

SPOTLIGHT ON:

Spotlight on 1: Effects of Limiting Retail Margins on Inflation: Theoretical Framework and Empirical Insights

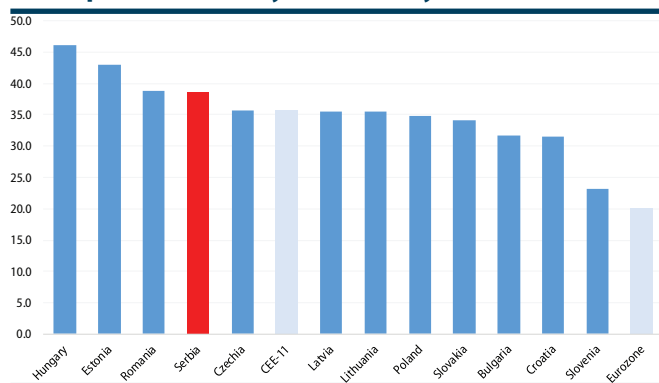
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By deciding to cap retail margins as of 1 September 2025, the Government is trying to respond to the fact that Serbia is one of the European recordholders when it comes to the rise in food prices. Although the declared goal is to protect living standards, the key question arises: what real effects and economic consequences will this measure produce in the domestic economy? This “Spotlight On” offers an ex ante analysis of the potential effects, drawing on a review of economic theory and, more importantly, on an analysis of recent experiences in Hungary and Romania, which have been applying similar pricecontrol models. Two key conclusions follow from the analysis. *First*, the effect of the measure on slowing overall inflation will in all likelihood be limited and shortlived, although a moderate reduction in prices can be expected for part of the products covered. *Second*, the measure introduces significant market imbalances and carries the risk of pronounced negative consequences. It seriously calls into question the current business model and profitability of the retail sector, which could lead to layoffs and disruptions in the supply chain. If it were to last longer, the measure would discourage investment because of increased unpredictability in economic policy, and abolishing it without a preprepared exit strategy would carry the risk of “suppressed inflation” and a sudden price shock, as witnessed in Romania when its multiyear cap on electricity prices was removed.

Inflationary Pressures in Serbia and CEE in the Period 2021-25 and the Economic Policy Response

The period after 2020 brought Central and Eastern Europe (CEE) a series of exceptionally large economic shocks that resulted in the highest inflation rates in decades. According to Eurostat data, yearonyear inflation in CEE peaked at 17.3 per cent in September 2022, although some

Graph 1. Cumulative growth of consumer prices in the period from July 2021 to July 2025



Source: author's calculation based on Eurostat data.

countries recorded significantly higher rates, such as Hungary (26.2 %), Estonia (25.2 %) and Lithuania (22.2 %). By comparison, Serbia, with a maximum inflation rate of a high 15.5 % recorded in March 2023, actually found itself among the countries with a relatively lower peak of the inflation wave – behind Slovenia, Croatia, Slovakia and Romania. However, if one looks at the overall burden of price growth, the picture is somewhat different. Cumulatively, the average consumer basket in Serbia increased in price by 38.6 % in the period from July 2021 to July 2025, which is slightly above the CEE average of 35.6 % and almost twice as much as in the euro area. Only Hungary (46.2 %), Estonia (43 %) and Romania (38.6 %) recorded higher cumulative price growth in the region.

Two key events defined inflation developments in this period: the COVID19 pandemic and the conflict in Ukraine. The pandemic caused deep disruptions in global supply chains, creating bottlenecks in production and transport, which first led to a sharp rise in the prices of raw materials and then of final products. At the same time, the countries of the region responded to the crisis with expansive fiscal and monetary policy aimed at supporting the economy and the population during lockdowns, which stimulated aggregate demand and thus further amplified price pressures. In this respect, Serbia stood out for its very high, nonselective support to the population, for which it spent four times more budget funds than comparable CEE countries.² Additional demand-side pressure came from a strong increase in wages, which in many countries of the region, including Serbia, markedly outstripped productivity growth. This was, among other things, a consequence of adverse demographic and migration trends. On top of this already complex situation, Russia's invasion of Ukraine in February 2022 acted as an accelerator of the cost-of-living crisis. The CEE region, because of its geographic proximity and high dependence on energy imports from Russia, was particu-

¹ Fiscal Council of the Republic of Serbia and the editorial board of the Quarterly Monitor

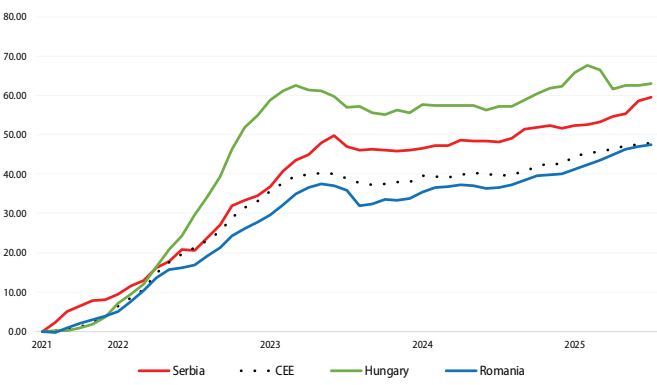
² Fiscal Council (2022). *Anticrisis budgetary measures during the COVID19 pandemic: costs, results and lessons*.

