price competitiveness, all three measures indicated an improvement only in Finland. Ireland, on the other hand, was the only Member State experiencing a deterioration of all relative price competitiveness indicators. For all other Member States, the different deflators pointed into opposite directions.
- In a medium-term perspective, the intra-euro area cost competitiveness positions of Austria and, in particular, Germany continued to be more favourable than their 1995 to 2005 averages. On the other hand, Ireland, Portugal, Greece, Italy and Spain continued to face cost competitiveness positions that were considerably worse than their 1995 to 2005 averages. Price competitiveness positions were more favourable than their medium-term averages in Germany, Finland, France and Austria, while they were considerably worse in Spain, Italy, Greece and Ireland, with the exception that the Irish price competitiveness position based on export prices was somewhat better than its medium-term trend.

Relative cost and price indicators: intra-EU developments

- In non-euro area Member States, cost competitiveness improved significantly in Hungary and Cyprus between the second and third quarter of 2006. Of all other non-euro area Member States, Latvia and the UK recorded the strongest loss of cost competitiveness. The same trend was broadly reflected in price competitiveness indicators.
- Except for Sweden, cost competitiveness positions were worse than their 1995 to 2005 averages for all non-euro area Member States, with the cost indicators showing deviations ranging between 0.2 percent (Malta) and 30.1 percent (Czech Republic).

DATA ON PRICE AND COST COMPETITIVENESS

QUARTERLY REPORT - THIRD QUARTER 2006

I. INTERNATIONAL DEVELOPMENTS

1. BILATERAL EXCHANGE RATES OF THE EURO

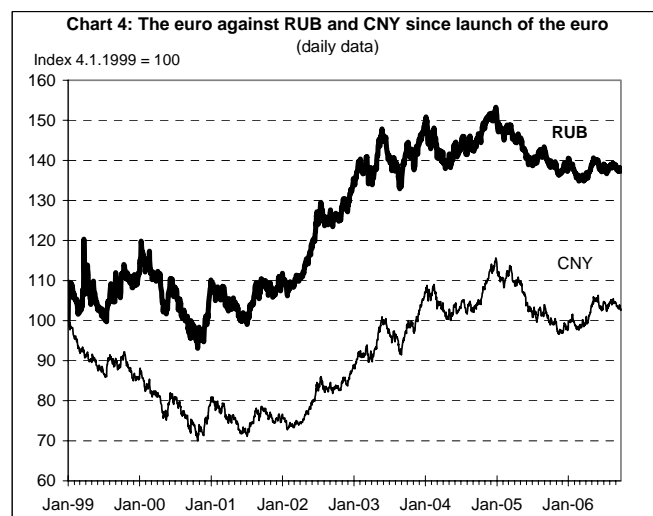
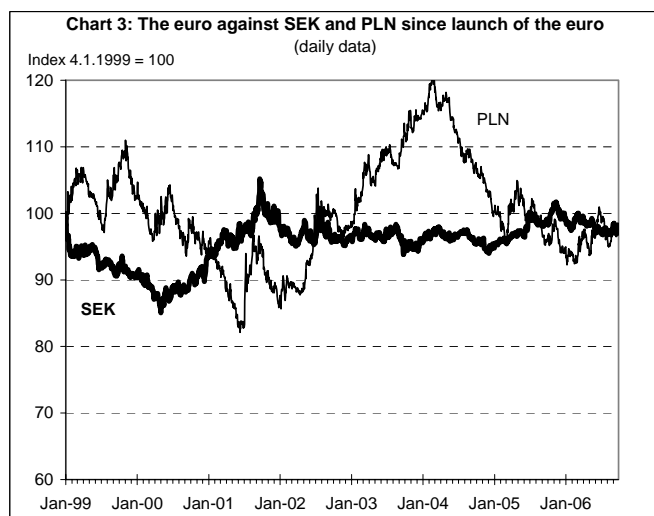
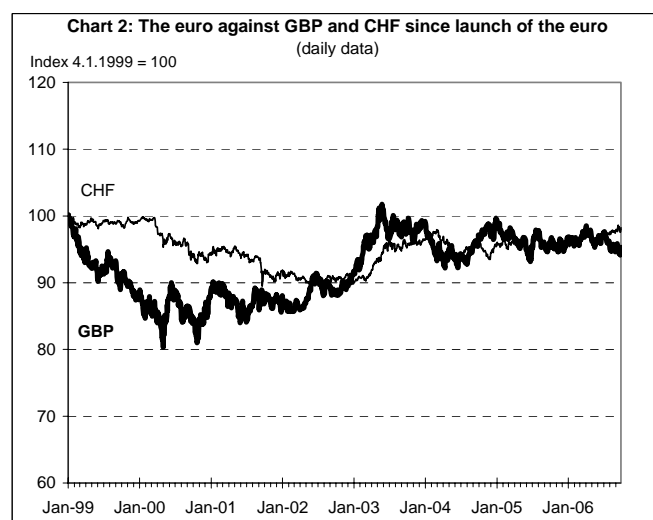
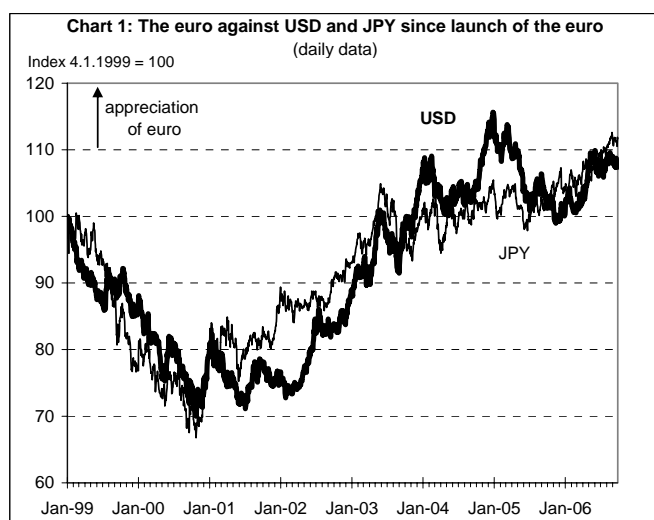


