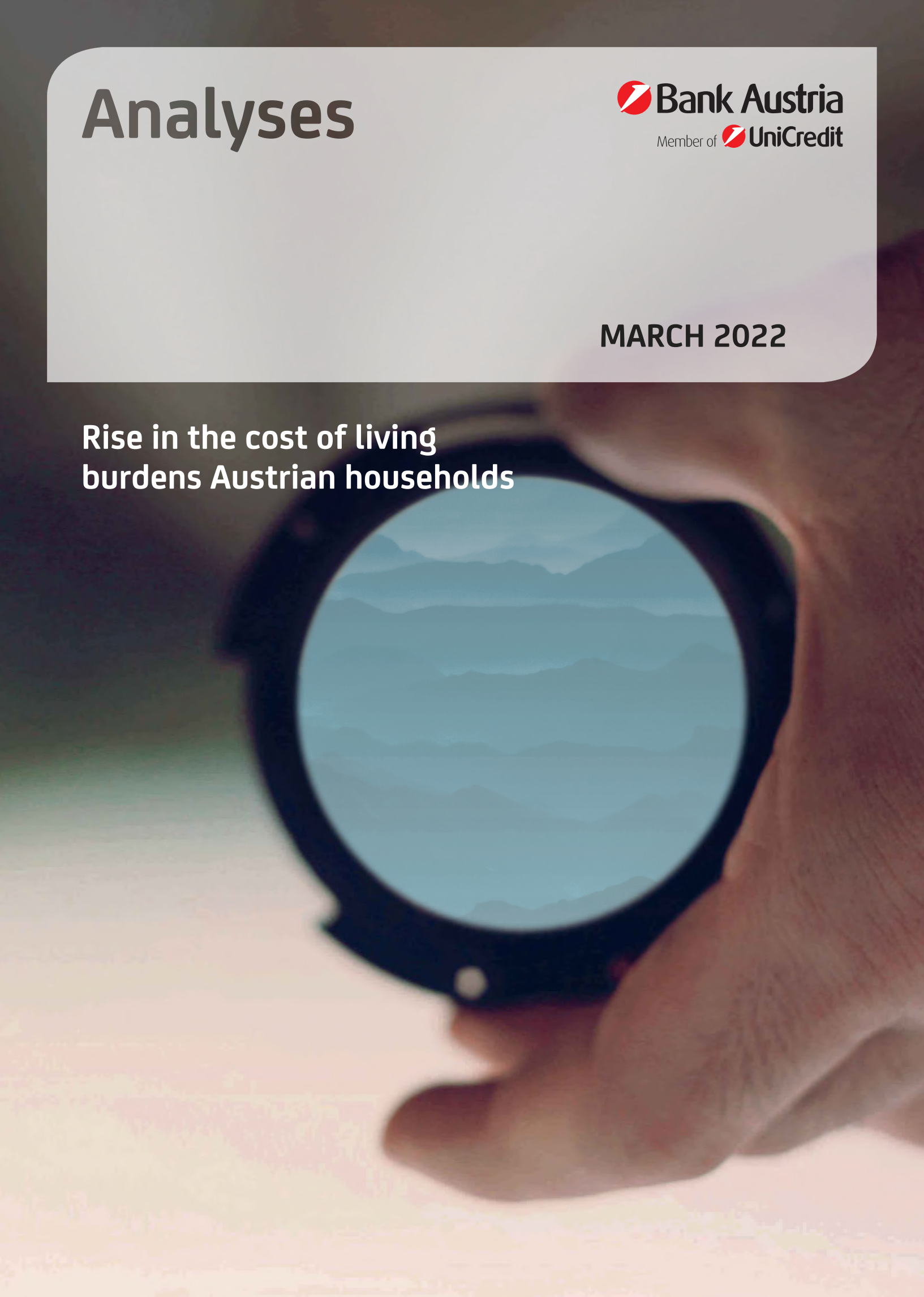


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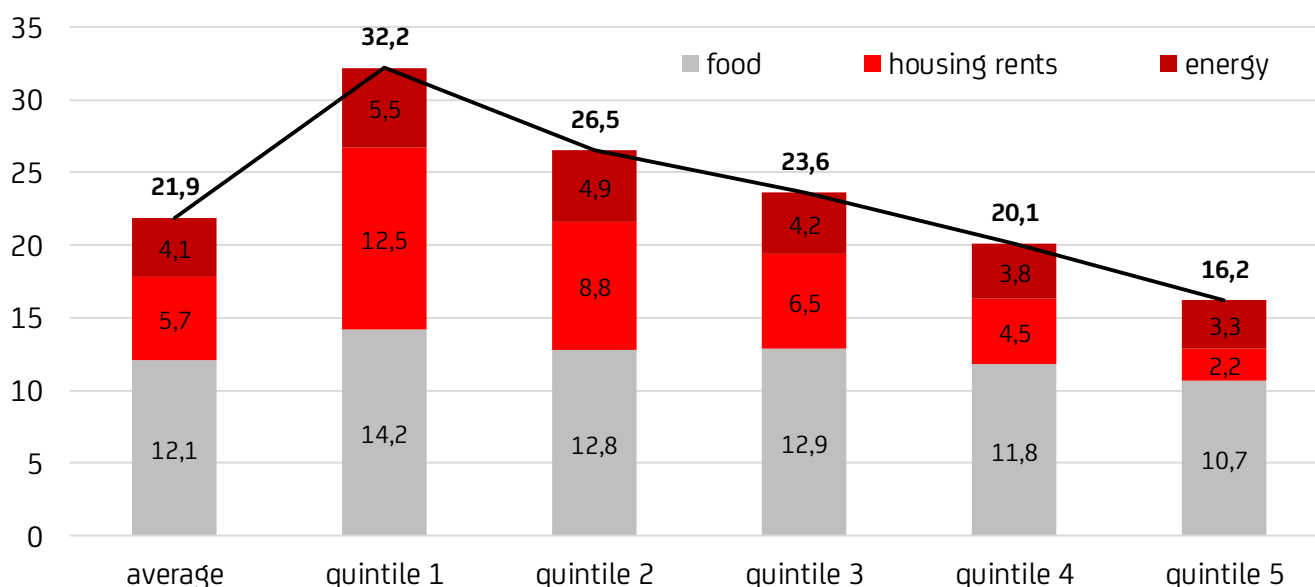
MARCH 2022

**Rise in the cost of living
burdens Austrian households**



ABOVE-AVERAGE BURDEN ON LOW-INCOME HOUSEHOLDS DUE TO RISING INFLATION

**Share of necessary cost of living in total household expenditures (2020,
%, in quintiles)**



Sources: Statistik Austria, UniCredit Research

- The necessary cost of living for food, housing energy and rents is rising sharply, additionally fueled by the Ukraine conflict, which has pushed gas and electricity prices to record highs. Increased wholesale prices are now feeding into consumer food prices. Inflation has risen to 5.9 per cent year-on-year in February 2022.
- These price increases disproportionately affect the lowest income groups. The share of total household expenditure of the lowest income quintile on necessary cost of living (household energy, rent and food) is almost 1/3, while the top income quintile spends less than half of this expenditure, 16% of total household expenditure.
- The different expenditure shares for sharply rising costs of living of the individual income groups have important macroeconomic effects. Fiscal measures to mitigate the rising cost of living should remain targeted at the lowest income groups and necessary living costs, not only for reasons of fairness, but also for economic reasons.