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larly affected. Natural gas and oil prices reached record levels, which had a cascading effect across all sectors of the economy – from production costs in industry and agriculture and transport to the prices of electricity and heating for households.

Although the high rise in the general price level posed a huge macroeconomic challenge, what turned this inflationary episode into a first-rate social and political problem was the fact that the largest price increases were recorded in energy and food – the very domain of basic necessities. Because these items have a relatively larger share in the average consumer basket, the extremely high rise in food prices over the past four years was a particularly heavy blow to household budgets throughout the region. Data show that Serbia was one of the outliers in Europe on this issue. While cumulative food price growth in CEE amounted to about 48 %, Serbia recorded the second-highest increase, at almost 60 % (Graph 2), with only Hungary recording a greater increase (around 63 %). In other words, food inflation in Serbia was as much as 55 % higher than the rise in the general price level.

Graph 2. Cumulative growth of food prices in the period July 2021 – July 2025 (%)



Source: author's calculation based on Eurostat data.

Part of the answer to why Serbia was one of the record-holders in food price growth lies in the structure of the increases. While the rise in the prices of industrially processed food was close to the regional average (54 % versus 50 % in CEE), what is specific to Serbia is the much faster rise in the prices of unprocessed food – fresh vegetables, fruit and meat. In Serbia, price growth in this group was by far the highest in the region, amounting to 73.1 % cumulatively, compared with only about 45 % in CEE. This suggests that, in addition to global factors, domestic factors also significantly influenced the prices of this group of products, above all frequent adverse weather and droughts, which contributed to weaker yields of fresh fruit and vegetables in 2025 and in several preceding years.

Faced with doubledigit inflation and rising public discontent, governments across Europe were under pressure to respond to the galloping costofliving crisis. The monetary policy response was standard and expected: central banks in the region, including the European Central Bank, aggressively raised policy rates in an attempt to curb aggregate demand. However, the effects of monetary policy on inflation are lagged and often insufficient to provide immediate relief, especially when price growth is driven by shocks in energy and food markets – factors that interest rates have limited impact on. Therefore many CEE governments resorted to nonstandard, administrative measures of direct market intervention, which were initially aimed at capping energy prices. Serbia followed the same path: at the end of 2021 it temporarily froze electricity and gas prices, which cost the state budget as much as €3 billion through direct subsidies and state guarantees for Srbijagas debt.

Not long afterwards, some countries in the region went a step further by introducing measures to control food prices, among which Hungary and Romania were particularly prominent. These measures, epitomised in direct price freezes and caps on retail margins, were presented as a key tool in combating the rise in the cost of living. The Hungarian government promoted them as the central pillar of its “family protection” policy, while the Romanian government’s stated goal was to protect purchasing power and curb speculative price increases. Although politically popular, these interventionist policies produced a wide range of economic consequences that manifested themselves in different ways in the two countries (see Section 3).

With the adoption of the Regulation on Special Conditions for the Trade of Certain Types of Goods,³ the Government of Serbia has taken a similar interventionist path, already seen in Hungary and Romania, with the same basic goal – protecting living standards. The Regulation, which has applied since 1 September 2025 and is limited to six months, introduces a pricecontrol mechanism for 23 categories of products. It covers most staple food products but also household chemicals, personal hygiene products and baby supplies, which, according to our estimates, account for roughly onethird of the average consumer basket in Serbia.

3 <https://www.paragraf.rs/propisi/uredba-o-posebnim-uslovima-za-obavljanje-trgovine-za-odredjenu-vrstu-robe.html>

The key elements of the measure are as follows:

- **Margin cap.** A maximum retail margin of 20 % in retail, wholesale and distribution was defined, calculated on the net selling price. An important rule is that if the margin on the day the Regulation entered into force was lower than 20 %, the retailer is obliged to apply that lower rate.
- **Freeze on purchase prices.** The Regulation also introduces a pricefreeze element, stipulating that the invoice price charged by the supplier may not be higher than the price applicable on 1 August 2025.
- **Cap on fees.** To prevent retailers from recouping lower margins through other channels, the total amount of all fees (such as rebates, listing fees, etc.) that a retailer may charge the supplier is capped at 10 % of the total net value of invoices. There are exceptions for logistics rebates (limited to 3 %) and fees for shrinkage and writeoffs (limited to 1 %). It is also forbidden to introduce new or increase existing fees that were not contracted before 1 August 2025.
- **Scope.** These measures apply to large, nonspecialised retail chains and wholesalers whose annual revenue in 2024 exceeded RSD 4.5 billion.

The theoretical framework: what does economics say about price controls and margins?

Price and margin caps are among the oldest and most politically attractive forms of economic intervention, especially in periods of high inflation or pronounced price shocks. While their proclaimed goal – protecting consumers' purchasing power and ensuring the affordability of essential goods – is clear and socially acceptable, economics has long pointed to the complex, multilayered and often counterproductive consequences of such measures. Moreover, recent research in this area moves away from simple supplyanddemand models, which predict shortages and black markets and a loss of welfare as a basic consequence of market intervention. Instead, the focus is now on more subtle but extremely important mechanisms of market adjustment. These adjustments include changes in product quality, the strategic introduction of new, unregulated products, the passthrough of prices to other market segments (the so-called “waterbed” effect), as well as longterm consequences for investment and innovation. Analyses of these more complex mechanisms show that the real effects of price control are often much deeper and more damaging to overall welfare than first assumed.

