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## The cost-of-living crisis and poverty in Europe

*The cost-of-living crisis is driving up hardship and financial insecurity across Europe, but it is not affecting all countries or groups in the same way. Overall, countries and groups who entered the crisis facing the greatest risk of poverty have been the worst affected, but differences in energy policies have also driven differential impacts in less predictable ways. Similarly, there is a considerable commonality in the ways that national governments have chosen to support variations in the level of resources and in the priority given to different types of help. This article also explores the immediate and long-term consequences of the increasing hardship created by the cost-of-living crisis and the prospects for some positive impacts through accelerating action on climate change.*

Across the whole of Europe, the cost-of-living crisis is pulling more people into poverty, deepening hardship for those who were already struggling and increasing financial precariousness for some on middle incomes who were previously secure.

However, these trends are not playing out in the same way in each country, and they are shaped by three main factors. First, the pre-existing levels and depth of poverty and the strength or otherwise of the protections in place before the current crisis. Second, differences in energy supplies, use and energy efficiency. Third, variations in the response of governments and the level and type of support they are offering households and businesses.

Soaring inflation is at the heart of the crisis, with its rate in the euro area jumping from 2.5% in 2021 to 10% in 2022.<sup>1</sup> It was already climbing even before Russia invaded Ukraine, caused by the post-pandemic opening up of economies and pressure on global supply chains. However, it was turbocharged by the conflict in Ukraine and the sudden restrictions on energy supplies, causing prices to shoot up. The impacts have not only been seen in energy bills, they have also fed into sharp rises in other costs, especially food. On average,

<sup>1</sup> Eurofound (2022) "The cost-of-living crisis and energy poverty in the EU: Social impact and policy responses". Background paper, Eurofound, Dublin.

across Europe, energy costs rose by 42% and food by 11.1%.<sup>2</sup> Wider pressures have followed, including on public services. In October of this year, the mayors of the Eurocities network wrote to leaders warning that “skyrocketing energy prices, and inflationary pressure is now putting the provision of public services at risk”.<sup>3</sup>

However, the impacts of these costs vary significantly between different countries. First, because the extent to which higher energy costs have driven rises in the cost of living has diverged sharply. The IMF calculates<sup>4</sup> that energy bills have raised the cost of living by less than 5% in certain countries including France, Spain, Finland, Sweden and Croatia. By contrast, energy has driven up the cost of living by more than 10% in the Netherlands, Italy, Denmark, the Czech Republic and the UK.

Both sources of energy and energy efficiency matter, as well as the speed and effectiveness of responses to the current crisis. The UK has fared particularly poorly, seeing the biggest direct cut to households’ spending power in Western Europe. This is in part due to greater reliance on gas for its heating and slower action to control prices. However, it is also suffering from poor home energy efficiency due to its old housing stock and the scaling back of interventions to improve it over the decade leading up to the crisis. Other countries have reaped the benefits of better approaches.<sup>5</sup> For example, Germany’s long-term programme to improve energy efficiency through grants, loans and advice, and Finland’s use of tax incentives to shift away from oil heating. Overall, though, Europe as a whole is suffering more because it failed to move faster on energy efficiency. Fixing this is vital from the perspective of climate change, but has been given even greater urgency by the crisis in Ukraine: buildings are responsible for a third of Europe’s greenhouse gas emissions, but three quarters (75%) of its buildings are energy inefficient.<sup>6</sup> There is hope that the intensity of this crisis will accelerate shifts to greater energy efficiency, renewables and even more sustainable food chains and plant-based diets. But in the meantime, it is those on the lowest incomes who are paying the highest price for the continent’s slow progress.

Second, those countries with higher levels of poverty to start with are also seeing much higher proportions of people struggling to cope with rising bills. The fifth round of Eurofound’s “Living, working and COVID-19” survey, carried out in spring 2022, showed that the proportion of respondents reporting being behind with utility bills was as low as 7% in Denmark and Sweden, countries with low pre-crisis poverty, and as high as 50% in Greece, which had started with far higher poverty levels.

Across countries, the nature of these economic pressures means they land especially heavily on those with lower incomes, who spend proportionally more of their incomes on food and other essentials. For those households too, cutting back on the expenses which

<sup>2</sup> Ibid.