Table 1: Evolution of the bilateral exchange rates of euro area's main trading partners (quarterly averages)
Change relative to previous periods (quarterly averages; pre-1999: synthetic euro)

| | previous quarter Q3-06/Q2-06 | previous year Q3-06/Q3-05 | medium-term avg. Q3-06/avg 95-05 | | previous quarter Q3-06/Q2-06 | previous year Q3-06/Q3-05 | medium-term avg. Q3-06/avg 95-05 |
|---------|---------------------------------|------------------------------|-------------------------------------|---------|---------------------------------|------------------------------|-------------------------------------|
| USD/EUR | 1.3% | 4.5% | 13.9% | SEK/EUR | -0.7% | -1.4% | 2.7% |
| JPY/EUR | 3.0% | 9.2% | 16.5% | PLN/EUR | 0.1% | -1.6% | 1.1% |
| GBP/EUR | -1.2% | -0.5% | -1.7% | RUB/EUR | -0.1% | -1.8% | 53.2% |
| CHF/EUR | 0.9% | 1.5% | 1.0% | CNY/EUR | 0.7% | 2.3% | 20.2% |

2. NOMINAL EFFECTIVE EXCHANGE RATES

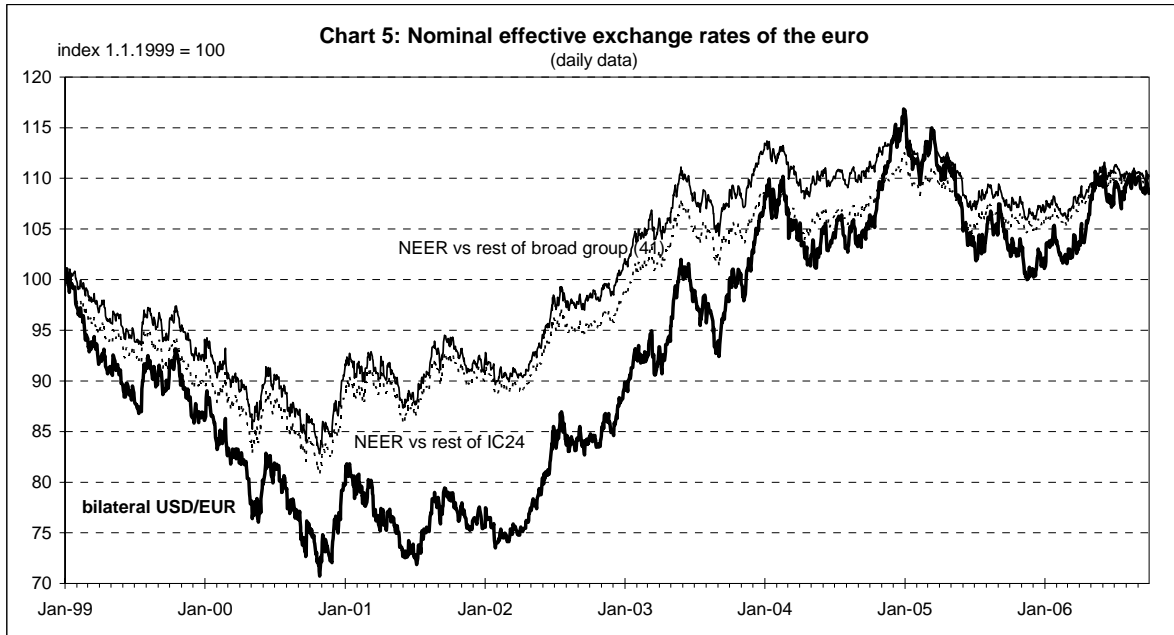
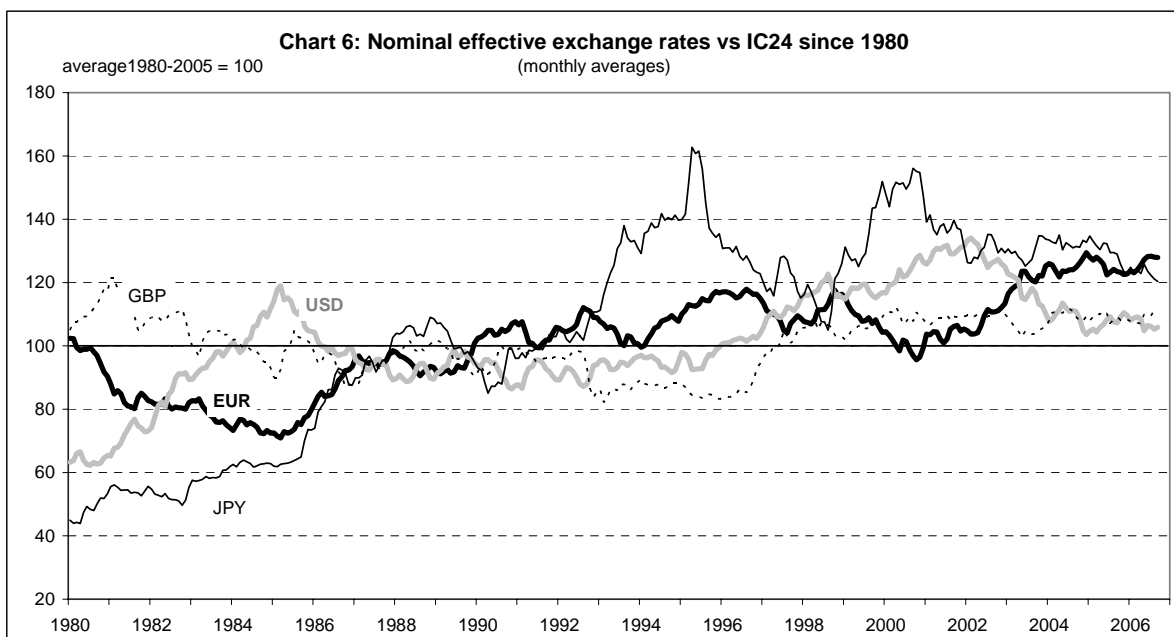