A significant theoretical shift in the analysis of price controls was brought about by Casey Mulligan's paper⁴, which challenges the traditional model's assumption that the product is fixed and that firms adjust to regulation primarily by changing quantity. Instead, his paper explores how markets adjust when both quality and quantity are variable outcomes. Methodologically, Mulligan develops a model that decomposes production into market inputs (materials, capital) and inputs provided by the consumer (their time, effort, acceptance of lower quality). In this framework, a price ceiling is not regarded merely as a limitation on the final price but as a constraint on the average price of all “upstream” market inputs that the firm uses. The key conclusion is that price controls change the mix of inputs rather than just the quantity. A price cap encourages firms to substitute more expensive market inputs with cheaper inputs provided by consumers, which in practice is manifested as longer queues, lower service quality or products with cheaper ingredients. This implies that traditional analyses, which measure only the welfare loss due to reduced quantity, considerably underestimate the true social costs of price control because they ignore the loss due to quality degradation – a hidden cost for consumers.

One of the more common strategies used by firms with a broad range of products in response to price regulation is known as the “waterbed effect”. This phenomenon describes a situation where a regulatorinduced reduction in the price of one product leads to a compensatory increase in the prices of other, unregulated products, effectively shifting the burden of regulation onto consumers in another segment of the market. The paper by Christos Genakos and Tommaso Valletti⁵ provides one of the clearest empirical confirmations of this effect in the telecommunications market. Analysing whether a reduction in regulated wholesale prices (so-called calltermination rates) leads to an increase in retail prices for endusers, the authors arrived at an unambiguous conclusion. On the basis of a panel econometric analysis of mobileoperator data in more than twenty countries, they showed that the “waterbed” effect is real and economically significant. Their results suggest that a 10 % reduction in the regulated price led to an average increase in retail prices to users of between 5 % and 10 %.

4 Mulligan, C. B. (2024). *Equilibrium Responses to Price Controls: A Supply-Chain Approach*. NBER Working Paper 32216.

5 Genakos, C., & Valletti, T. (2011). *Testing the 'waterbed' effect in mobile telephony*. *Journal of the European Economic Association*, 9(2), 315–347.

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The next important question that has arisen is whether advances in technology that enable sophisticated price monitoring have eliminated some of the traditional problems of pricecontrol policy. An important insight into this topic is provided by the study by Alberto Cavallo and Diego Aparicio⁶, which analyses a modern, “smart” version of this measure in Argentina – targeting specific products identified by barcodes and backed by technology that enables monitoring by consumers. Analysing a unique dataset on daily prices and availability for over 50 000 items, the authors came to three important conclusions. First, contrary to classical expectations, widespread shortages were largely avoided, thanks partly to more efficient oversight enabled by technology. Second, the impact on overall inflation was small and temporary; although the prices of controlled products were lower during the life of the measure, this effect was largely neutralised by their increase immediately after the controls were lifted. Third, and most important, the study confirmed a key adjustment mechanism: firms circumvented the regulation by introducing new, similar products (with new barcodes) at higher, uncontrolled prices. This shows that although technology can solve the monitoring problem and reduce the risk of shortages, it cannot eliminate the fundamental incentive for firms to adjust strategically and protect their profit margins.

The broader economic consequences of price controls have been analysed in detail in the World Bank study entitled *Price Controls: Good Intentions, Bad Outcomes*.⁷ This study, which combines a review of the existing literature with an analysis of a unique dataset on the prevalence of such measures in WTO member countries, examines the real economic consequences of policies that are often implemented with the goal of social protection. The report’s conclusions are unambiguous: despite good intentions, price controls systematically undermine investment and economic growth, worsen poverty, create a significant fiscal burden for the state and make it difficult to conduct effective monetary policy. The report explains that these measures lead to inefficient resource allocation and reduce incentives for investment by domestic and foreign enterprises. In practice, this often turns into unsustainable subsidy systems, where the state has to cover producers’ losses (particularly in the energy sector and agriculture) to maintain supplies at artificially low prices, potentially creating great pressure on public finances. For these reasons, the World Bank concludes that targeted social programmes, such as direct cash transfers or vouchers for the most vulnerable households, are a far more efficient and equitable mechanism of protection than general and nonselective price controls.

Particularly important for understanding food price movements in CEE in recent years are studies of the asymmetric passthrough of prices along the supply chain. A study by the Hungarian Centre for Economic and Regional Studies⁸ directly analysed this phenomenon on the pork market in Hungary, in a period that included government pricecontrol measures. Using advanced econometric methods, the study found the existence of longrun asymmetry: increases in producer prices are quickly and fully passed through to consumers, but when farmgate prices fall the benefit is not transmitted to retail prices either as quickly or to the same extent. This finding indicates the presence of market power in the processing and retail sector, and an important finding is that even government pricecontrol policy did not manage to eliminate this structural inefficiency. That this is not unique to Hungary was confirmed by the work of Rezitis and Tsionas, which provides a broader, panEuropean context.⁹ Their results unequivocally confirm the existence of the phenomenon known as “rockets and feathers” (prices rise quickly like rockets and fall slowly like feathers) as a systemic feature of the European food market, where retail prices respond more strongly and faster to increases than to decreases in purchase prices.