<sup>3</sup> Eurocities (2022) “Cities demand a ‘bold and unified European response to the energy crisis’”.

<sup>4</sup> Kammer, A. (2022) “Europe must address a toxic mix of high inflation and flagging growth”. IMF Blog.

<sup>5</sup> Hodgkin, R. and T. Sasse, (2022) “Tackling the UK’s energy efficiency problem: What the Truss government should learn from other countries”. Institute for Government, London.

<sup>6</sup> Goyens, M. (2022) “The cost of living crisis: an opportunity to move to sustainable lifestyles?”. OECD Forum Network, Paris.

have risen most means going without essentials, causing serious hardship, rather than simply reductions in leisure spending.

It is striking, too, that the impacts of these problems vary across different groups in society. Women<sup>7</sup> and families with children are especially bearing the brunt of the situation. By November, a survey of six countries for the French anti-poverty NGO Secours Populaire<sup>8</sup> found that nearly half (48%) of parents had cut back on their own food to feed their children, a similar proportion (49%) were worried about not being able to meet their children's needs in the future, and a third (33%) said they were already unable to give their children as varied a diet as they would like. The study also showed that different groups were most at risk of falling into poverty in each country – in Germany retired people were most at risk, in Italy it was young adults, and in the UK it was single-parent families.

Sustained rises in poverty and families having to go without essentials is likely to have consequences that continue far beyond the point at which the immediate economic crisis eases. Worse mental and physical health, higher debt, reduced financial resilience and damaged child development will have consequences that may well last for years into the future. The World Health Organization estimates that a third of the higher number of deaths seen in the winter compared to the summer is due to cold homes.<sup>9</sup> Tragically, this figure is likely to rise significantly this winter as more people find themselves unable to afford to turn on their heating. People on low incomes are already more likely to be in poor health. Across the EU, among those struggling to make ends meet, over a fifth report poor health, compared with only 4% of people finding it easy to make ends meet.<sup>10</sup> This means that this group is already more vulnerable to the most serious consequences of living in cold, damp homes. Research by the UK's Joseph Rowntree Foundation recently found that 3 million people on low incomes could not afford to heat their homes, and 2.5 million were also unable to afford enough food – around a quarter of the poorest fifth of the country.

Poor mental health is even more closely linked to poverty and financial insecurity. In the EU, 84% of those finding it difficult to make ends meet were found to be at risk of depression, compared to 36% of those who were easily making ends meet.<sup>11</sup> Unsurprisingly therefore, as the cost-of-living crisis has tightened and people on low incomes have found themselves unable to afford basic essentials, charities offering mental health support have already reported big rises in the numbers turning to their helplines.

Family relationships are often damaged by such financial pressures and their health consequences, with relationships breaking down and increases in domestic abuse driven by financial strain and recession. There have already been reports of domestic abuse rising as a result of the cost-of-living crisis. The economic situation not only increases abuse but makes it harder for victims to leave because of the risk that they will find themselves facing

7 Eurofound (2022) "The cost-of-living crisis and energy poverty in the EU".

8 Vilain, O. (2022) "Exclusive poll: Europeans on the brink". Secours Populaire, Paris.

9 Finch, D. (2022) "The cost of living crisis is a health emergency too". The Health Foundation, London.

10 Eurofound (2022) "Living, working and COVID-19 in the European Union and 10 EU neighbouring countries".

11 Ibid.

destitution if they do. A survey of frontline staff at one of the UK's main domestic abuse charities, Refuge, found that the cost-of-living crisis is leading half of survivors to return to their abusers.<sup>12</sup>

In Eastern Europe, alarming numbers of children are being forced into poverty by the war. In Russia itself, 2.8 million more children are now in poverty, with half a million more in Ukraine and 110,000 more in Romania. A UNICEF study of the impacts of the cost of living crisis in Eastern Europe and Central Asia has warned that 4,500 more babies may die before their first birthdays and an additional 117,000 children may drop out of school this year.<sup>13</sup> The UN warns that childhood poverty often has lifelong impacts, with developmental, educational and health consequences leading to a far higher risk of poverty in adult life – a cycle that is all too familiar in every European country as well.

