

COUNTER-INFLATIONARY POLICIES: A TENTATIVE APPRAISAL OF EUROPEAN EXPERIENCES

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Overview

Commonalities and differences of the recent resurgence of inflation across Europe

The response at European level

National policy packages

Policy trade-offs – the 4 Ts

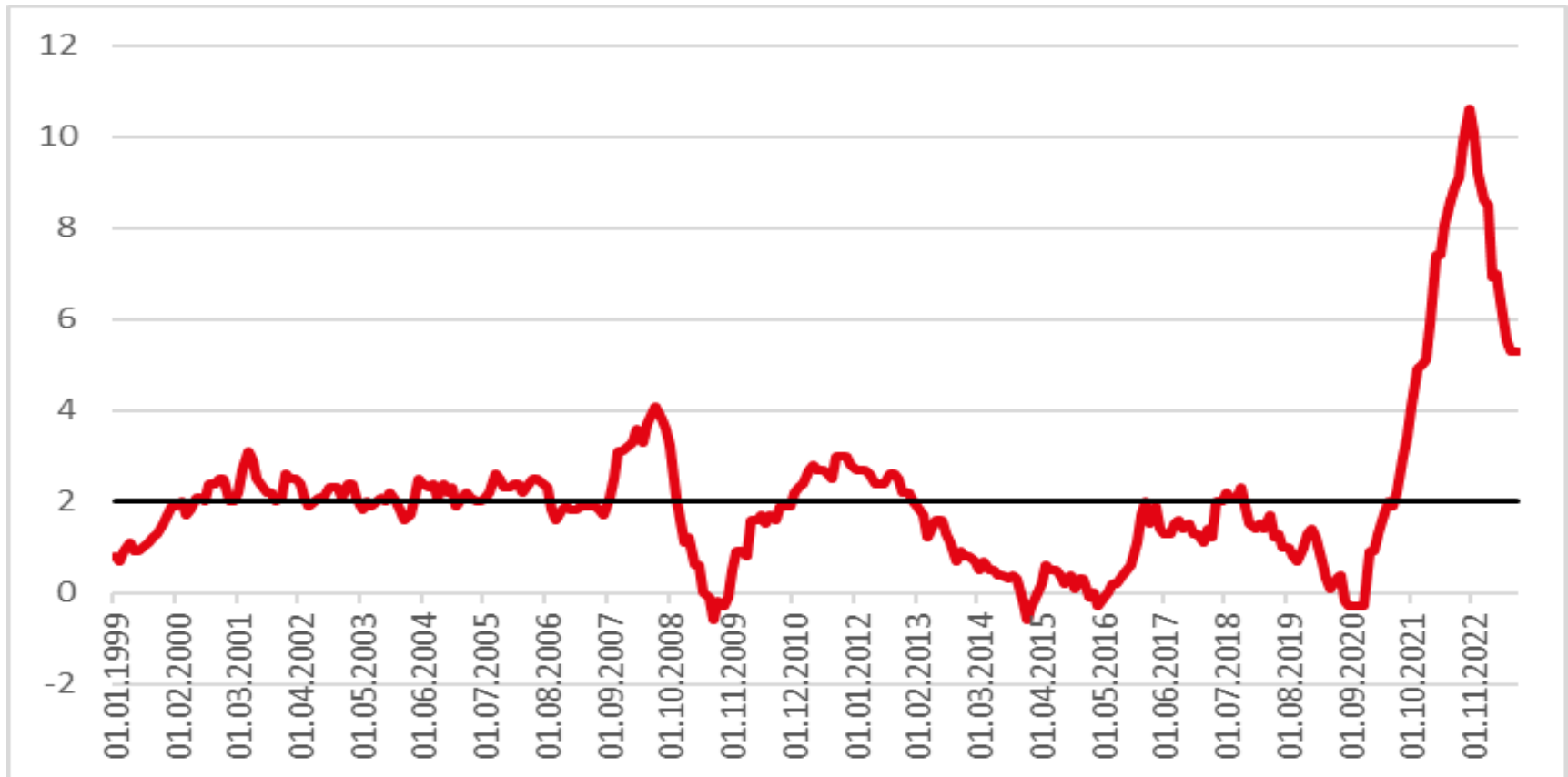
Provisional findings on policy effectiveness and trade-offs (distributional, ecological)