These findings have profound implications for pricecontrol policy. The existence of asymmetric price passthrough points to significant market power in the intermediate and final segments of the supply chain, such as processors and large retail chains. In such an environment, introducing caps on retail margins can be particularly problematic. While the government tries to limit the margin in retail, actors with market power further upstream can absorb all the benefits of any fall in the prices of raw materials, preventing them from being passed on to consumers and thus nullifying the purpose of the intervention. This suggests that administrative measures alone are insufficient if the structural factors that allow such behaviour – above all high market concentration – are not addressed at the same time.

This brief review of recent papers provides a coherent picture of the expected effects of price and margin caps. Research consistently shows that although these measures can provide the appearance of shortterm stability, they trigger a series of market adjustments that undermine their stated goals in the long term. The main mechanisms identified in the li-

6 Cavallo, A., & Aparicio, D. (2018). *Targeted price controls on supermarket products*. NBER Working Paper 24275.
 7 World Bank. (2020). *Price controls: Good intentions, bad outcomes*. In *Global Economic Prospects*, January 2020: Slow Growth, Policy Challenges (pp. 51-60). World Bank.
 8 Bareith, T., Fertő, I., & Podruzsik, S. (2025). *Price transmission in the Hungarian pork market*. *Agricultural and Food Economics*, 13(1). <https://doi.org/10.1186/s40100-025-00353-x>
 9 Rezitis, A. N., & Tsionas, M. G. (2019). Modeling asymmetric price transmission in the European food market. *Empirical Economics*, 57(5), 1545–1569. <https://doi.org/10.1007/s00181-018-1510-x>

perature include changes in quality and product range, price spillovers to unregulated products (the so-called waterbed effect), a reduction in longterm investment and innovation, and, in extreme cases, shortages. Several common themes run through the studies reviewed. The first is the tradeoff between shortterm relief and longterm inefficiency. While price controls can temporarily curb the rise in the prices of certain products, they do so at the cost of distorting market efficiency, reducing incentives for production and sometimes at significant fiscal cost. The second key theme is the importance of market structure. In markets with high concentration and significant market power – a common situation in food retail – actors can use their position to neutralise benefits to consumers. The third and most important theme is the central role of prices as an information mechanism. All studies confirm that suppressing price signals is the root of the problem; prices convey essential information on scarcity, encouraging rational consumption and adequate supply. When that mechanism is blocked on a lasting basis, resources can be misallocated along the entire supply chain.

Finally, the natural question arises: if economists have been warning of the harmfulness of price controls for decades, why is the measure still so popular? An important behavioural economics explanation is provided by the paper by Dal Bó and coauthors,¹⁰ which investigates how understanding economic tradeoffs affects public support for price regulation. Through a survey experiment, the authors showed that citizens have strong, almost innate moral objections to sudden price increases, considering them fundamentally unfair and exploitative. However, the experiment also revealed a key nuance: support for regulation drops markedly when respondents are informed about the economic tradeoff – namely, that higher prices can stimulate additional supply and thus more quickly resolve a shortage.

Nevertheless, even after the explanation, a significant gap remains between utilitarian economic reasoning (which favours efficiency) and the moral intuition of the public (which favours fairness). This gap reveals the paradox of pricecontrol policy. On the one hand, economic analysis consistently shows that price controls are an expensive and inefficient response to supplyside shocks. On the other hand, behavioural analysis shows that the public instinctively demands such measures because it perceives them through the prism of fairness, not efficiency. Politicians, responding to an electorate guided by strong moral intuitions about “fair prices”, often implement pricecontrol policies that economists see as harmful, which explains their persistence despite the abundance of evidence about the shortcomings of such measures.

How these theoretically predicted mechanisms and distortions are manifested in practice is best illustrated by case studies from the immediate neighbourhood. The experiences of Hungary and Romania with administrative control of prices and margins in recent years provide a valuable insight into the practical implementation and real consequences of these policies in the modern European context.

Case studies: experiences in Hungary and Romania with limiting retail margins

Hungary represents the most pronounced example of the prolonged and comprehensive use of administrative price controls in the European Union. Its policy can be divided into two clearly defined phases: an initial phase of direct price freezes, which produced dramatic consequences, and a later phase of moving to a more subtle – yet still highly interventionist – model of capping retail margins. The first phase began on the eve of the 2022 parliamentary elections, when Prime Minister Viktor Orbán’s government, faced with rising inflation, decided on the radical step of freezing the prices of petroleum products. In February 2022 this policy was extended to basic staples. The prices of six key products – granulated sugar, wheat flour, sunflower oil, pork leg, chicken breast and UHT milk – had to be returned to the level of 15 October 2021. This measure was extended several times, and the list of products was later expanded to include eggs and potatoes. After the fiasco with the fuelprice freeze¹¹ and confronted with galloping food inflation, which reached almost 50 % yearonyear in December 2022, the Hungarian government changed strategy in March 2025¹² and moved to the second phase – capping profit margins in retail.

The new strategy was spelled out in a decree that limited retail margins to a maximum of 10 % for roughly 1 000 essential food products grouped into 30 categories. The obligation applied to all retail chains with annual turnover of more than one billion forints (about €2.5 million), and the move was justified with the claim that retailers were applying “unacceptably high” and “unjustified” margins. Given that the exemption threshold was set quite low, it can

10 Dal Bó, E., Finan, F., Exley, C. L., & Safarik, B. (2022). *Is the price right? The role of economic trade-offs in explaining reactions to price surges*. NBER Working Paper No. 30737.