Across European governments, public finances are also taking a serious hit. During the Covid pandemic, many governments spent an unprecedented amount of money supporting their citizens and businesses, expecting to be able to repair their public finances as the pandemic eased and economic recovery took hold. Instead, they were immediately plunged into a crisis of similar proportions and found themselves again spending eye-watering amounts of money helping their populations weather the storm.

The response of most governments in Europe to the pressures caused by rising energy costs has included four components – reducing energy or consumption taxes, regulating retail energy prices, cash transfers to vulnerable groups, and support for businesses. Only four countries – France, Malta, Portugal and Spain – have also imposed wholesale price regulations. However, despite this commonality, the level of funding directed to these measures varies very significantly,<sup>14</sup> with some countries concentrating on direct support for households and businesses, and other countries focusing funding on utility companies.

To support households and businesses, Germany is estimated to be spending 7.4% of GDP, Greece 5.7%, Italy and the Netherlands 5%, the United Kingdom 3%, France 2.8% and Poland 2.2%. By contrast, Sweden is only spending 0.3%, Finland 0.5% and Belgium 0.8% of GDP on this type of support.

Those countries not spending as much to directly support households and businesses tend instead to be directing higher levels of spending at utility companies. Sweden is spending 4.4% of GDP on credit, loans and bailouts for utility companies, with Denmark and Finland close behind at 4%. By contrast, this proportion is far lower in countries whose spending has gone to individuals and businesses – 1.9% in Germany, 1.7% in the United Kingdom and 0.4% in France (although the French government is currently being sued by its main energy provider, EDF, after it was forced to sell energy to consumers at a loss without similar compensation).

12 Refuge (2022) "New data from Refuge warns that cost of living crisis is forcing survivors of domestic abuse to stay with abusive partners".

13 United Nations (2022) "Surge in poverty-stricken children in Eastern Europe, Central Asia".

14 Sgaravatti, G., S. Tagliapietra, and G. Zachmann (2022) "National fiscal policy responses to the energy crisis". Bruegel Datasets, Brussels.

The methods and scale vary, but every country will enter 2023 with its public finances under significant strain. To make matters worse, the hoped-for economic recovery has been knocked off course, making the future outlook for repairing public finance much gloomier. The OECD's economic outlook for September 2022<sup>15</sup> suggests that the world's economy is slowing even more than had been expected, with annual growth in 2023 expected to be just 2.2%. Within Europe, Italy's economy is expected to grow by only 0.4%, and France's by 0.6%, while the UK's is expecting no growth at all next year and Germany's economy is expected to contract by 0.7%. In fact, more than half of countries in Europe are expected to enter a recession this winter. Although inflation should start to decline next year, it is still expected to remain high, at around 6% in advanced economies and 12% in emerging European economies.<sup>16</sup> Pressure on both households and businesses will therefore remain intense.

This will be the third blow to people struggling to get by. First, the Covid pandemic affected people in poverty more heavily than those who were better off before the pandemic, both in terms of health and economic impacts. Those who were already on low incomes found themselves pulled deeper into poverty as economies shut down, while many Europeans who had never faced poverty before were dragged into it. People with secure jobs that could be done from home were more able to maintain their living standards and also stay safe. Those with lower paid and more insecure jobs were more likely to lose them and, if their work continued, they were more likely to have to leave their home and work in ways that put them at greater risk of contracting the illness.

The pandemic particularly drove increases in poverty in around half of EU member states – Portugal, Greece, Spain, Italy, Ireland, Slovenia, Bulgaria, Austria and Sweden.<sup>17</sup> In the UK, as in many European states, those on lower incomes used up savings and found themselves in more debt as a result of the pandemic, whilst many on higher incomes increased their savings and financial security as their incomes held up and their leisure spending was curtailed.<sup>18</sup>

The second blow was the cost-of-living crisis of 2022, which saw poverty and debt rise and extremely concerning spikes in food poverty and destitution. Now, these same groups face a third blow in 2023 – a blow of recession, continued high prices and governments constrained in their response by both their financial situation and the need to avoid stoking inflation even higher.

High inflation is driving central banks to tighten monetary policy by raising interest rates, with the European Central Bank raising rates for the first time in 11 years. Governments then have to use fiscal policy to protect their most vulnerable citizens. At the same time, however, governments are keen to avoid further stoking inflation through too much or too broad a fiscal stimulus, leaving them with few tools to kick-start economic recovery.

