



Brussels, 12.2.2013
COM(2013) 69 final

**REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND
THE COUNCIL**

**on the implementation of Regulation (EC) No 450/2003 of the European Parliament and
of the Council concerning the labour cost index (LCI)**

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1. INTRODUCTION

Regulation (EC) No 450/2003 of the European Parliament and of the Council of 27 February 2003 concerning the labour cost index¹ (referred to here as the ‘LCI Regulation’) establishes a common framework for producing and transmitting comparable labour cost indices in the European Union. The Commission (Eurostat) publishes a quarterly news release on the hourly labour cost index². Complete data are available online, broken down by economic activity and labour cost components. In addition to the index figures, both quarter-on-quarter and year-on-year growth rates are published.

In July 2003, the Commission adopted Regulation (EC) No 1216/2003³, setting out in greater detail the procedures for transmitting the index, the specific (seasonal) adjustments to be made and the content of the national quality reports. Then in March 2007, the Commission adopted Regulation (EC) No 224/2007⁴. It amends Regulation (EC) No 1216/2003 and extends the scope of the labour cost index to cover the economic activities defined by NACE Rev. 1, sections L, M, N and O. This extension means that non-market services, which account for the major share of these sections and which may have different dynamics from market services, are also covered. In August 2007, the Commission adopted Regulation (EC) No 973/2007⁵. This amended a number of regulations on specific statistical domains, among them the Labour Cost Index, in order to implement the statistical classification of economic activities NACE Revision 2.

Pursuant to Article 13 of Regulation (EC) No 450/2003 the Commission must submit a report to the European Parliament and the Council every two years. The report should examine the quality of the LCI data in particular. The current report refers to the transmissions of LCI data from reference quarter 2010Q3 to quarter 2012Q2.

In Annex I of Regulation (EC) No 1216/2003, the quality of the labour cost index is defined in terms of the following dimensions: relevance, accuracy, timeliness and punctuality, accessibility and clarity, comparability, coherence and completeness.

¹ *OJ L 69, 13.3.2003, p.1.*

² The quarterly news release is published on the dates set in the release calendar; both can be found on Eurostat’s website (<http://ec.europa.eu/eurostat>).

³ Commission Regulation (EC) No 1216/2003 of 7 July 2003 implementing Regulation (EC) No 450/2003 of the European Parliament and of the Council concerning the labour cost index (OJ L 169, 8.7.2003, p. 37).

⁴ Commission Regulation (EC) No 224/2007 of 1 March 2007 amending Regulation (EC) No 1216/2003 as regards the economic activities covered by the labour cost index (OJ L 64, 2.3.2007, p. 23).

⁵ Commission Regulation (EC) No 973/2007 of 20 August 2007 amending certain EC Regulations on specific statistical domains implementing the statistical classification of economic activities NACE Revision 2 (OJ L 216, 21.8.2007, p. 10).

As in the last reporting period, the level of accuracy, accessibility and clarity remains satisfactory. This report will therefore focus on improvements made concerning relevance and coverage and address the issues of coherence with national accounts data and comparability with respect to working-day adjusted data. Particular attention is paid to the problem of the punctuality of data transmissions, and the impact of late data transmissions on the quality of the published European aggregates.

2. GENERAL PROGRESS SINCE THE LAST REPORT

The major changes introduced in 2009 relating to the introduction of the new NACE Rev.2 classification and the coverage of non-market services were described in the 2010 report⁶. Since the last report, progress has been made on a number of specific issues.

Generally speaking, the availability and quality of the labour cost index (LCI) continued to improve. Progress was made in making seasonally adjusted data available, to the extent that in the foreseeable future the seasonally adjusted LCI could become the main reference in Eurostat's press releases, as is the case for all other infra-annual macroeconomic statistics. National quality reports were increasingly provided on time and almost all Member States now report the metadata on a quarterly basis, explaining changes in the data and providing useful background information. The volatility of the index has decreased, thanks mainly to the improvement in the hours-worked series, which continues to be closely monitored.

One of the areas that have received more attention during the last two years is the coherence of the Labour Cost Index with other Labour Cost statistics, with a particular focus on quarterly national accounts data. Coherence has been analysed from both a theoretical and an empirical point of view and the results have been discussed with the Member States.