Table 2: Nominal effective exchange rates
(vs. broad group (41), index average 1999 = 100)

| | Third quarter of 2006 (monthly averages) | | | Change relative to previous periods (quarterly averages) | | |
|-------|---|--------|--------|---|------------------------------|------------------------------------|
| | Jul-06 | Aug-06 | Sep-06 | previous quarter Q3-06/Q2-06 | previous year Q3-06/Q3-05 | medium-term avg Q3-06/avg 95-05 |
| EUR12 | 115.2 | 115.0 | 114.8 | 0.7% | 2.2% | 14.6% |
| USA | 91.5 | 90.8 | 91.1 | -0.7% | -2.8% | -6.1% |
| Japan | 91.5 | 90.8 | 90.0 | -2.0% | -6.7% | -7.1% |
| UK | 103.5 | 105.4 | 105.5 | 1.9% | 2.2% | 8.5% |



3. PRICE COMPETITIVENESS BASED ON CPI (HICP WHEN AVAILABLE)

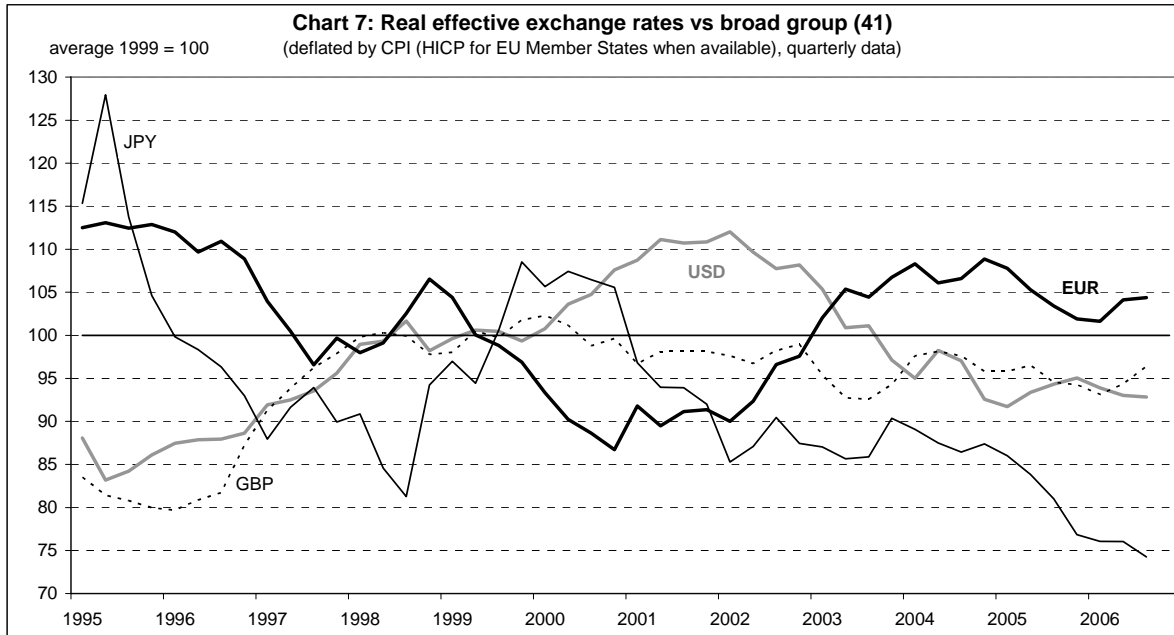
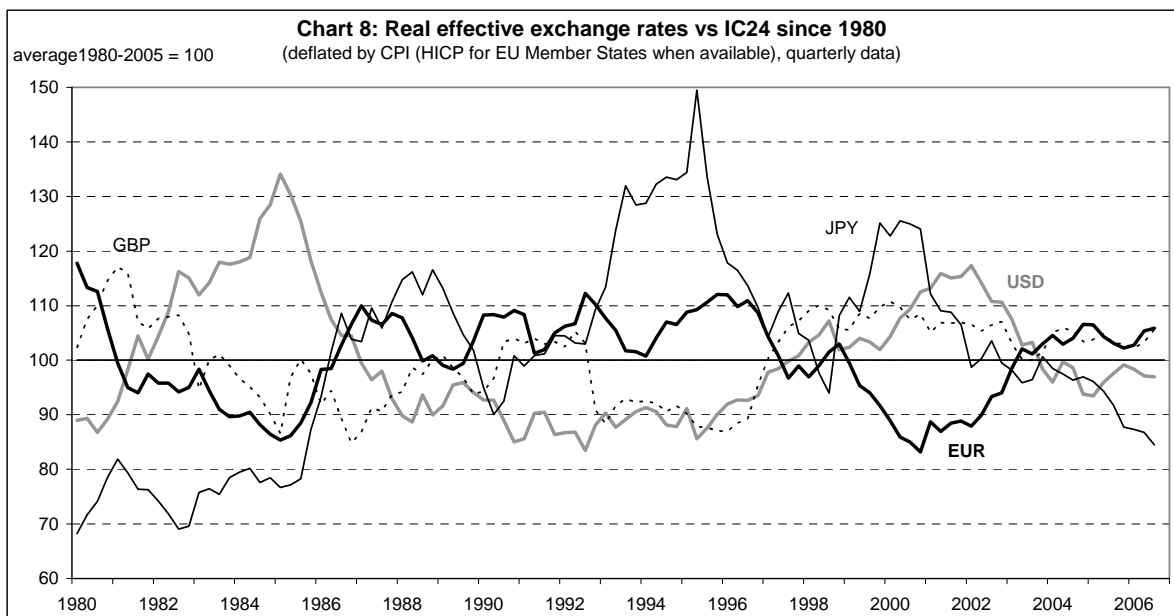