Draws on national case studies in a comparative project led by IMK and Arbeiterkammer Vienna (Nov 2022) and provisional findings October 2023:

Austria, Croatia, France, Germany, Greece, Hungary, Italy, Netherlands, Poland, Spain

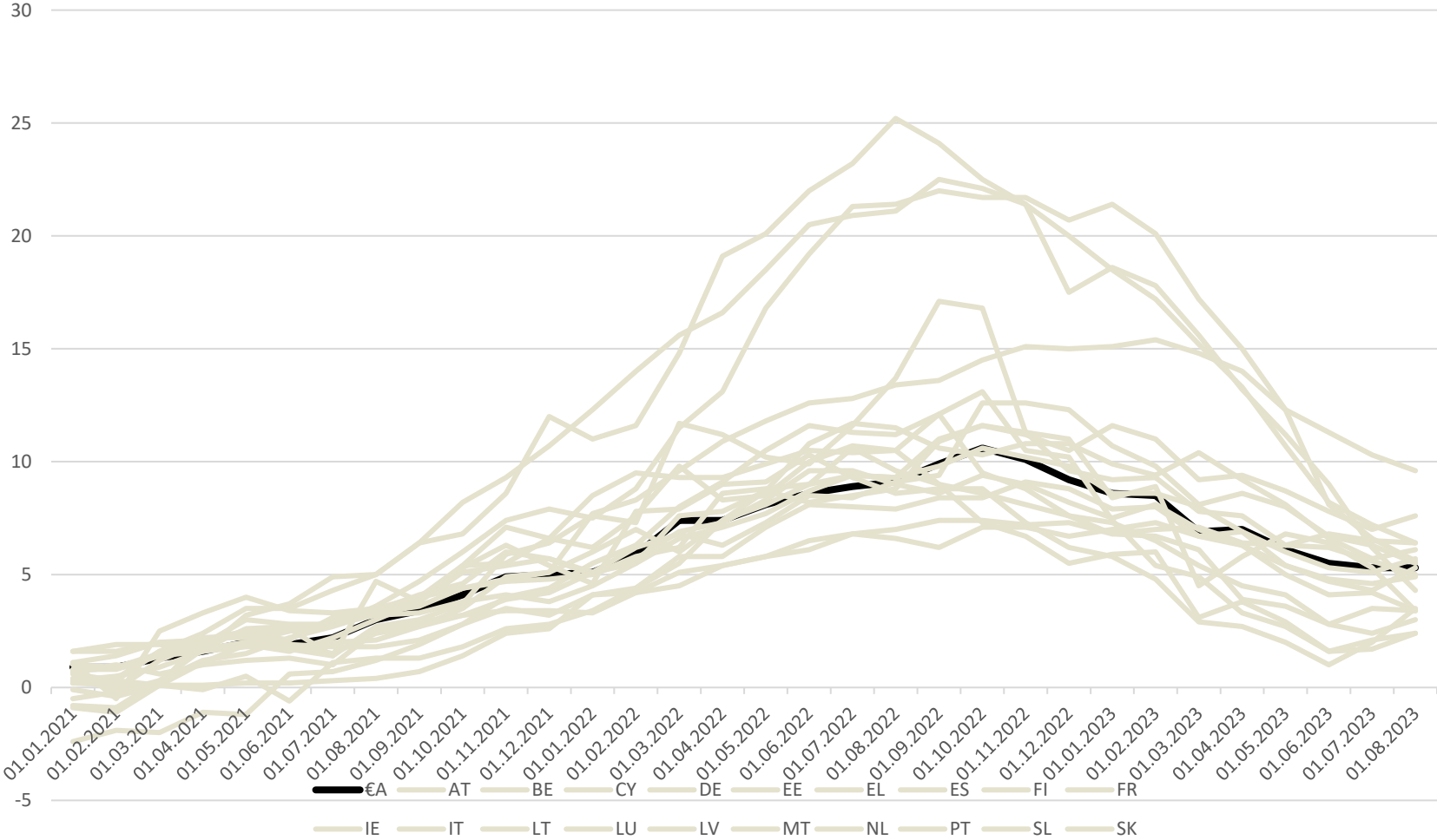