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Status: March 2022

Recovery from pandemic, supply bottlenecks and Ukraine conflict drive up prices

The cost of living is currently rising rapidly in Austria. In February 2022, inflation rose by 5.9 percent year-on-year. Energy prices have climbed particularly sharply due to the escalation of the Ukraine conflict. The price of residential energy rose by 25.3 percent year-on-year. Liquid fuels experienced a particularly strong price spike, rising by 48.9 percent compared to the previous year. The price of gas also rose particularly sharply, by 64.3 percent, due to the increased uncertainty of supply. In the wake of the gas price increase, the electricity price also climbed (+14.9 percent compared to the previous year). The price increase for fuels caused by the rise in crude oil prices to as much as 130 US dollars per barrel amounted to a high 29.1 percent year-on-year in February 2022. The rise in costs due to the prolonged increase in energy prices is now having a strong impact on food prices for consumers. Food prices increased by 4.3 percent year-on-year in February and food prices are expected to continue to rise due to the Ukraine conflict, as Ukraine has been a global heavyweight in wheat and maize exports and security of supply is in question. In contrast, actual rents paid fell slightly in February by around 2 percent year-on-year, supported in part by the suspension of the benchmark rent increase in the previous April. However, rents have been strong drivers of the cost of living over the longer term. In the past five years alone, from 2017 to 2021, rents in Austria increased by over 18 percent, or more than 3 ½ percent annually, with general inflation of only 2 percent over the same period.

Cost of living accelerate due to Ukraine conflict

Energy prices rise particularly sharply

Share of necessary household expenditure for low-income households twice as high as for high-income households

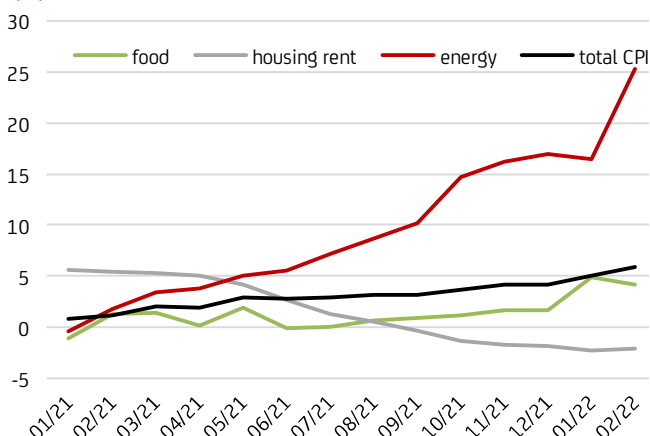
For households in the top income quintile, cost of living accounts for only one-fifth of total individual inflation, but for the lowest income quintile it accounts for almost 30 percent.

Rising cost of living places weighs more heavily on low-income households

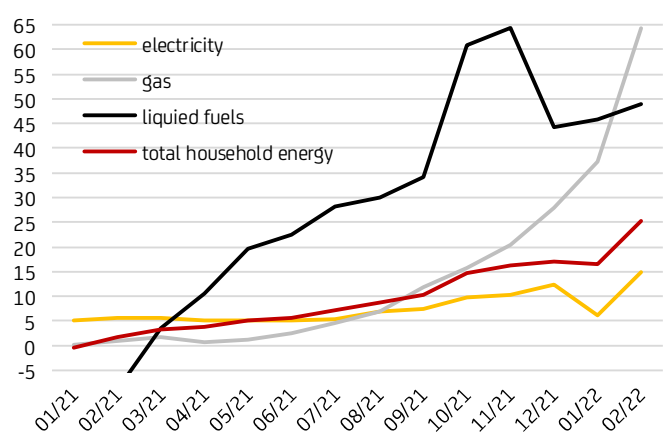
The current price increases are a particularly heavy burden for low-income households. Households with lower incomes have to spend an above-average share of their household expenses on essential living costs such as rent, food and housing energy. For the lowest income quintile, i.e. the 20 percent of Austrian households with the lowest income, this item accounts for almost one third of total household expenditure. For the highest income quintile, on the other hand, the share of essential living costs is only half, at 16 percent.