11 Fuel prices were fixed well below market levels, which simultaneously discouraged imports (because they became unprofitable for foreign suppliers) and stimulated excessive demand, including so-called “fuel tourism” from neighbouring countries. A combination of falling imports, the overburdening of domestic company MOL’s capacity and artificially increased demand led to a logistical collapse, mass shortages at many filling stations and panic buying, forcing the Hungarian government to abruptly abolish the measure in December 2022.

12 It is important to note that at the time the new measure was introduced, yearonyear growth in food prices had already been reduced to around 6 %.

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be concluded that the intention was to cover virtually the entire retail sector in the country. Encouraged by the initial results (food prices fell on average by almost 3 % in April 2025 compared with March), the Hungarian government expanded the scope of the measure already in May, introducing a 15 % margin cap on a wide range of drugstore and household products such as soaps, detergents and diapers, specifically targeting large drugstore chains (such as DM, Rossmann and Müller). In addition, extra obligations were imposed on retailers: they had to hold in stock at least the average daily quantity of products sold in 2024, and the share of privatelabel products within regulated categories was not allowed to rise above the level at the start of 2025.

The application of pricecontrol measures in Hungary immediately provoked deep divisions and controversy among economic actors and policymakers. The sharpest split was between the government and the Hungarian National Bank. While the government claimed that the measures protected households and reduced overall inflation by 5–6 percentage points, the central bank’s governor expressed the diametrically opposite view – that the measures actually increased inflation by an additional 3–4 percentage points.¹³ His argument, supported by many economists, was based on the “waterbed” effect: faced with losses on regulated products, retailers were forced to offset them by raising prices on other, unregulated items. The negative consequences for the business sector were tangible. Large retail chains reported significant financial losses, and the Spar chain estimated its losses at about 10 billion forints (approximately €24 million) solely as a result of the pricefreeze measures. Food producers faced different but equally serious problems. The 10 % cap on retail margins effectively made their purchase prices – until then a business secret – publicly available. This undermined their negotiating position and prompted retailers to turn to cheaper imported alternatives in order to maximise profit within the legal framework, putting domestic producers at a disadvantage.

Hungary’s experience confirms that administrative measures caused a series of classical market disruptions predicted by economic theory. Because prices were frozen at artificially low levels, demand for regulated products exploded, leading to shortages and rationing. Retailers reported selling three times more of certain items than usual – for example, during the summer they sold an entire year’s worth of sugar. To prevent shelves from being completely emptied, many stores were forced to introduce quantity limits per customer on their own initiative. The measures also had an unexpectedly strong impact on small retailers. Although formally exempt from the obligation to apply the measures, independent retailers could not compete with the artificially low prices in supermarkets, which led to a drastic drop in sales and pushed them to the brink of survival. The deepest insight into the inefficiency of the measures was provided through confirmation of asymmetric price passthrough in the previously mentioned study of the Hungarian Centre for Economic and Regional Studies. Since the main cause of this phenomenon is the high concentration of the market and the dominant position of large processors and retail chains, the study concluded that administratively fixing prices does not solve the underlying problem but only temporarily masks the symptoms, while the structural inefficiency of the market remains untouched.

It is important to note that the Hungarian government’s change of strategy, from direct price freezes to a more subtle mechanism of margin caps, does not represent a step toward market liberalisation but a tactical adaptation. Direct price freezes, especially on fuel, led to very visible and politically damaging consequences such as shortages and long queues. The government needed an instrument that would retain the popular narrative of “protecting families” but whose negative consequences would be less obvious to the wider public. Capping margins meets that criterion: prices can still fluctuate, avoiding absolute shortages, but the government retains the appearance of control. The negative effects – such as pressure on retailers’ profitability, a reduction in investment or a switch to cheaper imported raw materials – are longterm and harder to directly attribute to government policy in the eyes of the average voter. Thus this evolution represents a move to a politically more sustainable and more easily defensible model that is nonetheless still highly interventionist.

Unlike Hungary, which experimented with different models, Romania opted from the outset for a single but very specific mechanism – capping margins along the entire supply chain. This approach, although less dramatic in its consequences than Hungary’s price freezes, provoked fierce debate and strong opposition from business. In August 2023 the Romanian government introduced an emergency ordinance capping retail margins on basic food products. Although the measure was intended as temporary, it was extended several times, and its key feature is its layering, because it prescribes maximum margins for each link in the supply chain. Initially the measure applied to 14 groups of basic food products,¹⁴ and the list was later expanded to products such as cream, butter and cream cheese.

¹³ <https://centraleuropeantimes.com/hungarian-central-bank-chief-attacks-orban-governments-economic-policy-again/>

¹⁴ Bread, fresh cow’s milk (1.5 % fat), Telemea cheese, yoghurt, white wheat flour, corn flour, eggs, sunflower oil, fresh chicken and pork, fresh fruit and vegetables, white potatoes and white sugar.

The Romanian model of capping retail margins is defined as follows:

- **Processors.** The maximum permitted margin amounts to 20 % relative to the cost of production.
- **Distributors** (cumulatively). The total margin across the entire distribution chain, regardless of the number of intermediaries, is capped at 5 % relative to the purchase price.
- **Retailers.** The maximum margin in retail is capped at 20 % relative to the purchase price, to which direct and indirect operating costs can be added.