Out of the bottle

€A HICP m/m-12



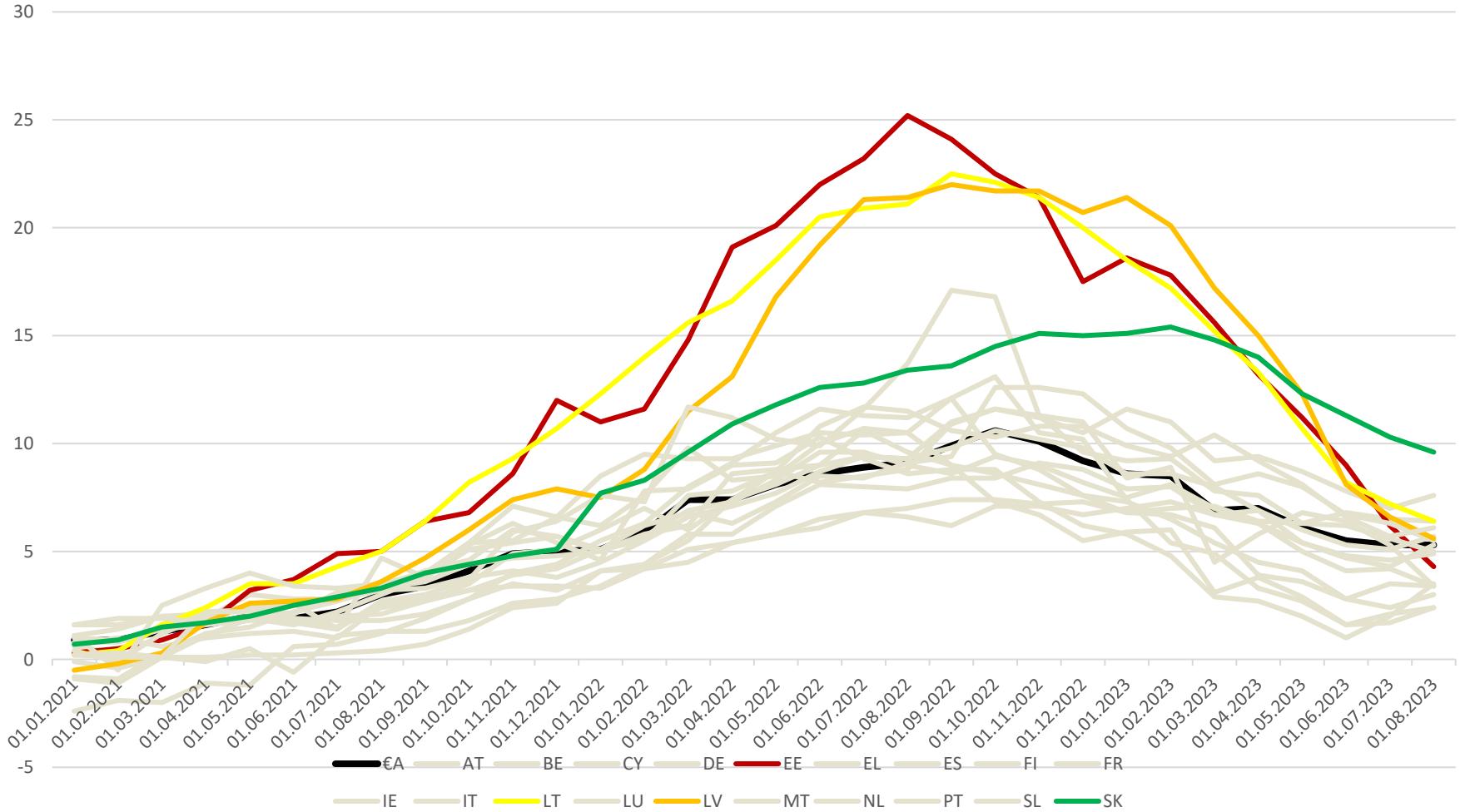
Mind the gap

€A MS HICP m/m-12