The Commission (Eurostat) has also improved the availability of timely data on hourly labour cost levels using estimates which make prominent use of the labour cost index. Feedback from users on this innovation was very positive. Member States were involved in the process and experiences relating to this exercise were shared.

Despite these positive developments, there are still a number of issues which require further efforts by certain Member States in order to complete the harmonisation process. These issues are discussed below.

While the Member States have implemented and maintained the necessary infrastructure for the production of the LCI, the Commission (Eurostat) has maintained and enhanced its production system for the reception, verification, processing, storage and dissemination of the Labour Cost Index data in a timely manner. These processes, which became fully operational in 2005, are continuously reviewed and updated.

3. EVALUATION OF QUALITY AND THE IMPACT ON EUROPEAN AGGREGATES

3.1 Relevance

Changes in labour costs per hour worked are a significant indicator for the analysis of short- and medium-term economic developments. The Commission and the European Central Bank

⁶ COM (2011) 102.

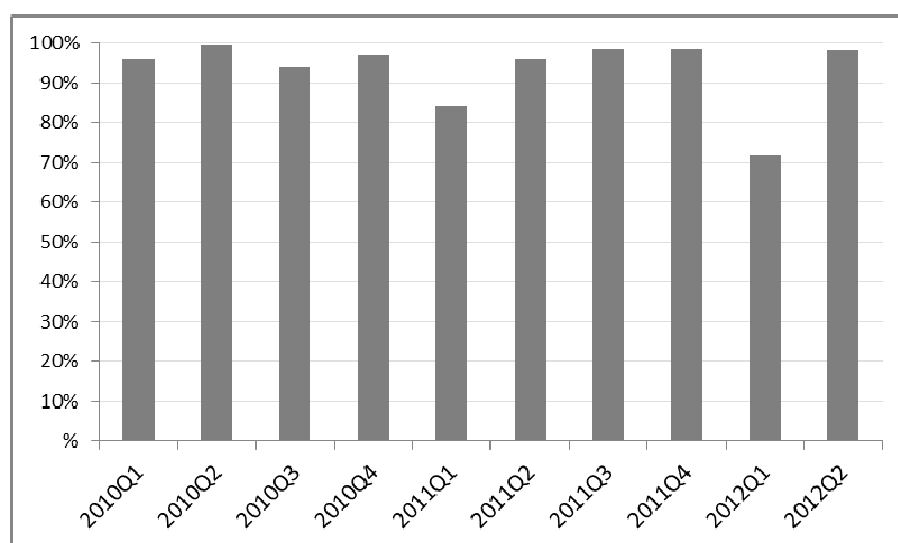
rely on an index of labour costs per hour worked, which shows the short-term evolution of labour costs, to assess possible inflationary pressure due to developments in the labour market. The index needs to be calculated promptly, for each Member State, for the whole EU and for the euro area. The labour cost index is also important for the social partners in wage negotiations and for the Commission itself in monitoring short-term developments in labour costs. The Labour Cost Index (LCI) is one of the Principal European Economic Indicators (PEEI)⁷.

Besides the demand for information on quarterly percentage changes in labour costs as measured by the LCI, there is a growing interest in information on labour costs in absolute terms (euros per hour). In April 2012, Eurostat published for the first time early estimates (for 2011) of hourly labour costs in euro and national currencies. These estimates are based on 2008 Labour Cost Survey benchmark data, which have been extrapolated to 2011 using the LCI non-seasonally adjusted data. The estimates meet a strong user demand for timely and complete information on the level of hourly labour costs. The Commission has received positive feedback regarding this use of the LCI figures, and several users have expressed their interest in breakdowns by NACE sections as well as cost components. In order to meet this demand, Eurostat is now in the process of implementing a regular production environment so as to make full use of the available information from the LCI. Member States are, and will continue to be, involved in all decisions concerning the details of this publication.

3.2 Punctuality and Revisions

The punctuality of data transmissions from Member States has not improved since the previous report delivered in 2011. For a variety of reasons, some Member States have failed to deliver the LCI in time (70 days after the reference quarter) for some of the quarters. Punctuality is of the utmost importance, since delays in data delivery mean that estimates have to be used for European Union and euro-area aggregates. This can result in unnecessarily large revisions afterwards. Figure 1 shows the available data (as a share of EU total labour cost levels in euro) for each quarter at the time of the press release.