Another significant difference from the Hungarian case is that the introduction of this measure in Romania provoked an almost unanimous and very strong backlash from the entire food industry and the retail sector. The employers' association in the food industry (Romalimenta) characterised the government's plan as potentially "catastrophic", warning that capping margins would jeopardise supplies, reduce product quality and lead to job losses. Particular concern was expressed in important export sectors, such as the meat industry, whose representatives claimed that the measure would reduce their competitiveness in the international market and discourage investment in modernisation. Retailers also expressed concern and called for a detailed impact study before further implementation, fearing that the cap might disrupt the market, causing more harm than good in the long run. The climax of the conflict came when the Romanian government announced a plan to extend the margincap system to all domestic food products. This proposal met strong opposition from the entire business sector, led by the umbrella employers' organisation Concordia. Faced with arguments that such a move would violate the principles of a market economy and would be practically unenforceable, the government eventually abandoned the plan. Instead of unilaterally imposing measures, a compromise was reached, and a joint pricemonitoring commission was formed, consisting of representatives of the state, processors and retailers, with the aim of controlling price movements through dialogue among all interested parties.

There is consensus among the various actors in Romania, including the Government and the Competition Council, that the margincap measure achieved its immediate goal – the prices of the covered staple products did indeed fall initially, by an estimated average of between 20 % and 30 %. However, the Competition Council has from the outset pointed to the other side of the coin – although the prices of the targeted products were lower than they would otherwise have been, this simultaneously resulted in higher prices for other, unregulated products. This can be seen from the movement of monthly inflation for the whole group of food products in the consumer price index, which after the introduction of the measure in August 2023 fell only once, by about 3 %.¹⁵

Quantitative confirmation of the measure's limited reach was provided by an independent study by the FriedrichEbertStiftung.¹⁶ The analysis showed that some products in large retail chains did indeed fall in price between September and December 2023, ranging from 10 % (chicken) to as much as 45 % (fresh onions). However, the authors emphasised that it is practically impossible to quantify precisely how much the measures themselves contributed relative to other factors affecting the prices of the products in question. Still, the more important conclusion of the study is that the margincap measure on food evidently had a relatively modest positive effect on the budget of the average household, contributing savings of only 0.6 % of the total value of the consumer basket. By comparison, the previous cap on energy prices had a far greater impact, reducing costs by 10.4 % of the basket's value. These results suggest that although it is a politically visible and popular measure, the contribution of caps on margins in the food supply chain to relieving the population's budget may be quite limited.

Finally, Romania's experience with lifting longstanding caps on prices in the energy sector serves as a strong warning of yet another consequence of prolonged administrative price controls. Romania had for years had a complex and costly system of capping gas and electricity prices for households, but after pressure from the European Commission, the government had to dismantle this system for electricity on 1 July 2025. The consequences were immediate and dramatic: according to Eurostat, prices in the group "electricity, gas, heating and solid fuels" jumped almost 20 % instantly, adding one percentage point to overall inflation. This event clearly illustrates the phenomenon of suppressed inflation, which indicates that prolonged administrative measures do not eliminate inflationary pressures, they merely temporarily mask them. When such measures are finally lifted, accumulated pressures are unleashed at once, creating a price shock that in extreme cases can destabilise the economy and severely hit consumers.

When we summarise the experiences of Hungary and Romania, comparative analysis reveals fundamental similarities in the challenges they faced but also significant differences in approaches and outcomes. Although both countri-

¹⁵ A similar conclusion can be drawn indirectly from Graph 2. The rise in food prices in Romania was noticeably lower than in Hungary and Serbia, but it did not diverge from the average of CEE countries, most of which did not implement similar pricecontrol measures for food products.

¹⁶ Didiță, M.-E., & Surdea-Hernea, V. (2024). *Price caps in Romania. What was the impact of the government's measures?* Friedrich-Ebert-Stiftung Romania. <https://romania.fes.de/e/price-caps-in-romania-what-was-the-impact-of-the-governments-measures>

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es had the same declared goal – protecting citizens’ living standards from inflation – their paths differed markedly. Hungary applied a “shock therapy” approach, starting with aggressive freezes on energy and food prices. This quickly led to dramatic and publicly visible negative consequences, above all a collapse in fuel supply, forcing the government to change strategy and tactically retreat to a margin cap measure less prone to causing outright shortages. Romania, on the other hand, from the beginning applied a more complex model of caps along the entire value chain, thereby avoiding the worst scenarios of shortages. However, it faced strong and organised opposition from industry, which ultimately limited the government’s ambitions and forced it to seek dialogue and compromise. Thus, while the Hungarian government managed to unilaterally impose its will on business, the Romanian government had to modify its policy by taking account of business arguments.

We also observe that both countries, despite differences in approach, faced the same set of negative, unintended consequences that fundamentally call into question the effectiveness of such measures. The most important common consequence was the waterbed effect. In both cases, economic actors responded to lower profits on regulated products by raising prices on unregulated goods. This phenomenon was explicitly confirmed by the highest economic authorities in both countries – the governor of the Hungarian central bank and the chairman of the Romanian Competition Council. Consequently, although the prices of certain items in the basket fall, the total cost of shopping for a household does not necessarily decline, calling into question the net effect of the measures on overall inflation and the real household budget. The experience of both countries also emphasises that administrative measures are ineffective in addressing structural problems in the market. In conditions of high market concentration in processing and retail, there is asymmetry in price passthrough – cost increases are passed through to consumers quickly, while reductions are not passed through to the same extent. Price caps do not solve this problem; they merely temporarily conceal it, leaving consumers exposed to market inefficiencies in the long term.