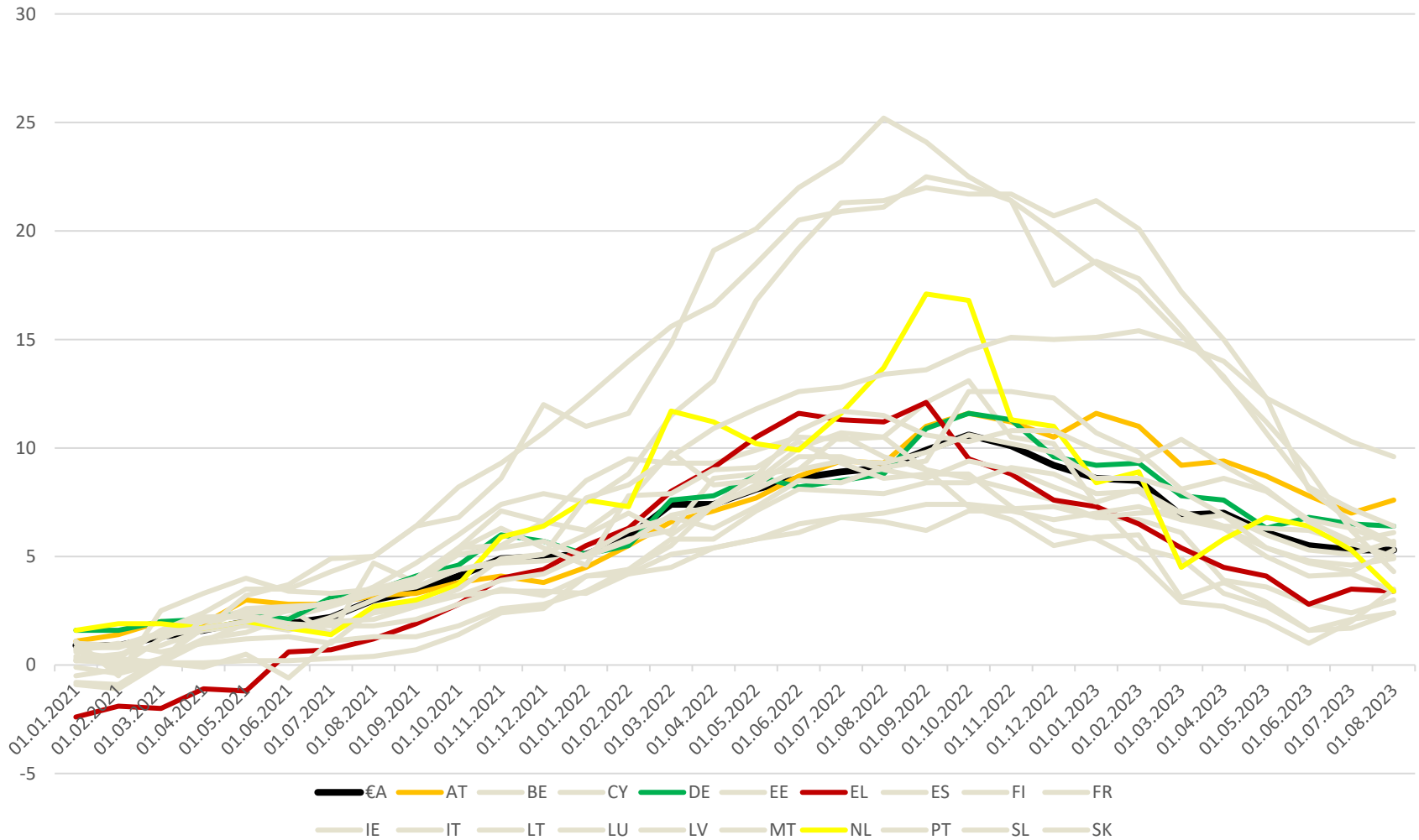
Baltic high

Selected €A MS HICP m/m-12



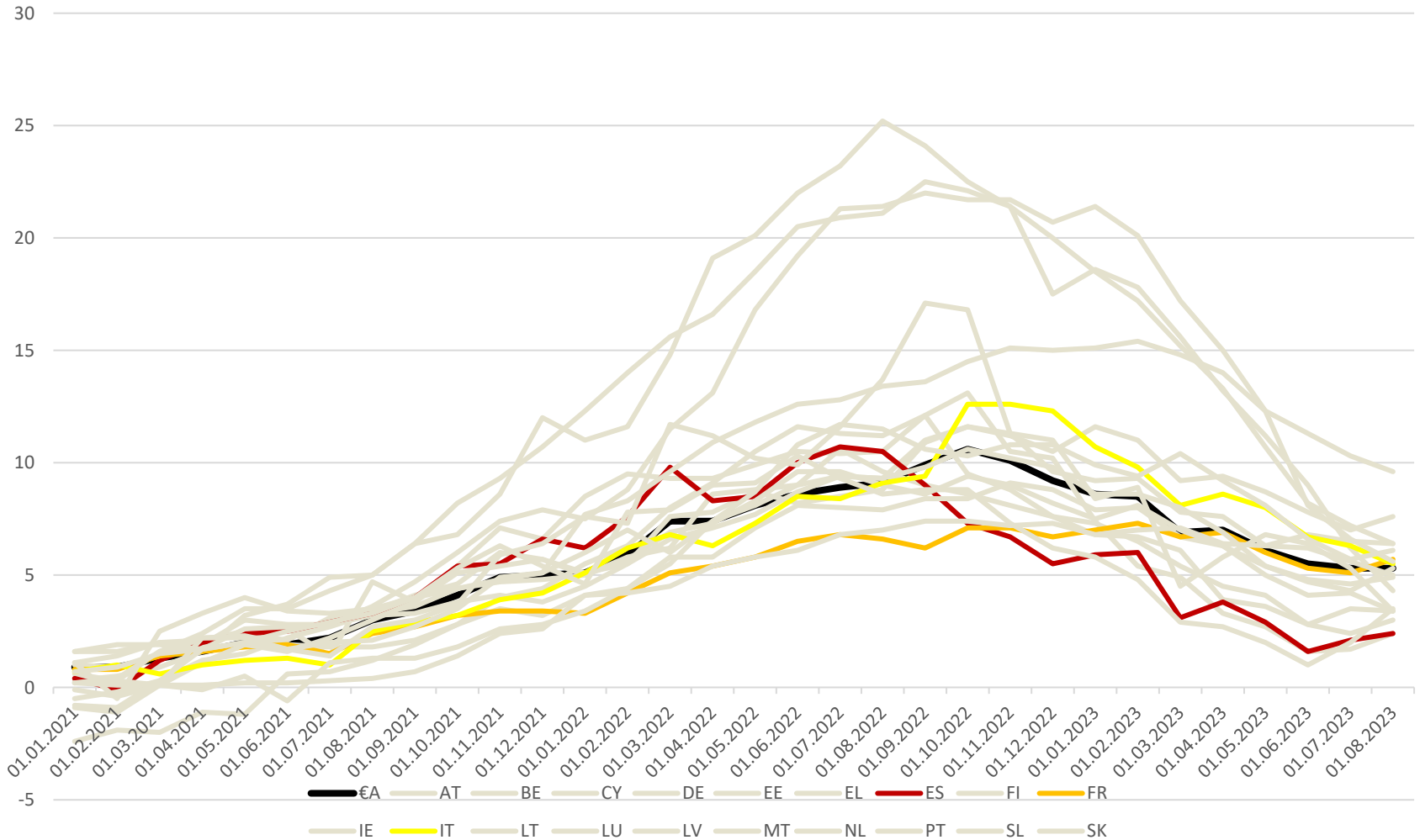
Policy sustainability?