Figure 1: Available LCI data at time of release, % of EU total labour cost level in euro

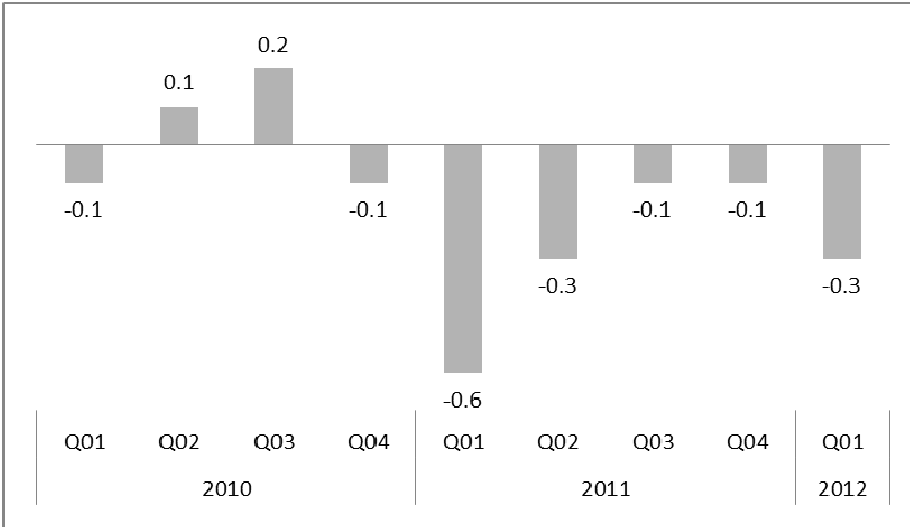


⁷ COM(2002) 661, Communication of the Commission to the European Parliament and the Council on Eurozone Statistics.

Some Member States (Germany, Luxembourg, Malta, Poland and the UK) sent their data late once between the reference quarters 2010Q3 and 2012Q2. At the time of writing this report none of these Member States had a structural problem with producing and delivering the LCI figures on time. Both Belgium and Ireland did not send data on time twice during the relevant period, and Greece four times. While the issues preventing Ireland and Belgium from sending data on time have now been solved, Greece does seem to have a structural problem with producing and delivering LCI data on time.

Concerning revisions, it should be borne in mind that the LCI is made up of different variables (labour costs, hours worked), which may be taken from several sources. This means that revisions may occur at any time, affecting the last quarter, several quarters or whole years of data. Whenever data for the base year is concerned, the whole series has to be revised. Revisions of the EU-27 headline figure (year-on-year growth rate) have exceeded 0.3 percentage points three times since the first quarter of 2011. In all three cases, the revision can be traced back to the amount of data available at the time of the press release. Another issue is the possible upwards bias of first releases compared to later transmissions (see figure 2). Eurostat is currently investigating this issue in detail, making use of longer time-series.

Figure 2: Revision between reference quarter and 2012Q2 of EU-27 NACE Rev. 2 B_N aggregate in percentage points



3.3 Comparability — Working day adjustment

Article 1 of Commission Regulation (EC) No 1216/2003 states that LCI figures have to be transmitted in non-seasonally adjusted (NSA), working-day adjusted (WDA) and working-day and seasonally adjusted (SA) form. There are some exceptions, as some Member States have derogations on the delivery of NSA data and some Member States can only provide series which are too short for seasonal adjustment for NACE Rev. 2 sections O to S. This Regulation does not explicitly state whether working day/seasonal adjustments have to be made using the direct or the indirect approach. Indirect adjustment implies that the adjustment is made only on the basic series, which are then used to construct higher-level aggregates. Direct adjustment implies that every single series, including higher-level aggregates, are adjusted individually. Both approaches have their advantages and drawbacks, and both are supported by the European Statistical System (ESS) handbook on seasonal adjustment. Member States employ either approach when adjusting the LCI.

