

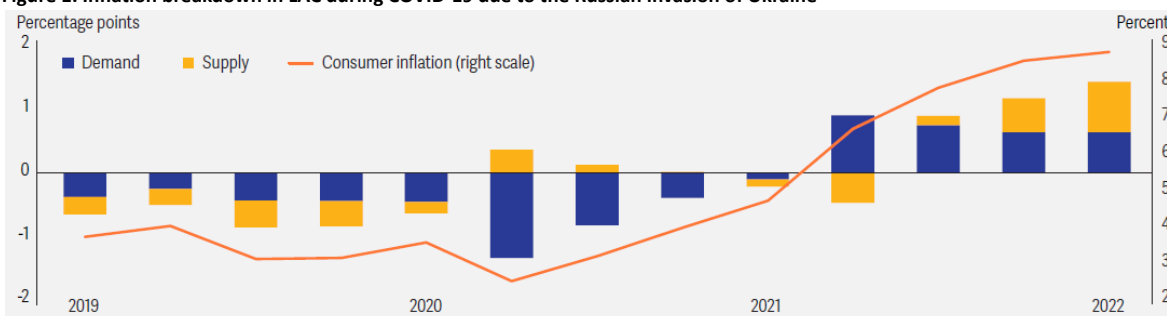
Potential effects of increasing inflation and recommendations for the region

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Context

Since 2020, there has been an increase in inflation in the region. In 2021, inflation in the region was strongly marked by an increase in demand, probably linked to fiscal support measures to face the crisis. However, since the end of 2021, there has been an increase related to supply problems, mainly energy and food.

Figure 1. Inflation breakdown in LAC during COVID-19 due to the Russian invasion of Ukraine

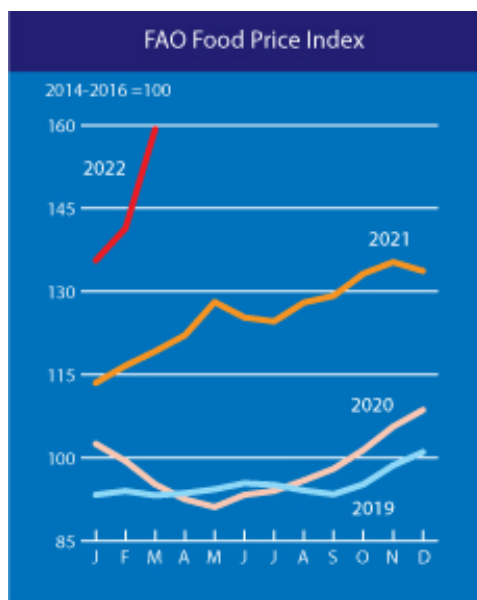


Source: Based on Ruch and Taskin, 2022.

Note: Based on sign-restricted Bayesian VAR models. Decompositions only show demand and supply shocks and exclude other shocks. Shocks are measured as deviations from a model-based constant. The models are updated to 2022:Q1 using the available actual data and forecasts for inflation and GDP growth from JP Morgan. Regional aggregates are a weighted average of Brazil, Chile, Colombia, Mexico, and Peru using 2020 GDP in constant US dollars. "Consumer inflation" is shown as a deviation from a model-based constant or initial condition.

Source: World Bank. 2022.

Figure 2. FAO Food Price Index.



Source: FAO. 2022.

FAO has also expressed concern about rising food prices. The FAO food price index in March 2022 was 12.6% higher than in February 2022, with a giant leap that took it to a new level, the highest since its creation in 1990. In April it presented a slight decrease of 0.8%, despite this it is 29.8% above the value recorded in the same month last year. Among the food prices that have risen the most in recent months are vegetable oil, with an increase of 23.2% in March compared to February and a slight decrease of 5.7% in April, and 17.1% in cereals in March and a slight decrease of 0.4% in April. In April, dairy products (0.9%), meat (2.2%) and sugar (3.3%) showed moderate increases.

In addition, it should be kept in mind that in 2021 extreme poverty reached 13.8% and poverty reached 32.1%, thus reaching the highest level of extreme poverty in 30 years. The increase in inflation translates into higher prices which, added to the effects of the socioeconomic crisis due to COVID-19 and the structural problems of the region, could increase food insecurity and poverty among vulnerable people.

Potential programmatic risks

Operational risks

- **Insufficient resources for ongoing** projects due to price increases not considered in project planning (the original budget is not enough to cover evolving prices).
- **Increase in implementing costs** for programmes and activities in the short and medium term.
- **Fewer people assisted or a decrease in assistance coverage.** The money disbursed will not be enough to cover the items/services initially expected and calculated. People's purchasing power will be reduced, so the intervention will be less impactful.
- **The costs of delivering cash and voucher assistance programmes may increase** in the context of inflation.

Contextual risk

- The current rise in **inflation is regressive** and low-income households are most affected by the increase in the cost of living.
- **Increased risk of social unrest in certain countries in the region.** Particular attention should be paid to countries currently facing complex contexts or with a recent history of social conflict/unrest over economic issues in the last 15 years (since the 2008 crisis).
- **Increased food insecurity**, particularly in terms of availability and access.
- **Difficulties for governments to meet social needs:** restrictive measures to spending.
- Increased risk of gender-based violence at household level and increased poverty and extreme poverty.

Recommendations

- **Analyse the inflation tendency** and understand how the population is adapting to it (take an Age/Gender/Diversity approach), to avoid causing harm by targeting only the most vulnerable.
- **Monitor prices for the Minimum Expenditure Basket (MEB)** and energy expenses in countries where RCRC has operations. Even in the case of sectoral objectives, it is recommended to monitor the MEB, rather than specific sectoral goods only. If there is no MEB, other sources such as the Consumer Price Index can be used. It is key to define the frequency of the price monitoring, independently of the transfer frequency. Ideally, the monitoring will be done in a coordinated way with other actors.
- Implement **inflationary adjustment measures** to determine the budget for activities and projects that will last for 3 months or beyond (this is based on the assumption that the inflation in the region might remain at an average of 7% in 2022). Plan for extra funding for this and, if necessary, include a clause in the donor agreement.
- **Foresee/agree on triggers to review** the transfer **value** or a change in the assistance **modality** in advance. This will help adapt in a quick manner avoiding delays in the coordination and implementation of the changes.
- **Negotiate prices with vendors** where vouchers are being used, to keep them stable for a fixed period, maintaining purchasing power for participants (especially useful in short interventions).
- Consider the disbursement of CVA in hard currency (such as USD), but only after a thorough technical evaluation that looks at the consequences.
- Strengthen **environmentally smart** food security and agriculture programmes and activities.
- **Harmonize** the response and decision making with other actors and donors.
- Base all **decision-making on evidence** and solid analysis, not on anecdotal examples.
- Ensure **constant and clear communication with the population** about changes in the programme.

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