AT EL DE NL HICP m/m-12



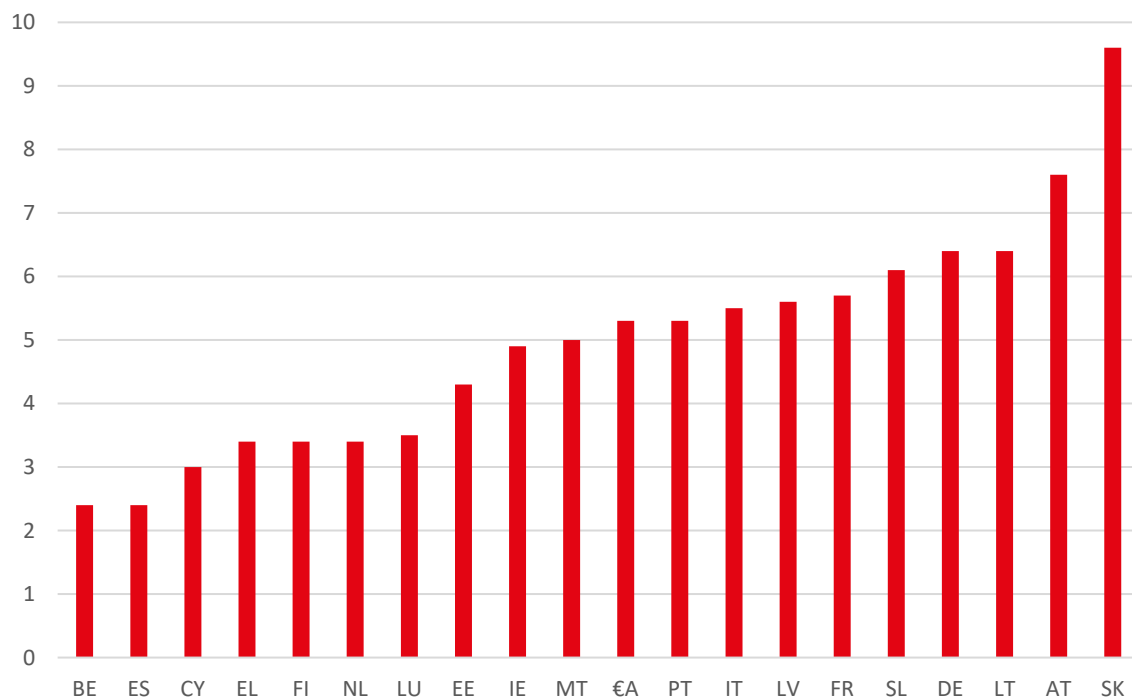
Policy sustainability?

IT ES FR HICP m/m-12



Inflation differentials

HICP Aug 2023 m/m-12



In a currency area
sustained inflation
differentials are
unsustainable

Real exchange rate will
force adjustment

Renewed danger for
currency area?

4 types of drivers of outcomes

Different cyclical dynamic when the shock hit

- E.g. some CEE MS

Different exposure to import-price shocks

Measurement issues (NL)

Success of national policy and institutions in limiting price rises

- What was deployed?
- What can be sustained economically?
- What about the trade-offs with social and environmental objectives?