Usually, both approaches produce similar results, and no problems arise due to the choice of one or the other. However, if the identification of a correct model for adjustment is difficult in view of the volatility of the raw data, problems may occur, generally when using the direct approach. For instance, it might happen that the adjusted index of the total cost component is either higher or lower than the adjusted index of all its sub-components. Therefore, Eurostat has systematically checked the data delivered by all Member States for coherence of the total index and its sub-components by NACE section.

In one case only, the discrepancies were found to be so large that Eurostat did not publish the working-day adjusted data for the relevant periods. Instead, the year-on-year growth rate which was published had to be calculated on the basis of non-seasonally adjusted data. The discrepancies had arisen in this case because the working-day adjustment had been applied to a series which did not in fact exhibit significant working-day effects.

To avoid similar cases in the future, Eurostat has communicated to the Member States concerned that adjustments should only be made if working day effects are statistically significant.

3.4 Coherence with national accounts figures

In the annual quality report, Member States are asked to compare the growth rates of the LCI with those of hourly compensation of employees in national accounts (ESA95 definition). Full coherence cannot be expected. Even if almost identical definitions of labour cost are used, statistical treatments and sources differ. Furthermore, the collection of hours-worked data is particularly difficult in both domains. Despite these differences, the degree of coherence (or lack thereof) between the two data collections can be used to identify potential problems in either collection. Not all Member States produce quarterly data for compensation of employees or quarterly hours worked in national accounts. An overview of coherence is therefore not possible for Greece, Malta, Luxembourg, Portugal or the United Kingdom. Latvian data is available, but cannot be used for the purpose of this exercise due to a break in the compensation of employees series in 2011.

For this quality report, Eurostat compared the non-seasonally adjusted NACE Rev. 2 section B to N aggregates. For at least one quarter, data from Estonia, Ireland, Spain, Hungary, Poland, Romania and Slovenia exhibited large discrepancies and diverging signs in the growth rates of the LCI and the growth rate of hourly compensation of employees derived from national accounts. Moreover, Bulgaria, the Czech Republic and Sweden showed relatively large discrepancies in the growth rates of the LCI and compensation of employees per hour.

Eurostat has been analysing in detail the coherence of the LCI with National Accounts data and the Labour Cost Survey and will continue to do so. The results of the analysis are discussed with Member States so as to identify and address underlying problems, in particular with respect to hours worked, with a view to improving coherence across the different statistical domains.

3.5 Completeness

Sweden and Finland now also deliver seasonally adjusted data. Now that seasonally adjusted data for all Member States is available, it becomes feasible to publish quarter-on-quarter growth rates not only in Eurostat's online database but also in the quarterly press release. Careful analysis of data quality and user needs will however precede such a step.

In September 2012, Eurostat released for the first time EU and EA aggregates including NACE Rev. 2 sections O to S. These NACE sections encompass public administration and defence, compulsory social security, education, human health and social work activities, arts, entertainment and recreation, and other service activities. NACE Rev. 2 O to S data for the EU and EA aggregates is available from 2008 onwards. They make up about 30% of the NACE Rev. 2 B to S aggregate for the EU-27, and complement the data available so far with important information. Users have been particularly interested in information about the evolution of labour cost in the public sector, mainly covered by NACE Rev. 2 section O (public administration and defence).

The quarterly news release has been adapted to show the NACE Rev. 2 B to S aggregate now as the headline indicator, while still showing full information on the previously used NACE Rev. 2 B to N aggregate. In addition, figures for the NACE Rev. 2 O to S aggregate are published in the press release.

4. CONCLUSIONS

Overall, the quality of the LCI has continued to increase since the previous report in 2010; the improvements in relevance and completeness are particularly noteworthy. Moreover, the full availability of aggregates (including the NACE Rev. 2 sections O to S) has added to the overall usefulness of the LCI. The publication of yearly estimates of labour-cost levels based on the LCI provides users with significant new added value. The punctual delivery of data by Member States is still not fully satisfactory, although no country except for Greece was systematically late. Member States will have to continue channelling resources into measures to achieve punctual data transmissions.

In recent years, the Commission (Eurostat) has regularly urged Member States to step up their efforts. On the basis of the data delivered and other national documentation, including quality reports, the Commission will continue the regular monitoring of the remaining non-compliance and quality issues. Where the desired improvements are not taking place as planned, the relevant national authorities will be approached and the Commission will take the necessary measures to enforce compliance.