Taking into account the different shares of consumption expenditure of individual households, the strong price increases of essential cost of living show a significantly stronger price increase for households in the lower income segments. On average, the share of essential costs of living amounts to 22 percent of total household expenditure in Austria. Based on the current inflation rate, this results in an impact of these categories on overall inflation that is above average at 24.5 percent. While for households in the highest income quintile the cost of living is only responsible for about one fifth of the individual total inflation, this share is almost 30 percent in the lowest income quintile.

Chart 1: Price development for cost of living
(yoy in %)



Grafik 2: Price development for household energy
(yoy in %)



Source: Statistik Austria, UniCredit Research

Low-income households have no reserves to compensate for the increase in the cost of living

The heavy burden of the high increase in the cost of living for households in the lower income segments becomes particularly clear when absolute income levels are taken into account. Broken down into quintiles, the monthly household expenditure for the lowest-income twenty percent of households is less than 1,800 euros, whereas for the highest-income twenty percent of households it is well over 5,000 euros. A comparison of average monthly household expenditure with household income shows that in the lowest income quintile, expenditure even exceeds income. This is possible because larger purchases in particular are often financed by alternative sources of money, such as savings, gifts, inheritances or loans, and on the other hand the incomes are not likely to be recorded in full due to a lack of information on private transfers or property income. In the highest-income households, on the other hand, incomes are in some cases significantly higher than household expenditure, as an increasing proportion of income is saved. Since the lowest income quintiles have hardly any savings, the strong price increase in the cost of living cannot be compensated by reserves, but leads directly to a restriction of consumption.

Strong increase in fuel prices affordable for most of the affected households, but food and housing energy not affordable

Rise in fuel prices hits high-income households above average

In our analysis, we have not included in the necessary cost of living the expenses for fuel for the operation of private means of transport, which have increased by almost 30 percent year-on-year due to the sharp rise in the price of crude oil in February and are the subject of particularly strong public discussion, because in most cases alternatives are available in the form of public transport, while the consumption of food or housing energy or rental costs have no alternative. In addition, it can be seen that the share of expenditure on the operation of private means of transport in total household expenditure increases disproportionately strongly with rising income. Thus, the share of household expenditure on the operation of private means of transport in the lowest income quintile is only 5 percent, while in the highest income quintile the share is more than 50 percent higher at around 8 percent. This means that the sharp increase in fuel prices puts a much heavier burden on high-income households, which often get several cars with higher performance and fuel consumption, than on low-income households, which often do not have a private means of transport at all. The burden thus hits households with a high savings ratio harder, who can compensate for the cost increase through existing reserves without having to cut back on consumption.

Chart 3: Share of increase in cost of living in total inflation
(February 2022, in %)

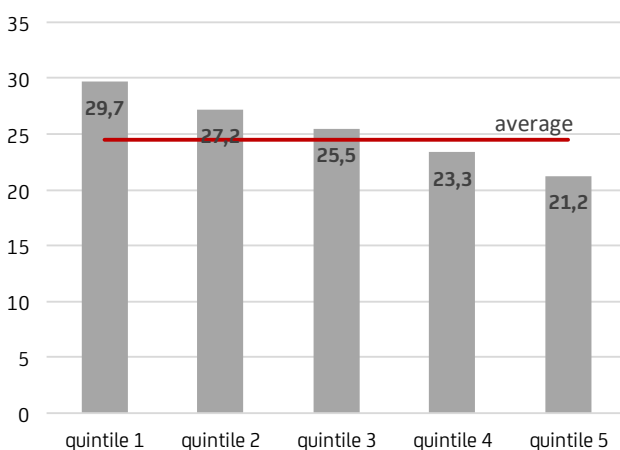
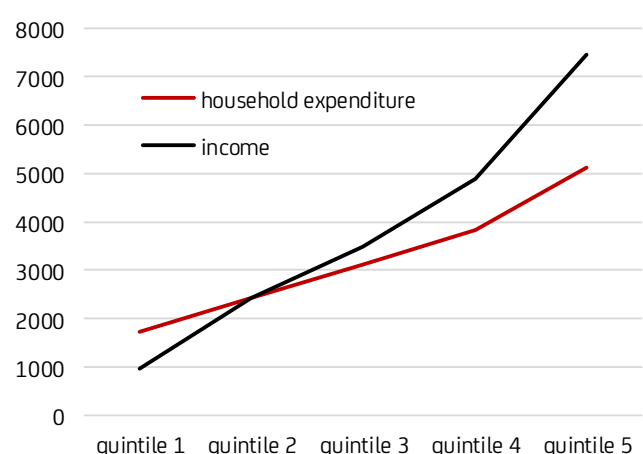