EU level preconditions building on covid response

Suspension of fiscal rules since March 2020 (covid) extended in May 2022

Similarly state aid rules had been liberalised and this was extended and expanded

Under the title RePowerEU the European authorities sought to promote energy saving, recover part of windfall profits, build storage capacity, and expand and repurpose grants and loans under the Recovery and Resilience Facility

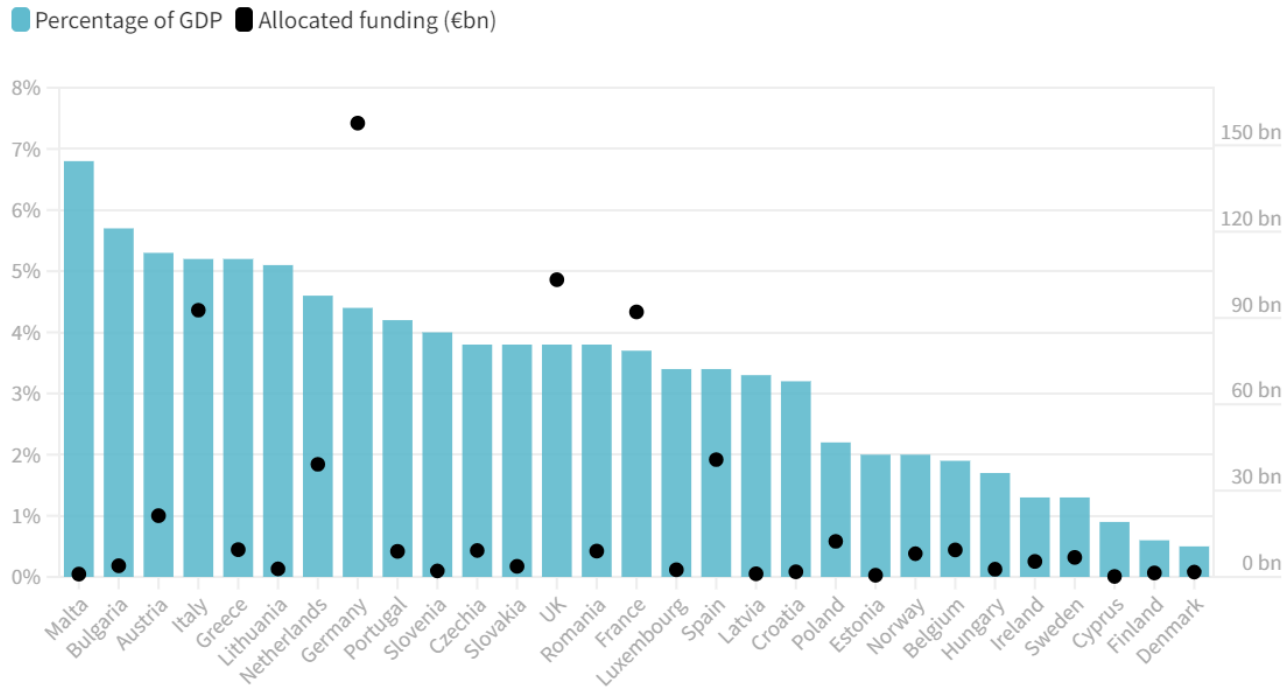
Overview of measures in 10 EU MS (provisional)

	Austria	Croatia	France	Germany	Greece	Hungary	Italy	Netherlands	Poland	Spain
Energy tax cut	✓	✓	✓	✓	✓		✓	✓	✓	✓
Gasoline tax cut			✓	✓	✓		✓	✓	✓	✓
VAT tax cut	✓	✓		✓	✓		✓	✓	✓	✓
Retail price control	✓	✓	✓	✓		✓	✓	✓	✓	✓
Wholesale price control			✓	(✓)		✓			✓	✓
State-owned company mandate		✓	✓		✓				✓	
Windfall profits tax	✓	✓		(✓)	(✓)	✓	✓	✓	✓	✓
Transfers to (vulnerable) households	✓	✓	✓	✓	✓		✓	✓	✓	✓
Transfers to (vulnerable) firms	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Bi- or tripartite agreement social pact				?						✓