Table 3: Real effective exchange rates (CPI / HICP)
(vs. broad group (41), index average 1999 = 100)

| | Most recent four quarters (quarterly averages) | | | | Change relative to previous periods (quarterly averages) | | |
|-------|---|-------|-------|-------|---|------------------------------|------------------------------------|
| | Q4-05 | Q1-06 | Q2-06 | Q3-06 | previous quarter Q3-06/Q2-06 | previous year Q3-06/Q3-05 | medium-term avg Q3-06/avg 95-05 |
| EUR12 | 101.9 | 101.6 | 104.1 | 104.4 | 0.3% | 0.9% | 2.8% |
| USA | 95.0 | 93.9 | 93.0 | 92.8 | -0.2% | -1.6% | -5.5% |
| Japan | 76.9 | 76.1 | 76.1 | 74.3 | -2.4% | -8.3% | -21.1% |
| UK | 94.3 | 93.1 | 94.3 | 96.4 | 2.2% | 2.0% | 1.9% |



4. COST COMPETITIVENESS BASED ON UNIT LABOUR COSTS IN TOTAL ECONOMY

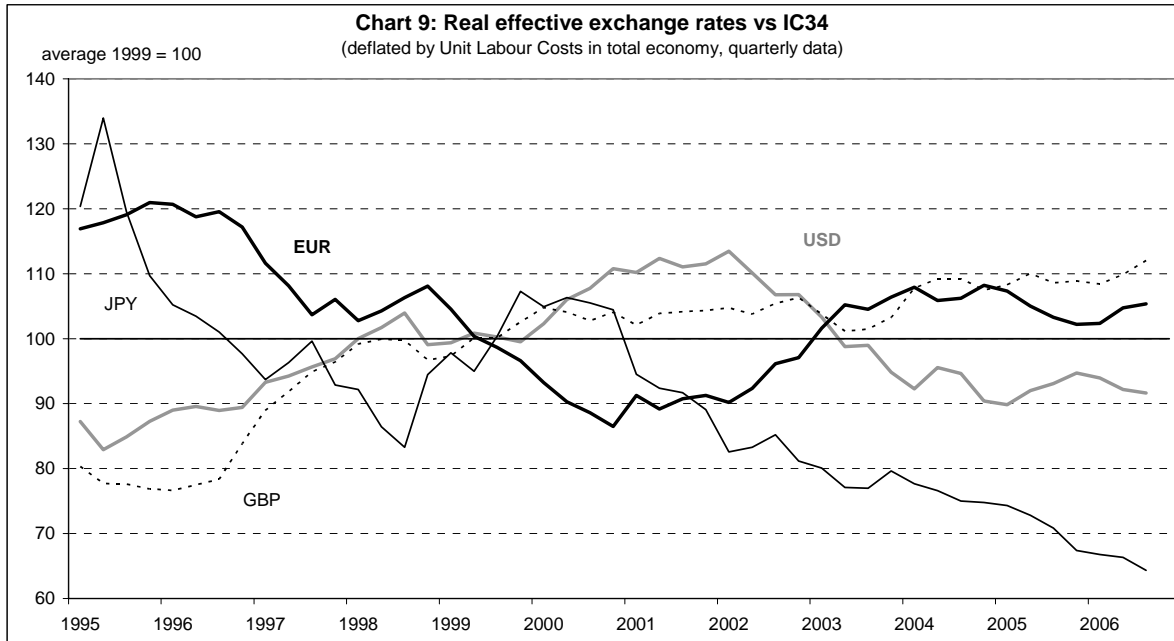
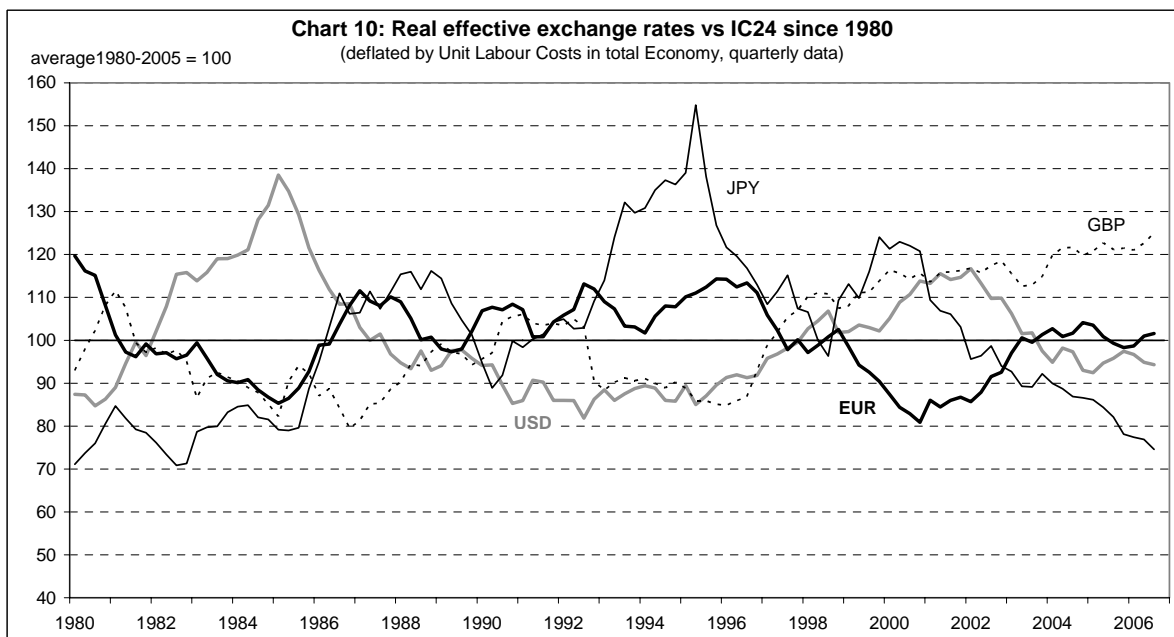