Chart 4: Household expenditures and income
(2020, monthly in EUR)



Source: Statistik Austria, UniCredit Research

Energy cost compensation — but how?

Energy cost compensation only makes sense if targeted at affected income groups and exclusively for relevant household expenses

While overall inflation is broadly similar for all income groups given spending patterns (see chart 6), the sharp increase in necessary living costs, especially for food and housing energy, creates an above-average burden for lower-income households. The different expenditure shares for these sharply rising living costs have important macroeconomic implications. The propensity to consume is significantly higher in lower income groups simply because they are at or near their budget limit. It follows, among other things, that fiscal policy measures to mitigate the rising cost of living should be targeted at the lowest income groups and exclusively at necessary living costs, not only for reasons of fairness but also for economic reasons. Therefore, in our view, priority should be given to direct transfers to support rental, housing energy and food costs for particularly affected households, or to an adjustment of wage and income tax for an envisaged energy cost compensation. In the case of general, less targeted measures, such as a (temporary) reduction in VAT, especially on fuel prices, mineral oil tax or a general increase in the commuter allowance, there is a danger that high-income households with a high savings rate will be subsidised by lower-income households at the budget limit.

Chart 5: Expenditures spent on operating private means of transport (share in total expenditures in % resp. EUR, 2020)

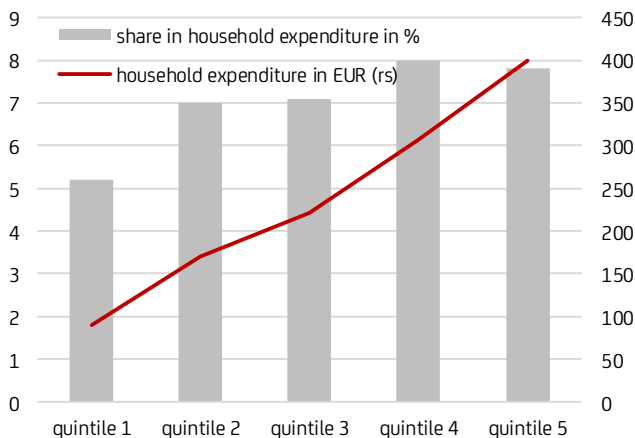
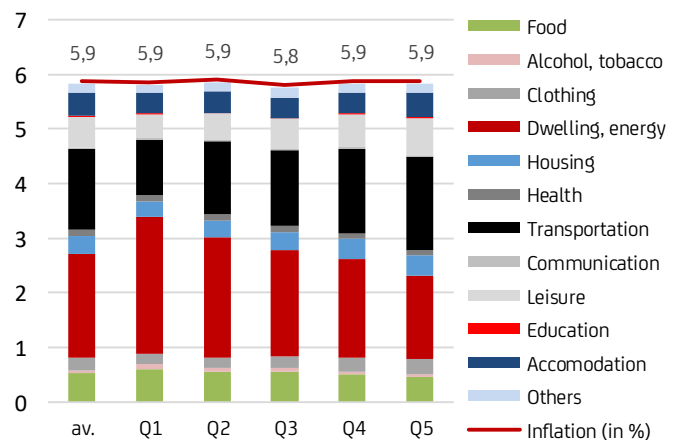


Chart 6: Household inflation by income quintiles (February 2022, in % with shares of the main expenditure groups)



Source: Statistik Austria, UniCredit Research

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