Lastly, it is important to note that in both countries the measures were heavily promoted as a tool to protect citizens, sometimes with clear political goals, such as the preelection period in Hungary. However, their economic sustainability is highly questionable, because they operate as a mechanism for temporarily suppressing inflation. Experience with lifting the measures (fuel in Hungary, electricity in Romania) clearly illustrates the risk that suppressed inflation may be released with even greater force when the measures are lifted, leading to a sudden price shock.

In essence, price control measures in Hungary and Romania were not a cure for deeper economic problems but merely symptomatic therapy. Both countries faced significant structural challenges: Hungary had high inflation and large budget and trade deficits, while Romania had a large budget deficit and wage growth that significantly exceeded productivity growth. In such a macroeconomic context, price control is a politically attractive way to create the appearance of addressing the cost of living crisis without implementing the harder and unpopular – but necessary – structural reforms such as fiscal consolidation, improving the business environment or strengthening antimonopoly bodies.

What can Serbia expect from a policy of limiting retail margins?

Based on a detailed analysis of the experiences of Hungary and Romania, it is possible to formulate wellfounded predictions about the possible effects and consequences of applying a similar price control measure in Serbia. The main lessons learnt in neighbouring countries reveal that there is clear potential for shortterm benefits but also long-term risks and structural damage that this policy can cause if its duration is prolonged. The first and immediate consequence that can be expected is a moderate fall in the prices of part of the products covered, which may bring some relief to consumers. However, the final net effect on overall inflation and household budgets depends on the specifics of the Serbian model for capping retail margins, which can be described as a hybrid of the Hungarian and Romanian models and has its strengths and weaknesses relative to the measures taken by neighbouring countries. Bearing this in mind, our preliminary analysis indicates that the new measure should lead to a fall in the prices of some of the covered products, but its effect on overall inflation trends will not be dramatic or longlasting – similar to what happened in Hungary and Romania.

An argument supporting the thesis that the effect in Serbia may be stronger than in neighbouring countries is the very wide coverage of products. According to statements by the Minister of Finance, the measure will cover as many as about 20 000 items, which is a significantly wider scope than in Hungary and Romania. By covering such a broad range of products, the Government has effectively narrowed the space for the waterbed effect, because retailers will have fewer opportunities to offset lower margins on regulated products by raising prices on the remaining small number of unregulated items. Additionally, the Regulation contains a provision that margins cannot be raised up to the prescribed maximum of 20 % if they were lower before it came into force, which further strengthens its potential.

On the other hand, some factors suggest that the ultimate effect could still be somewhat modest. First, a retail margin cap of 20 % represents a less restrictive threshold compared with Hungary (10 % for food products) or Romania, which capped margins along the entire food supply chain. Namely, a survey by the Statistical Office of the Republic of Serbia (SORS) in 2023,¹⁷ on a sample of 31 basic food products,¹⁸ showed that the average retail margin on these items amounted to a relatively low 14.9 %. That is well below the upper limit of 20 %, which apparently will neither be binding nor lead to a dramatic reduction in the prices of most basic food products. The results of this survey lead to the conclusion that domestic large retail chains in this market segment somewhat follow the usual practice of major European retail chains, which base profitability on relatively low margins but large turnover.

Perhaps the most important insight from the SORS study is that in Serbia the largest margins in the food supply chain are not found in retail but in the processing sector. According to data from this study, food processors in 2023 had an average gross margin (54.1 %) 3.6 times higher than retailers (14.9 %). This result is broadly in line with general trends in the European food market, because the analysis by EuroCommerce and McKinsey¹⁹ showed that the average gross margin of the seven largest food manufacturers in 2023 was 52.2 %.²⁰ Considering that the Government of Serbia's Regulation focuses primarily on retail and wholesale, and does not directly touch the high margins in the processing industry, its reach in reducing final prices for consumers is structurally limited. With such margins along the supply chain in the food industry and retail, the model applied by Romania would certainly have had a much greater effect on reducing food prices in Serbia than the existing one.

Comparative analysis of the legal solutions in Serbia, Hungary and Romania reveals a few more advantages and disadvantages of the domestic model that influence the overall effectiveness of the measure itself. Two characteristics make the Serbian Regulation potentially more robust. First, the domestic Regulation is specific because it very precisely regulates and caps the total fees and rebates that a retailer can charge the supplier (a limit of 10 %, with special limits for logistics and writeoffs), which was not the case in Hungary and Romania. This closes one of the obvious “loopholes” for circumventing the substance of the measure. Second, the Serbian Regulation contains a provision that the supplier's invoice price may not be higher than the price that applied on 1 August 2025. This measure directly prevents processors or importers from simply raising their price to the retailer. Unlike Romania, where the government directly prescribed a maximum margin for processors (20 %), the Serbian government has indirectly forced them to absorb any increase in production costs and accept a lower margin than the one charged before the Regulation was adopted.

On the other hand, the domestic solution is weaker in terms of preventing other forms of strategic adjustment by retailers. The Hungarian decree, as we have seen, contained very specific “antiadaptation” clauses: the obligation to maintain minimum stocks and a ban on increasing the share of privatelabel products. The Serbian Regulation, by contrast, contains a less precise provision that retailers are obliged to ensure the “unhindered supply” of regulated products. This leaves retailers in Serbia more room to adjust, such as slightly reducing the availability of regulated, lowprofit products (without formally violating the rules) or more aggressively promoting their own, more profitable brands, whose share is not capped as in Hungary.

