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The global struggle against inflation

Do energy shields, taxing windfall profits, or price caps protect people effectively from inflation? We report from Latvia, France, and Tanzania

Latvia

Latvia is making headlines. On the foreign policy front because the country, like the neighbouring states of Estonia and Lithuania, is seen as a possible next target of attack for the Russian Federation. But also in terms of domestic and economic policy, because in July, at 21.5 per cent, it had the highest inflation rate since the 1990s – that is at the beginning of its transformation from a planned to a market economy.

Broken supply chains are one reason for the high inflation, but also the Russian war of aggression against Ukraine. The rising energy prices are a powerful factor here. Although Latvia's dependence on Russian gas is to end on 1 January 2023 with an import ban, finding alternatives is, as in Germany, not easy.

It is also unclear whether enough gas is on hand and stored, at least for the foreseeable future. At a press conference, Prime Minister Krisjanis Karins expressed his conviction that it is. However, the responsible company Latvijas Gaze, in which Russian energy company Gazprom (34 per cent) and Uniper Ruhrgas (18.26 per cent) also hold shares, is not ready to confirm his statement.

Even if Latvians have been confronted with the consequences of high inflation several times in recent history, not only during the transformation in the 1990s, but also during the 2008/2009 financial crisis, the effects are once again very painful. Because everyone is hit when heating, food, housing, and transport costs skyrocket.

All these items represent a large share of the household budget of the average Latvian citizen, more than in other countries. Heating costs in particular will rise dramatically in a country where, in addition to the

cold winters, the in-between seasons tend to be rather cool. Instead of €170, a friend suddenly faces a €614 bill for heating costs.

The prices of groceries like dairy products, bread, coffee, sugar, and meat (beef) have also risen by at least a third. No wonder that a recent survey gave €1,646 as the desired average income, 12 per cent more than in the previous year. Ten years ago it had been just a little over half that amount.

The state has understood that it has to intervene. In the case of heating costs, it will partially compensate high prices. For the elderly, pensioners, and the disabled, the government has announced that it will provide inflation compensation. Is that enough? Financial expert Andris Suvajevs is sceptical: 'Many households will not be able to bear this, and there will be enormous pressure on municipal social service providers to share the costs.'

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But government agencies are not inclined to be generous with social benefits. Latvia prides itself on a low national debt of just some 43 per cent of gross domestic product. By comparison: in Germany the equivalent figure is 68 per cent, in Italy 152 per cent. This is generally understood as a safety valve against serious crises and is consistent with a very high level of scepticism towards too much state intervention, which is certainly an ongoing consequence of the turning away from state management in the days when the country was a constituent republic of the Soviet Union.

The national parliament will be re-elected on 1 October. At the moment, at least ten parties are being given a good chance of clearing the five per cent hurdle. The coalition negotiations will again be difficult. But with the cold season is approaching there will not be much time. In addition to private households, hospitals have also reported the need for funding to be able to finance the rising costs. Nor can a new variant of the corona virus be ruled out in Latvia.

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France

After a long phase with annual price increases of little more than 1 per cent, inflation has been visibly gathering pace in France since 2021. With the beginning of the war in Ukraine, it continued to pick up speed. In July, the inflation rate reached 6.1 per cent, its highest level since 1985, and the French statistical office expects a further increase to 6.5 to 7 per cent by the end of the year. These are numbers that evoke memories of the 1970s.

But economists point out that the current inflation dynamic differs from the 'classic' case of parallel increases in the prices of all goods and wages. At the moment this is primarily an 'imported inflation', affecting only the prices of certain goods, above all energy — electricity prices rose sixfold in the first half of the year — and food. So far, the development of wages and salaries has not been able to follow this increase. Given the rapidly increasing energy prices, the French government had already in autumn announced the *bouclier énergétique* (energy shield), a package of measures intended to cushion the inflation shock for households.

The price of gas was 'frozen' and the increase in electricity prices capped at 4 per cent until the end of 2022. Needy households with annual incomes of up to €10,000 also received a one-time credit, a *chèque énergie*, of up to €277 for their electricity and gas bills. And households that heat with heating oil should also receive relief in winter. €230 million in aid has made available for this purpose. In order to slow down the price spiral at the petrol pumps, a price reduction of 30 cents per litre of fuel (from November only 10 cents) is being granted. The economic research institute OFCE estimates that these measures have curbed the rise in inflation by around 2 per cent.

Nevertheless, this 'protective shield' for energy prices is not undisputed. While it has so far been able to contain inflation in France compared to its neighbours, critics argue that the measures ought to be targeted more at vulnerable groups. In addition, the measures to date are emblematic of the tension that exists between the short-term goal of maintaining purchasing power and the medium- and long-term goal of energy saving and energy transition. Up to now, flanking measures to stimulate energy saving have been lacking in France — even if a social debate about moderating consumption is slowly developing.

Already the dominant issue in the presidential and parliamentary elections in the spring, purchasing power is now also causing lively and controversial debates in the newly composed National Assembly, where after the elections the government camp no longer holds an absolute

majority. Prime Minister Elisabeth Borne therefore had to negotiate hard with the opposition to find a compromise that would win a majority for the proposed legislation to protect purchasing power that she introduced shortly before the summer break. In the process, diametrically opposed concepts for maintaining purchasing power collided. The Macronists are focusing primarily on the extension and expansion of the *bouclier énergétique.* This is intended, not least, to ensure popular acceptance of the sanctions against Russia, as Marine Le Pen has already publicly called on President Macron to lift them as being ineffective and, above all, harming their own people.