Table 4: Real effective exchange rates (ULCE)
(vs. 34 countries, index average 1999 = 100)

| | Most recent four quarters (quarterly averages) | | | | Change relative to previous periods (quarterly averages) | | |
|-------|---|-------|-------|-------|---|------------------------------|------------------------------------|
| | Q4-05 | Q1-06 | Q2-06 | Q3-06 | previous quarter Q3-06/Q2-06 | previous year Q3-06/Q3-05 | medium-term avg Q3-06/avg 95-05 |
| EUR12 | 102.2 | 102.4 | 104.8 | 105.3 | 0.6% | 2.0% | 1.6% |
| USA | 94.7 | 93.9 | 92.2 | 91.7 | -0.6% | -1.5% | -6.9% |
| Japan | 67.4 | 66.8 | 66.3 | 64.3 | -3.0% | -9.2% | -30.2% |
| UK | 108.9 | 108.4 | 109.8 | 112.0 | 2.0% | 3.2% | 13.9% |



5. COMPETITIVENESS OF THE USA AND JAPAN RELATIVE TO THE EURO AREA

Chart 11: Price and cost indicators for USA and Japan relative to EUR12

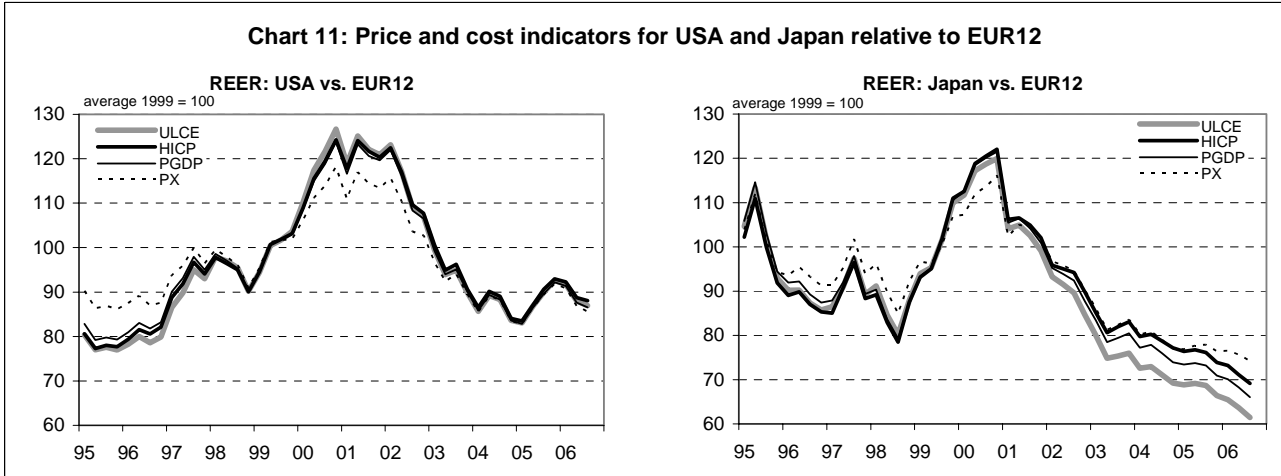
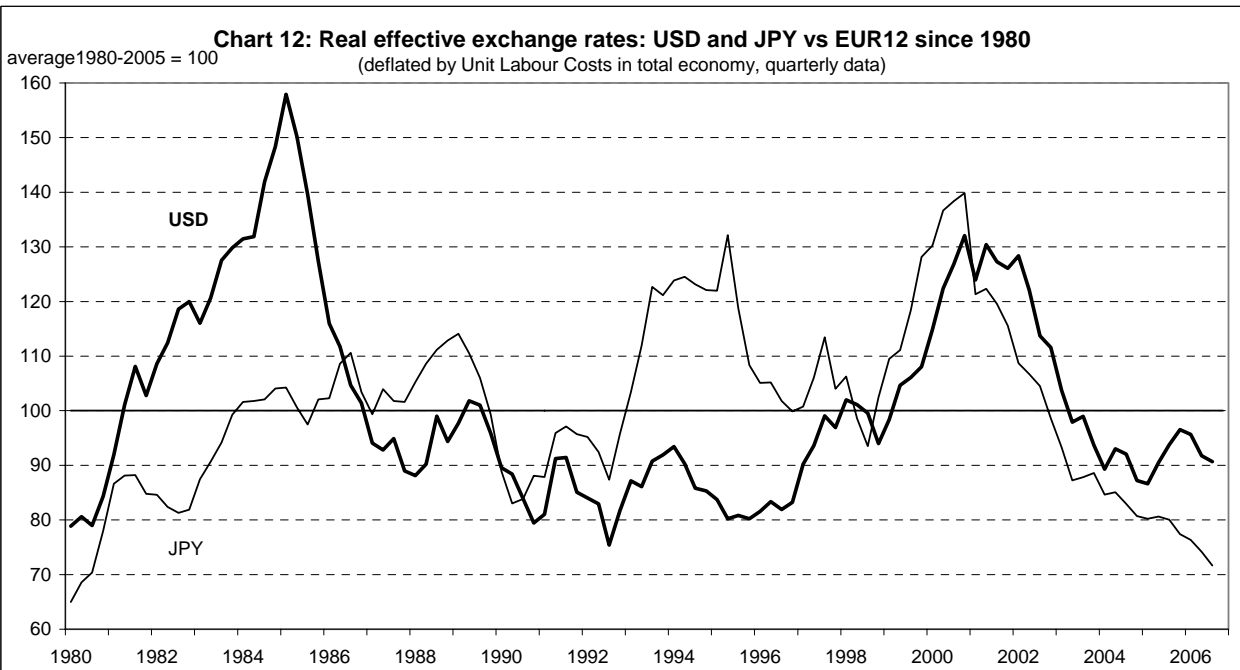