15 OECD (2022) "Paying the price of war: OECD Economic Outlook". Interim Report, September.

16 Kammer, A. (2022) "Europe must address a toxic mix".

17 Eurostat (2021) "Early estimates of income and poverty in 2020".

18 Bell, T. (2021) "The Covid certainty: more savings for the rich, more debt for the poor". Resolution Foundation, London.

This raises the spectre of continued stagflation and the risk that pressures on public finances lead more governments to cut back on social protections, further worsening the poverty and hardship that have already been fuelled by the unequal impacts of both the Covid pandemic and the subsequent cost-of-living crisis. The experience of the UK should stand as a warning to those contemplating this. After the financial crisis of 2008, UK governments from 2010 onwards imposed swinging cuts to both public services and welfare support. This led to sharp rises in deep poverty and destitution and also contributed to the country's woeful record of productivity and income growth over these years.

There are worries too for many governments about the potential social and political consequences of these conditions. Large majorities in Western European countries believe their governments are handling the cost-of-living crisis badly – from 82% in both Italy and the UK, to more than seven in ten in Germany, Spain and France, and more than six in ten in Denmark and Sweden.<sup>19</sup> And the political risks go beyond general dissatisfaction. Populist governments have already taken power in Hungary and Poland, while many fear that more such governments may be swept into power as living conditions worsen. The governments in both Slovakia and Estonia have collapsed in recent months, buckling under the pressure to do more to help struggling citizens, out of budgets already stretched after the pandemic. A poll of voters in France, Germany, Poland and the UK, which was published in September, found that not only were further rises in poverty likely but also majorities in every country were worried about social unrest. In Poland, three quarters (75%) said this, with 69% in France, 64% in Germany and 57% in the UK agreeing. In France, four in ten respondents wanted to see the return of the 'yellow vests' protest movement that caused such turmoil in 2018 in response to rising fuel costs.

While people across Europe are suffering hardship as a result of the cost-of-living crisis and Russia's war in Ukraine, there are even worse impacts across other, much poorer regions. The UN estimates<sup>20</sup> that the crisis has pushed 71 million people from 159 developing countries into poverty, with 49 million people in 46 countries already living in 'near-famine-like conditions' and 750,000 people at immediate risk of starvation. Teresa Anderson, at the NGO Actionaid, warned earlier this year that the wheat shortages caused by the war in Ukraine have exacerbated an already dire situation, with African economies reeling from the pandemic, climate change and political ineffectiveness. "If nothing changes, we could be facing a famine of unimagined proportions [...]. The situation is particularly extreme in the Horn of Africa, where 20 million people are already suffering severe hunger because of the ongoing drought".<sup>21</sup> This is, of course, an appalling humanitarian disaster. It is also likely to feed into greater instability around the world and increased movements of people. In many European countries, hostility to migrants is a significant issue, with perceptions of uncontrolled migration fuelling far-right parties. This situation is only likely to worsen as the populations of these countries themselves feel poorer and more insecure.

19 Connor, J. (2022) "New cost of living tracker reveals extent of crisis in Western Europe". YouGov.

20 Gray Molina, G., M. Montoya-Aguirre and E. Ortiz-Juarez, E. (2022) "Addressing the cost of living crisis in developing countries: poverty and vulnerability projections and policy responses", UNDP Report.

21 Schwikowski, M. (2022) "African food prices soaring amid Ukraine war", DW.

Perhaps most worrying of all – many predict that next winter will be far worse than 2022. This year, Europe was able to build up its stockpiles while Russian gas flowed over the summer. It was also able to import liquid gas from China. However, there seems little likelihood of either being repeated in 2023. The director of the International Energy Agency (IEA), Fatih Birol, has warned Europeans that next winter may be “more difficult than the winter we are experiencing now”.<sup>22</sup> Yet the IEA has also sounded a more optimistic note in its most recent report, noting that the global energy crisis is driving “a sharp acceleration in installations of renewable power, with total capacity growth worldwide set to almost double in the next five years [...] helping keep alive the possibility of limiting global warming to 1.5 °C”.<sup>23</sup>

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22 McNicoll, A. (2022) “Energy crisis: is next winter going to be worse?”. *The Week*.

23 International Energy Agency (2022) “Renewables 2022”. Fuel Report.