

INFLATION – WHAT DRIVES IT AND PROPOSED MEASURES

Inflation measured through the cost of living in the first half of 2025 was 3.84%, and the upward trend continued in July when inflation was 4.8%.

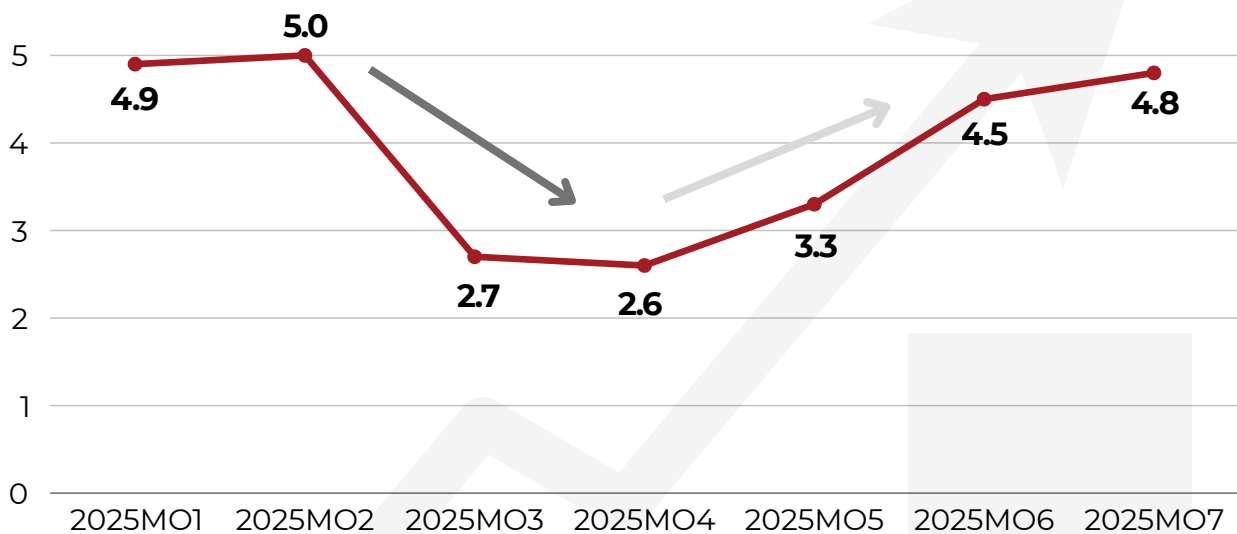


Chart 1: Inflation measured through the cost of living, annual rate of change

Source: SSO

Chart 1 shows two periods of inflation movement. During 2025, the period of decreasing the rate of growth of the cost of living starting from February and ending in April 2025, followed by the period from May to July 2025 with a renewed increase in inflation. In fact, the first period is when the Government intervened in the market by limiting the profit margin for a large number of products, while the second period is without actively applied measures by the Government.

From the data shown it is clear that the Government's measures had an effect and contributed to reducing the inflation rate, but with a limited short-term effect only during the period of application of the measures. Immediately after the end of the Government's measures, the inflation rate returns to the same level as in the previous months.

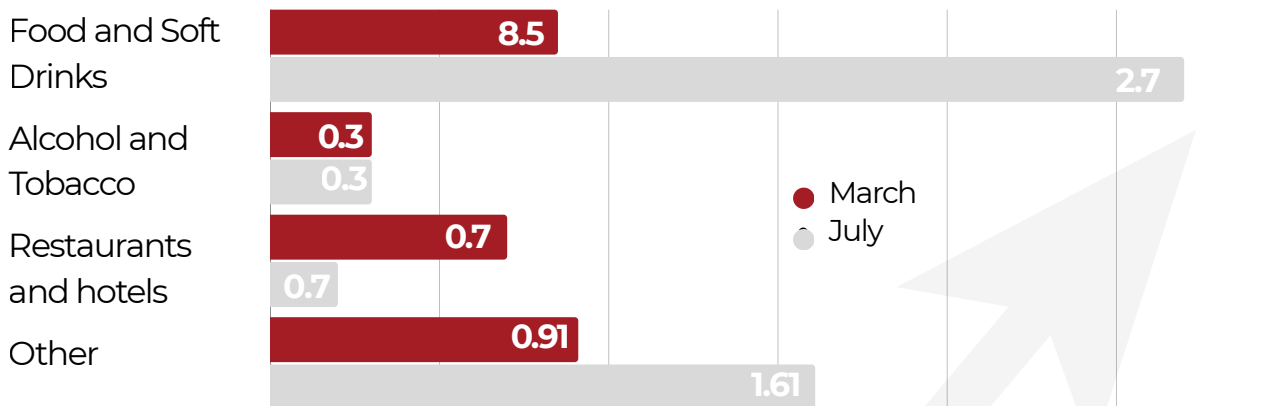


Chart 2 : Contribution to inflation in March vs July 2025

Source: SSO

The data in Chart 2 shows what drove inflation in March 2025 when government measures were in effect and in July 2025 when there was no government intervention.