Table 5: Relative price and cost indicators of USA and Japan relative to EUR12

| % change | over last quarter Q3-06/Q2-06 | | | | over last year Q3-06/Q3-05 | | | | compared to medium term average Q3-06/avg. 95-05 | | | |
|----------|----------------------------------|-------|-------|-------|-------------------------------|-------|-------|-------|---|--------|--------|--------|
| | ULCE | PGDP | PX | HICP | ULCE | PGDP | PX | HICP | ULCE | PGDP | PX | HICP |
| USA | -1.2% | -1.3% | -1.5% | -0.7% | -3.3% | -3.4% | -4.3% | -2.8% | -10.3% | -11.0% | -11.9% | -9.4% |
| Japan | -3.4% | -3.2% | -1.8% | -2.8% | -10.5% | -9.8% | -4.7% | -9.2% | -31.6% | -28.1% | -20.6% | -25.0% |

Chart 12: Real effective exchange rates: USD and JPY vs EUR12 since 1980



II. DEVELOPMENTS AT MEMBER STATE LEVEL

| Table 6: Relative price and cost price indicators: intra euro area | | | | | | | | | | | | |
|---|----------------------------------|-------|-------|-------|-------------------------------|-------|-------|-------|---|-------|--------|-------|
| % change | over last quarter Q3-06/Q2-06 | | | | over last year Q3-06/Q3-05 | | | | compared to medium term average Q3-06/avg. 95-05 | | | |
| | ULCE | PGDP | PX | HICP | ULCE | PGDP | PX | HICP | ULCE | PGDP | PX | HICP |
| BLEU | -0.1% | 0.2% | -0.1% | -0.1% | 0.0% | 0.7% | 0.1% | 0.2% | 0.1% | 1.0% | 6.8% | -0.2% |
| Germany | -0.5% | -0.3% | -0.6% | 0.4% | -2.0% | -1.5% | -2.4% | -0.6% | -11.0% | -9.4% | -9.6% | -4.3% |
| Greece | 0.8% | 0.3% | -0.2% | -1.0% | 3.0% | 1.5% | -0.4% | 1.5% | 9.6% | 8.3% | 7.5% | 4.6% |
| Spain | 0.6% | 0.6% | 0.1% | -0.4% | 2.1% | 2.7% | 0.7% | 1.5% | 7.5% | 13.4% | 7.3% | 6.3% |
| France | 0.3% | 0.0% | 0.1% | 0.0% | 1.1% | 0.0% | -0.5% | -0.2% | 1.1% | -2.4% | -6.2% | -1.3% |
| Ireland | 0.3% | 0.3% | 0.3% | 0.5% | 1.9% | 1.3% | 1.0% | 0.8% | 12.0% | 12.0% | -0.9% | 7.6% |
| Italy | 0.1% | 0.2% | 0.7% | -0.2% | 0.4% | 0.6% | 3.4% | 0.3% | 8.2% | 6.9% | 21.6% | 3.5% |
| Netherlands | -0.1% | -0.1% | 0.5% | -0.3% | -0.4% | -0.2% | 2.6% | -0.3% | 4.9% | 4.0% | 3.3% | 1.6% |
| Austria | 0.2% | 0.1% | -0.2% | -0.2% | 0.9% | 0.6% | -0.9% | -0.2% | -2.0% | -0.1% | -1.5% | -1.7% |
| Portugal | 0.1% | -0.1% | -0.1% | 0.0% | 0.6% | -0.4% | -0.5% | 0.6% | 9.6% | 5.3% | -0.6% | 4.6% |
| Finland | -0.2% | -0.3% | -0.2% | -0.4% | -0.4% | -0.8% | -1.3% | -0.8% | 0.1% | -3.0% | -13.9% | -4.1% |