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In addition, the aid package to preserve purchasing power, pushed through by the governing parties with the support of the conservative Republicans, contains moderate adjustments to social benefits and pensions that are below the inflation rate. The same applies to the index used to calculate public sector wages, which rose by 3.5 per cent. The package also provides for an expansion of the 'Macron premium' introduced after the yellow vest protests. This enables companies to pay employees a bonus of up to €6,000. Since no social security contributions or taxes are levied on this bonus, critics argue that it is an incentive for companies to avoid wage increases. At the urging of the Republicans, the possibility was also created for companies to 'buy back' part of the working time reduction from their employees in certain cases. France has a 35-hour week. The left-wing opposition sees the 'buyback option' as an attack on this achievement from the Jospin era, facing many workers with the choice of either improving their income or taking the rest they deserve.

For this reason the left-wing parliamentary opposition is accusing the government camp of doing everything it can to avoid general wage and salary adjustments for securing purchasing power. In response, it is pleading above all for an increase in the minimum wage beyond the inflation adjustment and for the convening of a 'wage conference'. Another point of contrast to the government camp was its call for a tax on windfall profits. In view of the situation-related high profits in some economic sectors, socialists and communists called for a special tax of 25 per cent for companies in the energy and transport sectors, which had

recently generated profits well above the magnitude of previous years.

The income from this special tax would then be used to finance a permanent reduction in VAT on fuel. In response to this debate, TotalEnergies has announced its intention to reduce the petrol price at its own gas stations by 20 cents in addition to the state-financed price reduction. It had previously become known that the company was able to triple its profits to €18.8 billion in the first half of the year. Other energy companies have now followed suit and announced that they want to lighten the burden on their customers.

With reference to such 'voluntary' transfers of profits, the conservative parliamentary majority initially rejected the demand for taxation of windfall profits. But after the summer break, the topic will definitely be back on the agenda. Overall, the debate on protecting purchasing power in the newly elected National Assembly shows a clear ideological convergence between the Macronists and the Republicans. So far, however, the government camp has not made any concessions towards the left-wing opposition and their proposals, and this also seems unlikely in the near future.

Thomas Manz, FES Paris

Tanzania

At the beginning of the year, the central bank had already warned that the rebound in oil prices after the Covid-19 crash and, above all, the delayed seasonal rains could fuel inflation. The ongoing disruptions in container shipping and global supply chains had pushed up transport costs and consumer prices even before the Russian war of aggression. A major daily newspaper attributed part of the rise in food prices to either profiteering or panic buying. Because even sardines are now being sold for a price that has 'never before' had to be paid. The only explanation for the fact that bananas are now twice as expensive is that traders are profiting from confusion.

While the global debate seems to revolve around wheat, Tanzania's consumption of wheat ranks fourth behind maize, cassava, and rice. The social importance of maize in Tanzania should not be underestimated: a meal is inconceivable without the beloved *Ugali* corn porridge. According to newspaper reports, the price of maize in June was 78 per cent higher than a year earlier. The main products of the wheat industry in Tanzania are noodles and bread. 80 per cent of the wheat, imported mainly from Russia, is consumed in cities and it can be assumed that it is more likely to be the wealthy and the middle class who buy such

products. Also crucial for many poor families is the fact that even the price of rice recently rose by 38 per cent compared to the year before.

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In order to cushion the social burden, the government under President Samia Suluhu Hassan is subsidising petrol prices, using bulk state procurement to control prices on the fuel market and is considering a price stabilisation fund. The increase in fuel prices is described as 'reasonably acceptable', with the price increase of nonetheless 33 per cent affecting bus fares in particular. In May, bus fares in Dar es Salaam rose by 100 Tanzanian shillings, the equivalent of 4 cents. This increase is simply not affordable for many commuters, as testified by people walking several kilometres to work. The bus company association is already complaining to the traffic supervisory authority that the adjustment is too small in view of the sharp rise in fuel prices.

Solving the problems of energy supply — specifically the frequent unavailability of electricity unless you have a diesel generator — has always been one of the most urgent tasks in the country, especially in the dynamically growing cities. Tanzania's electricity consumption in 2019 was 2.61 billion kilowatt hours. By comparison: the world average was 125.19 billion kilowatt hours. A hydroelectric dam is being built to generate energy for the greater Dar es Salaam area — forecast to be one of the world's 20 largest cities in 2050. However, drought and dwindling water reserves have already led to water rationing here last year.

The natural gas deposits in the southern region of Lindi are the source of infinite hopes. Now that liquefied natural gas is attracting a lot of attention worldwide, everyone is all the more keen to benefit from the boom. The government continues to seek investment in the energy sector. The new president, in office since 2021, has opened up the country to international partners, which has produced a change in the investment climate on the one hand and financing commitments such as IMF loans on the other. Whether she will actually be able, with the numerous loans, to create the much-needed fiscal policy leeway for investments and social spending, and to cushion the long-term effects of the pandemic and the Russian war of aggression, is now becoming a test case for her economic policy.

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