

TEXT

CAUSES AND CONSEQUENCES OF INFLATION



CAUSES

Inflation is the general increase in the price level of goods and services in an economy over a period of time. This reduces the purchasing power of money. Inflation can have several causes, which are often interrelated.

A major cause is **demand-side inflation**. This occurs when the total demand for goods and services increases faster than the supply. For example, consumers spend more due to higher wages, low interest rates, or optimism about the economy. Businesses cannot immediately keep up with the increased demand and therefore raise their prices.

There's also **cost-push inflation**. This causes production costs for companies to rise, for example, due to higher wages, more expensive raw materials, or rising energy prices. To maintain their profit margins, companies pass these higher costs on to consumers in the form of higher prices.

A third cause is **monetary inflation**, which is associated with an increase in the money supply in the economy. When there's a lot of money in circulation, while the production of goods and services doesn't grow proportionally, money loses value. This can be the result, for example, of loose monetary policy by central banks.

Finally, inflation can also be caused by **external factors**, such as wars, natural disasters, or disruptions in international supply chains. These events can lead to shortages of certain products, causing prices to rise.

INFLATION TYPES

Inflation can be classified in different ways, depending on its rate and characteristics.

Creeping inflation is a low and gradual inflation, usually around 1 to 2 percent per year. This form is often considered healthy because it stimulates economic growth without significantly eroding purchasing power.

Galloping inflation refers to a rapid and sharp rise in the price level, often with annual inflation rates of tens of percent. This form of inflation creates uncertainty and makes it difficult for consumers and businesses to make financial plans.

The most extreme form is **hyperinflation**. In this case, prices rise extremely rapidly, sometimes by hundreds or thousands of percent per year. Money then loses virtually its value, causing people to lose confidence in the currency and often switch to barter or foreign exchange.

Also sometimes referred to as imported inflation or **import inflation**. This occurs when prices rise because imported goods become more expensive, for example, due to a weaker national currency or rising global market prices.

CONSEQUENCES: two points of view

From a family's perspective:

The De Meester family lives in a terraced house just outside the city. Tom, the father, has worked as a secondary school teacher for fifteen years. His partner, Sofie, is an accountant at a medium-sized company. Together they have three children: Lisa, 14, Milan, 10, and Noor, 6. They lead a busy but well-organized family life—or at least they did, until inflation became increasingly noticeable in their daily choices.

Every month, Sofie starts by reviewing the family budget. This used to be a routine task, but lately she's noticed how the numbers are becoming less and less relevant. Groceries have become noticeably more expensive. Where she used to fill the shopping cart without a second thought, she now compares prices, chooses store brands more often, and simply leaves some items on the shelf. "It's only a euro more here, two euros there," she tells Tom, "but at the end of the month, it really adds up."

Tom is feeling the effects, too. His salary is indexed, but the increase always seems to come just too late and never quite enough. The energy bill worries him. In winter, they try to turn down the heating and put on extra sweaters. The children sometimes complain about the cold, but Tom and Sofie explain that energy costs money—more than before.

For the children, inflation is most visible in the small things. Lisa notices that her parents are more critical when she wants new clothes. Milan's football club is raising its membership fees, and Noor's school is charging more for outings. These aren't large sums in themselves, but together they force the family to make choices. A weekend getaway is postponed, and the annual amusement park visit is on the horizon.

As an accountant, Sofie understands perfectly what's happening: money is losing value, prices are rising faster than incomes. Yet, it feels different when it affects your own family. Saving is becoming more difficult, and the money that's been set aside seems less secure than before. "It feels like we're working harder to keep things the same," she says one evening at the kitchen table.

From an entrepreneur's perspective:

CHOCOKING was a success story for years. The company marketed affordable chocolate candies that were readily available in supermarkets and local shops. Under the leadership of CEO Clara Serneels, the company grew steadily. Production ran smoothly, prices were stable, and demand remained high. But that balance came under pressure as inflation became increasingly apparent.



It started with the raw materials. The price of cocoa rose sharply due to poor harvests and higher transportation costs. Sugar, milk powder, and packaging materials also became more expensive. What had previously been minor fluctuations now became structural price increases. Clara saw her cost reports turn redder month after month. Each chocolate bar cost more to produce, even before it left the factory.

And it didn't stop there. Energy costs for the production lines rose, as did wages. CHOCOKING wanted to continue paying its employees fairly, especially since they too were facing rising living costs. Wage indexation was necessary, but it significantly increased the company's fixed costs. Inflation suddenly felt no longer like an abstract economic concept, but like a daily challenge.

Clara faced difficult choices. If she were to pass the higher costs entirely on to the consumer, CHOCOKING risked losing customers. After all, chocolate isn't a commodity; people can easily switch to cheaper alternatives. But if she didn't raise prices, profit margins would be jeopardized, and investing in the future became increasingly difficult.

After lengthy meetings, Clara decided on a cautious strategy. Prices were raised slightly, but at the same time, the company sought cost savings. Packaging was simplified, processes were made more efficient, and suppliers were renegotiated. Innovation projects were postponed, and marketing budgets were managed more tightly. Inflation forced CHOCOKING to look more critically at every euro spent.

The uncertainty weighed on the entire company. Long-term planning became more difficult, as no one knew how long the price increases would last. Yet, Clara remained determined. She communicated openly with her staff and emphasized the need to adapt to keep CHOCOKING healthy.

For CHOCOKING, inflation didn't mean immediate doom, but it did represent a clear reality: business became riskier, margins narrower, and decisions more difficult. The company's story changed from carefree growth to cautiously seeking balance in an economy where money was becoming a little less valuable every day.



CONSEQUENCES OF INFLATION FOR HOUSEHOLDS	CONSEQUENCES OF INFLATION FOR BUSINESSES

AND WHAT ARE THE CONSEQUENCES FOR THE GOVERNMENT?

For the government, inflation feels like a constant balancing act. What citizens and businesses see at the checkout or on their energy bills translates into rising expenditures, difficult choices, and increasing budgetary pressure for the government.

When inflation rises, a significant amount of government spending automatically increases. Civil servant wages are indexed, as are pensions and social benefits.

This isn't a political choice, but a built-in mechanism to protect citizens' purchasing power. From a social perspective, this is essential, but financially, it means that federal government expenditures increase rapidly and sometimes unexpectedly. Every additional percent of inflation weighs heavily on the budget.

At the same time, the government is also seeing its own costs rise. Energy for government buildings, infrastructure projects, defense equipment, healthcare, and public transportation are becoming more expensive. Projects planned years ago suddenly turn out to cost much more than originally budgeted. As a result, investments have to be reviewed or postponed, putting pressure on long-term plans.

On the revenue side, inflation seems favorable at first glance. Higher prices increase VAT revenues and nominal tax revenues. But that advantage is relative. When families and businesses experience difficulties, economic activity slows down. Lower consumption and fewer investments ultimately mean less stable revenues for the government.

Moreover, the federal government feels the political and social responsibility to intervene. High inflation increases the pressure to implement support measures: energy premiums, temporary VAT reductions, subsidies, or targeted support for vulnerable groups. These measures are intended to protect purchasing power and prevent social unrest, but they increase the budget deficit and national debt.

Inflation also complicates policymaking. Decisions must be made more quickly, often in the face of uncertainty. What seems sufficient today may be insufficient tomorrow. The government must constantly balance social protection, budgetary discipline, and economic stability.

CONSEQUENCES OF INFLATION FOR THE GOVERNMENT