| Table 7: Relative price and cost price indicators: intra EU25 | | | | | | | | | | | | |
|--|----------------------------------|-------|-------|-------|-------------------------------|--------|--------|-------|---|--------|--------|-------|
| % change | over last quarter Q3-06/Q2-06 | | | | over last year Q3-06/Q3-05 | | | | compared to medium term average Q3-06/avg. 95-05 | | | |
| | ULCE | PGDP | PX | HICP | ULCE | PGDP | PX | HICP | ULCE | PGDP | PX | HICP |
| BLEU | -0.3% | 0.0% | -0.3% | -0.3% | -0.3% | 0.4% | -0.2% | 0.0% | -1.8% | -0.1% | 6.6% | -0.3% |
| Czech Rep | 0.1% | 0.4% | -0.3% | 0.5% | 4.3% | 5.2% | 1.5% | 5.1% | 30.1% | 25.9% | 9.0% | 22.4% |
| Denmark | -0.2% | 0.2% | 0.0% | -0.4% | -0.3% | 1.6% | 1.3% | -0.5% | 1.5% | 4.3% | 7.3% | -0.2% |
| Germany | -0.6% | -0.5% | -0.7% | 0.1% | -2.2% | -1.7% | -2.4% | -0.7% | -12.5% | -10.2% | -8.9% | -4.6% |
| Estonia | 0.4% | 0.1% | 0.0% | 1.0% | 2.0% | 1.4% | 0.7% | 2.2% | 14.9% | 18.2% | 14.0% | 14.3% |
| Greece | 0.6% | 0.1% | -0.4% | -1.2% | 2.7% | 1.2% | -0.7% | 1.3% | 7.6% | 7.0% | 6.9% | 4.3% |
| Spain | 0.4% | 0.4% | -0.1% | -0.6% | 1.8% | 2.5% | 0.4% | 1.4% | 5.7% | 12.3% | 7.3% | 6.1% |
| France | 0.0% | -0.2% | -0.2% | -0.3% | 0.7% | -0.3% | -0.8% | -0.4% | -1.1% | -3.5% | -6.0% | -1.3% |
| Ireland | 0.0% | -0.1% | -0.1% | 0.1% | 1.3% | 0.9% | 0.4% | 0.5% | 8.7% | 10.5% | -0.7% | 7.7% |
| Italy | -0.1% | 0.0% | 0.5% | -0.4% | 0.1% | 0.4% | 3.0% | 0.1% | 5.8% | 5.4% | 20.8% | 3.1% |
| Cyprus | -0.7% | -0.4% | 0.1% | -0.9% | -1.3% | -0.4% | 1.4% | -0.3% | 2.6% | 6.6% | 8.8% | 4.6% |
| Latvia | 1.4% | 0.9% | 0.4% | 0.6% | 6.0% | 4.9% | 3.0% | 4.1% | 4.0% | 13.0% | 20.2% | 7.2% |
| Lithuania | -0.1% | 0.3% | 0.6% | 0.3% | 0.8% | 2.2% | 4.1% | 1.5% | 17.3% | 20.8% | 31.7% | 15.8% |
| Hungary | -3.6% | -3.0% | -3.3% | -1.7% | -11.6% | -10.2% | -11.4% | -8.8% | 12.2% | 9.9% | -11.2% | 11.2% |
| Malta | 0.1% | 0.2% | -0.2% | -0.2% | 0.6% | 1.8% | 0.3% | 1.0% | 0.2% | 4.2% | -1.3% | 5.7% |
| Netherlands | -0.3% | -0.3% | 0.3% | -0.5% | -0.7% | -0.5% | 2.2% | -0.5% | 2.9% | 2.9% | 3.2% | 1.5% |
| Austria | 0.1% | 0.0% | -0.3% | -0.3% | 0.8% | 0.5% | -0.9% | -0.2% | -4.1% | -1.6% | -1.7% | -2.7% |
| Poland | 0.1% | -0.5% | 0.5% | -0.3% | 3.1% | 0.5% | 2.3% | 1.0% | 3.2% | 8.1% | 14.1% | 10.7% |
| Portugal | -0.1% | -0.3% | -0.3% | -0.2% | 0.3% | -0.6% | -0.8% | 0.5% | 7.9% | 4.4% | -0.6% | 4.5% |
| Slovenia | 0.2% | 0.3% | -0.4% | 0.1% | 0.6% | 0.9% | -1.2% | 0.4% | 1.4% | 1.0% | -0.6% | 2.8% |
| Slovakia | 0.2% | 0.3% | 0.0% | -0.5% | 4.4% | 5.2% | 3.4% | 4.9% | 21.0% | 24.3% | 10.8% | 32.7% |
| Finland | -0.5% | -0.5% | -0.4% | -0.7% | -1.0% | -1.3% | -1.7% | -1.1% | -2.2% | -4.3% | -13.9% | -4.1% |
| Sweden | 0.9% | 0.6% | 0.2% | 0.3% | 2.3% | 1.4% | 0.2% | 0.9% | -2.8% | -5.7% | -6.9% | -5.9% |
| UK | 1.4% | 1.4% | 1.6% | 1.8% | 1.5% | 1.0% | 2.0% | 0.9% | 8.4% | 3.4% | -1.0% | -1.8% |

