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Executive Summary

„Analyse der Terms-of-Trade Österreichs"

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Abstract

Terms-of-trade (ToT) refer to the amount of goods a country can import per unit of goods exported, i.e. the relation of export to import prices. As different factors have worked in opposite directions, Austria's ToT evolved relatively stable in the long run. Therefore, not only their development over time and in different sectors is the subject of this study, but also the determinants and their effects on the evolution of the Terms-of-Trade: We discuss monetary (crude oil price, exchange rate) and non-monetary determinants (product mix, product variety/quality, capital accumulation).

Keywords: Terms of Trade, Exchange rates, Exports

JEL-codes: F14, F31, F41

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Analysis of Austria's Terms-of-Trade – Executive Summary

Terms-of-trade (ToT) refer to the amount of goods a country can import per unit of goods exported, i.e. the relation of export to import prices. As different factors have worked in opposite directions, Austria's ToT evolved relatively stable in the long run. Therefore, not only their development over time and in different sectors is the subject of this study, but also the determinants and their effects on the evolution of the ToT: We discuss monetary (crude oil price, exchange rate) and non-monetary determinants (product mix, product variety/quality, capital accumulation).

Compared to other commodities, crude oil plays a dominant role in the evolution of foreign trade prices, since it is an important factor of production that is still hardly substitutable in current production processes. The price increase of crude oil weighs on the ToT of Austria, since it is an oil importing country. With regard to the other monetary factor, the nominal exchange rate, the analysis shows that domestic exporters set their prices mainly according to foreign market conditions ("pricing to market"). Hence, they bear the bulk of the foreign exchange risk: Depreciations tend to raise the ToT and exporters' profits; appreciation – dominating during the years since 1971 – requires productivity increases above average in order to maintain international competitiveness.

With regard to non-monetary factors, a reverse Prebisch-Singer trend prevails, which is typical for industrial countries: The demand for domestic manufactured goods is rather price and income elastic, its supply rather price inelastic. Such a product mix fosters the ToT over time (as opposed to commodity and primary goods exporting countries, whose ToT tend to decrease over time). Furthermore, compared to other industrial countries, Austria's export portfolio is qualitatively very high and broad, improving its export market share, trade balance and ToT: The broadening of the export portfolio (horizontal product differentiation) and quality improvements within product categories (vertical product differentiation) raise foreign demand for domestic goods. In turn, these effects counteract the downward pressure on the ToT that emerges from above-average GDP growth through higher export supply and enhanced import demand.

The technological intensity of a sector itself plays a minor role in ToT development, more so its change over time and especially its change vis-à-vis competitors. Quality induced ToT improvements contribute to the evolution of sector specific export market shares, but even more so do learning and spillover effects that can emerge from a tighter connection of exports to the specialization profile of domestic manufacturing.