The Economist

The Big Mac index

Value meal

Our lighthearted guide to currencies takes a closer look at the euro area

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THE prospect of an end to asset purchases by the Federal Reserve has caused gyrations in foreign-exchange markets. As emerging-market currencies slide and bullish bets on the dollar grow, it is time to read between the buns.

The Big Mac index is *The Economist*'s exchange-rate gauge. It is based on the theory of purchasing-power parity (PPP), which says that in the long run exchange rates should adjust so that the price of an identical basket of goods and services is the same across borders. Our basket contains a single good: the Big Mac, which uses the same ingredients almost everywhere (India's Maharaja Mac, which contains chicken, not beef, is an exception). Since buying a burger in Norway costs $7.48 at market exchange rates, compared with an average price of $4.56 in America, the Norwegian krone is 65% overvalued on our measure.

Other currencies look very undercooked. The greenback buys two and a half times more burger in South Africa than in America, and three times as much in India. Comparing emerging-market prices with rich-world ones is problematic, however, because labour costs are lower in poorer countries. The Chinese yuan is 43% undervalued on our basic gauge; adjusted for GDP per person, it is only 4% below fair value.

The euro is 2% overvalued on our burger index. This number is based on a synthetic Big Mac price, weighted by the GDP of euro-zone members. In reality, the price of a burger varies across the euro area, ranging from €2.60 to €4.10 ($3.34 to $5.27). The most expensive burgers are found in Finland: the "Finnish euro" is 16% overvalued. French gripes that a strong euro is hurting exports are borne out by burgernomics. The euro also looks too strong for Italy.

Track global exchange rates over time with our interactive Big Mac index (http://www.economist.com/bigmac)

Some of the cheapest burgers in the euro area can be found in Greece and Portugal. Greece in particular has been regaining competitiveness the hard way: unit labour costs fell by 6% in 2012 and wages in the first quarter of this year were 10% lower than a year earlier. Two years ago the index indicated that the “Greek euro” was 15% overvalued (the euro as a whole was too strong by 21%). Since then the price of a Big Mac in Greece has dropped by 20%, twice as much as the next-largest fall, in Ireland. The Greek euro is now 27% undervalued.

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