According to the data, in March 2025, inflation was driven mostly by services, and only 31.5 % by food and non-alcoholic beverages. In July 2025, when there were no active measures by the Government to reduce inflation, the cost of living was driven mostly by food and non-alcoholic beverages (56%) , and less by services.

All of this points to several conclusions:

- The Government's measures for reduction of inflation in March and April 2025 yielded results.
- State intervention has short-term effects, meaning that government measures only produce results while they are in force. A correction in the inflation rate or a return to trend occurs soon after the measures are lifted.
- Conversations with companies and business associations indicate dissatisfaction among enterprises with the introduced measures to limit product prices and margins.

Proposal for short-term measures to deal with inflation – Protocol for action:

Just as the National Bank has established a system for monitoring inflation and taking appropriate measures (most often to tighten or loosen monetary policy through interest rates), it is also necessary for the Ministry of Finance to establish a system/protocol for dealing with rising inflation .

- 1.A body should be established (similar to the Council of the National Bank) within the Ministry of Finance (this could be the Department for Macroeconomic Policy), which will regularly review inflation developments. Alternatively, the Fiscal Council could be assigned this task, or, as in 2008, a Committee for Coordination of Monetary and Fiscal Policy could simply be formed.
- 2.The body should include a representative from the Ministry of Finance, the National Bank, the Government, as well as a representative from academia and the non-governmental sector.
- 3.Government and monetary authority interventions should follow after a detailed diagnosis of the causes of inflation, meaning that the measures must be based on “evidence” of the main factors fueling inflation.
- 4.The body proposes measures to reduce inflation, in accordance with the conclusions of the analysis - that is, in accordance with the determined causes of high inflation, and with strong coordination of fiscal and monetary policy measures.
- 5.Introducing a rule to freeze prices and wages, however only in times of extreme conditions - inflation rate above 20%.

6. Rising food prices have the greatest negative impact on the living standards of low-income families, as they account for a large share of their total expenditure on food. Therefore, if inflation is mainly driven by rising food prices, intervention measures should provide (temporary) protection of their living standards, be targeted, and not general. For example, food vouchers could be provided to all recipients of a guaranteed minimum income.
7. Margin limitation should be applied in conditions when inflation exceeds 10% in the food and non-alcoholic beverages category, and other measures and policy instruments taken do not produce effects. This measure leads to market distortion, creates a significant net loss for society and therefore should not be a "standard" measure in the range of interventions. In addition, the cost of introducing this measure should be partially covered by the Government, i.e. the cost should be divided between the companies in the supply chain and the Government. The limitation of margins should last for a longer period, and the longest period should be the period of subsidizing margins by the Government.
8. Consistent application of the Law on Unfair Trade Practices. On the one hand, it is necessary to strengthen the inspection services, but on the other hand, education and dialogue between the concerned parties - manufacturers, importers, distributors and owners of retail chains - are also needed. The role of chambers of commerce is crucial in reducing the tensions that currently exist between participants in the supply chain.
9. Increase public sector wages in line with productivity growth.
10. Recommendations for other long-term measures - supply-side measures, i.e. stimulating domestic production. Of course, such measures will have the greatest contribution in the fight against inflation, but over a longer period of time.

Experiences from around the world

In Germany, there is a Council of Economic Experts (Sachverständigenrat), a five-member body that advises the German government on economic policy, including inflationary pressures, wages, and energy prices. Similarly, the Energy Prices Commission (2022) formed during the energy crisis proposed gas price caps and subsidies for households.

In France, there is a Council for Economic Analysis (Conseil d'Analyse Économique – CAE) that advises the Prime Minister through reports on inflation, food and wages. At the same time, in France there is also a Working Group on Price Negotiations that involves producers and traders to stabilize prices through voluntary agreements.

These bodies vary in structure - some are permanent councils, others are ad-hoc working groups - but all aim to offer balanced measures to stabilize prices, protect vulnerable categories, and maintain economic stability.