Abstract
In this paper, we estimate fundamental bilateral real exchange rates for a group of eight accession countries using a panel-cointegration approach for the period 1993-2003. We document a significant positive link between productivity levels and the corresponding real exchange rate levels. Future rises in productivity cannot be excluded on the basis of either our own analysis or the literature as a whole. Consequently, inflation pressure and real exchange rate appreciation in the accession countries probably remain a fact of life in the near future. The extent to which this is a problem for a fixed nominal exchange rate regime is hard to determine. Price dynamics in the accession countries are still quite flexible to accommodate substantial real exchange rate movements even when the nominal exchange rate is rather fixed; moreover, that price adjustment is mostly an internal process for the accession countries. Overall we conclude that a fixed exchange rate regime for each of the accession countries would be feasible in itself, despite possible future real exchange rate appreciations due to either the Balassa-Samuelson effect or demand shifts. We find current misalignments to be small, robust and generally in line with the literature. This implies current exchange rate levels provide a reasonable indication of the level at which a parity exchange rate could be set.