- No hayekians in a foxhole
- Most MS: broad mix of income support, (indirect) tax cuts, price caps (with govt support to producers), some creaming off of windfall profits,
 - Address trade-offs, respond to political constituencies
 - But intensity varies greatly
- Very limited attempts at tripartite „incomes policies“ measures.

Cost/impact – orders of magnitude

(Bruegel, IMK/AK nat reports)



	Croatia	France	Greece	Germany	Italy	NL	Poland	Spain
2022	5,6	1,4	4,9	1,4	2.8%	1,0	3,5	1,5
2023	5,0	1,2	1,4*	2,1		1,5	3,4-4,1	
			* to May					

Reasons to be cautious about estimates

Classification of counter-inflation measures can vary

Allocations in the budget do not equal actual spending and can change depending on take-up and market-price-developments (energy price caps)

Not always clear what counterfactual is (e.g. with increases in tax allowances)

Timing of announced measures/actual spending unclear/different

National policies face unpleasant trade-offs

Timely – Targeted – Temporary - Transformative

Examples:

Ease burden on the socially needy vs ease burden on affected industries

Shielding HHs/businesses vs need to incentivise energy saving (not distort price signal with subsidies)

Targeting measures to the needy versus timely measures that are simple and cheap to administer

Allowing/encouraging nominal wages to follow inflation (risk: inflation entrenchment), do not (real wage losses, demand shortfall)

Subsidies for energy saving/efficiency only have longer-term benefits

Distributional concerns and trade-offs

Clear case for targeting: higher inflation incidence, less adjustment capacity for low-incomes, greater stabilisation effect

But high heterogeneity within income deciles (car ownership, rural/urban)

Price reductions/caps for energy/food benefit on average poor relatively more, but absolutely less than wealthy (e.g. vehicle fuel also relatively)

IMK study of all measures (including min wage hikes) against HH types suggested real income losses of around 2.5% for most middle income groups. These were considerably lower for some low-income groups and for high-income families with limited inflation exposure.

Overall, price measures were overwhelmingly “untargeted”, income support measures much more so.

Targeting measures is administratively difficult, e.g. in Germany no cap on benefits from gas price brake from which wealthy likely to benefit substantially

Ecological concerns and trade-offs

Environmentally friendly policies tend to be counter-inflationary and pro-social only in the longer run (e.g. insulation of housing); the short-run social and income stabilisation effects are small.

Moreover, some tend to be claimed disproportionately by wealthy households (electric vehicles photovoltaic)

Poland and Greece are cited as countries with rather large subsidy/price cap programme that are maybe effective but not efficient, devoting scarce resources to households that could stabilise consumption by private means while reducing incentives to save energy.

At the same time, price caps” can be well designed to avoid creating perverse environmental incentives by relating household subsidies to the pervious year’s consumption so the marginal price remains high (DE, NL).

Tentative conclusions

MS have deployed a wide range of measures, despite fiscal constraints), helped by suspensions of EU rules & EU support.

Neither in distributional nor ecological terms have they been well-targeted in many countries and may prove unsustainable in some.

Strategic price reduction measures by governments have proven effective in supporting demand & reducing headline inflation, which lowers risk of 2nd round effects (“Iberian exception”)

Policies need to be well designed to avoid subsidising fossil fuel consumption and deadweight effects. But difficult trade-offs between “optimal” policy and implementation constraints.

Wage bargainers in a quandary. Pressure for wage compensation with risks. Tax-free one-off payments? (DE vs AT)

Tripartite solutions likely to be lower-cost/more effective, but limited signs.

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