Table 8: Relative price and cost price indicators of the EU Member States vs. rest of IC34

| % change | over last quarter Q3-06/Q2-06 | | | | over last year Q3-06/Q3-05 | | | | compared to medium term average Q3-06/avg. 95-05 | | | |
|-------------|----------------------------------|-------|-------|-------|-------------------------------|-------|--------|-------|---|-------|--------|-------|
| | ULCE | PGDP | PX | HICP | ULCE | PGDP | PX | HICP | ULCE | PGDP | PX | HICP |
| BLEU | 0.1% | 0.4% | 0.0% | 0.0% | 0.6% | 1.5% | 0.7% | 1.0% | 1.1% | 2.6% | 8.7% | 2.0% |
| Czech Rep | 0.3% | 0.6% | -0.1% | 0.7% | 4.8% | 5.8% | 2.0% | 5.7% | 31.8% | 27.6% | 10.1% | 23.9% |
| Denmark | 0.3% | 0.7% | 0.5% | 0.1% | 0.8% | 2.8% | 2.2% | 0.7% | 4.7% | 6.8% | 8.1% | 2.6% |
| Germany | -0.1% | 0.1% | -0.1% | 0.6% | -0.6% | 0.0% | -0.9% | 0.7% | -8.0% | -5.9% | -5.5% | -1.2% |
| Estonia | 0.7% | 0.4% | 0.3% | 1.3% | 2.6% | 2.0% | 1.2% | 2.8% | 15.9% | 18.9% | 13.9% | 15.2% |
| Greece | 1.1% | 0.6% | 0.1% | -0.8% | 4.0% | 2.6% | 0.5% | 2.4% | 10.2% | 9.3% | 9.1% | 5.8% |
| Spain | 0.7% | 0.8% | 0.2% | -0.3% | 2.7% | 3.5% | 1.3% | 2.3% | 8.2% | 14.7% | 9.1% | 8.1% |
| France | 0.5% | 0.3% | 0.3% | 0.1% | 1.9% | 1.1% | 0.4% | 0.8% | 2.5% | -0.1% | -3.3% | 1.4% |
| Ireland | 0.6% | 0.6% | 0.5% | 0.6% | 2.9% | 2.6% | 2.0% | 2.0% | 14.3% | 15.7% | 3.3% | 12.1% |
| Italy | 0.4% | 0.5% | 0.9% | 0.1% | 1.4% | 1.9% | 4.3% | 1.4% | 9.5% | 9.0% | 23.5% | 6.0% |
| Cyprus | -0.3% | 0.0% | 0.5% | -0.6% | -0.2% | 0.7% | 2.3% | 0.6% | 5.0% | 8.6% | 10.6% | 6.0% |
| Latvia | 1.6% | 1.2% | 0.7% | 0.9% | 6.6% | 5.5% | 3.6% | 4.7% | 5.0% | 14.0% | 20.6% | 8.1% |
| Lithuania | 0.2% | 0.7% | 1.0% | 0.7% | 1.4% | 3.1% | 4.9% | 2.2% | 18.3% | 21.9% | 32.5% | 16.7% |
| Hungary | -3.4% | -2.7% | -3.0% | -1.4% | -11.0% | -9.6% | -10.9% | -8.2% | 13.6% | 11.2% | -10.3% | 12.3% |
| Malta | 0.9% | 1.0% | 0.5% | 0.5% | 2.9% | 4.0% | 2.1% | 3.1% | 6.9% | 10.3% | 3.3% | 10.8% |
| Netherlands | 0.0% | 0.0% | 0.6% | -0.2% | 0.1% | 0.5% | 3.0% | 0.3% | 5.1% | 4.9% | 4.7% | 3.3% |
| Austria | 0.5% | 0.4% | 0.1% | 0.1% | 1.6% | 1.5% | 0.0% | 0.7% | -2.1% | 0.5% | -0.1% | -0.8% |
| Poland | 0.3% | -0.2% | 0.7% | -0.1% | 3.6% | 1.1% | 2.9% | 1.6% | 4.4% | 9.1% | 14.6% | 11.8% |
| Portugal | 0.2% | 0.0% | 0.0% | 0.0% | 1.0% | 0.2% | -0.1% | 1.1% | 9.9% | 6.3% | 0.8% | 6.2% |
| Slovenia | 0.5% | 0.6% | -0.1% | 0.4% | 1.3% | 1.7% | -0.5% | 1.0% | 2.3% | 1.8% | 0.1% | 3.5% |
| Slovakia | 0.4% | 0.6% | 0.2% | -0.3% | 5.0% | 5.8% | 4.0% | 5.4% | 22.2% | 25.5% | 11.6% | 33.8% |
| Finland | 0.1% | 0.1% | 0.1% | -0.2% | 0.4% | 0.2% | -0.5% | 0.2% | 1.7% | -1.0% | -12.0% | -1.0% |
| Sweden | 1.5% | 1.3% | 0.8% | 0.9% | 3.6% | 2.8% | 1.4% | 2.2% | 1.0% | -3.0% | -6.1% | -2.6% |
| UK | 2.0% | 2.0% | 2.2% | 2.2% | 3.2% | 2.8% | 3.6% | 2.4% | 13.7% | 8.2% | 2.7% | 2.4% |