Although we do not expect the new Regulation to dramatically slow overall inflation, its impact on the operations and profitability of Serbia's retail sector could be extremely unfavourable, even in the short run. Profitability in food retailing is a complex equation that starts with the gross margin but essentially depends on a firm's ability to manage operating costs efficiently in order to ultimately achieve a net profit. According to industry data, the typical cost structure in European retail is quite tight: out of every €100 of revenue, about €70.20 goes on the purchase of goods and over €28.20 on operating costs (rent, labour, energy, logistics), leaving only about €1.60 as net margin.

Gross margin, defined as the difference between revenue from sales and the purchase value of goods (Gross margin = Revenue – Purchase value of goods), is the first indicator of the pricing power and procurement efficiency of a retail chain. According to available data (Graph 3), gross margins of leading retail chains in Serbia in 2024 ranged from about 25 % (Lidl) to over 34 % (Super Vero), with an average of about 29 %. That is somewhat above the ave-

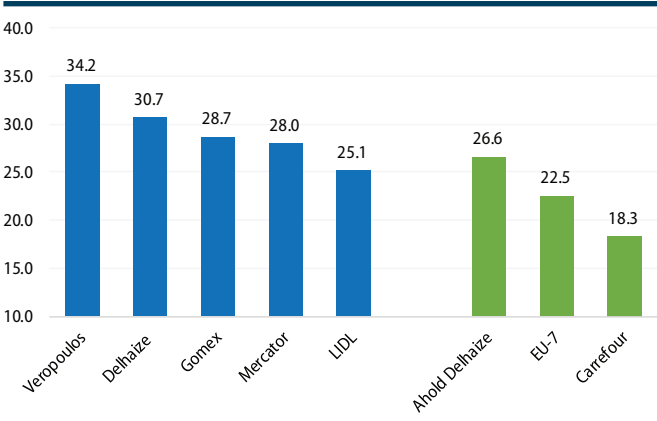
17 Kovačević, M., Stevović, M., & Šutić, V. (2023). *Research on margins in trade and the food industry and their impact on food price inflation in Serbia*. Trends, Q4 2023. Republic Statistical Office.

18 These products were grouped into eight analytical groups: fresh vegetables; fish; milk, cheese and eggs; oils and fats; bread and cereals; fresh pork; fresh chicken; and coffee and sugar.

19 EuroCommerce, & McKinsey & Company. (2024). The state of grocery retail 2024: Signs of hope. <https://www.mckinsey.com/industries/retail/our-insights/state-of-grocery-europe-2024-signs-of-hope>

20 EuroCommerce, & McKinsey & Company. (2024). The state of grocery retail 2024: Signs of hope. <https://www.mckinsey.com/industries/retail/our-insights/state-of-grocery-europe-2024-signs-of-hope>

Graph 3. Average grossmargin rate of retail chains in Serbia and the EU (%)



Source: author's calculation based on data from companies' financial statements for 2024 for Serbia and EuroCommerce & McKinsey (2024) for European retail chains.
Note: EU7 represents the average gross margin of seven European retail chains: Ahold Delhaize, Carrefour, ICA, Axfood, ELO S.A., Kesko, DIA, Jeronimo Martins and Sonae Retail.

large range of products and additional services (bakeries, delicatessens). Such a model inherently carries much higher operating costs, which is why, to make a profit, these retail chains usually rely on achieving somewhat higher gross margins. Ultimately, the margin structure also depends on the competitive environment in each individual country in which the retail chain operates.

A higher average gross margin in Serbia, as we have seen, can partly be explained by the dominance of the traditional supermarket format, but it is likely also partly the result of insufficient competition in the domestic retail market. Whatever the reasons, the fact is that the business model of domestic retail chains rests on gross margins of 25–30 %. Imposing a maximum margin of 20 % on a large part of their assortment – according to initial estimates, as much as 70–80 % – represents a strong blow to their profitability. Given that the wide coverage of products significantly narrows the space for the waterbed effect, savings will likely be sought on the side of cutting operating costs. Since wage expenditure is one of the key components of operating costs, one of the accompanying negative consequences of the Government's margincap decree could easily be a reduction in employment in the retail sector. This is particularly so because pressure on labour costs will be further intensified by the Government's decision to first increase the minimum wage by 9.4 % from October this year and then by another 10.1 % from January 2026. Faced with a simultaneous drop in revenue and a rise in costs, retailers may be forced to lay off workers. A particular problem is that the cumulative increase in the minimum wage of over 20 % in just three months will contribute to strengthening overall inflationary pressures in the economy, which in conditions of strict price control could further worsen market imbalances.

In a more extreme scenario, especially if the application of the Regulation were to be extended beyond the initial sixmonth period, some retail chains might look for savings by rationalising their sales network, that is, by closing less profitable outlets. Paradoxically, this could lead to a further weakening of competition in Serbia's retail market, especially in smaller towns. Thus the measure, introduced to correct the consequences of insufficient competition, could ultimately become a factor that further undermines competition.

If this measure were to last longer, a host of serious structural risks would open up. The first relates to disruptions in the supply chain. Faced with frozen purchase prices and the inability to pass on any rise in their own costs, producers, processors and importers may reduce or completely halt deliveries of regulated products. For consumers, this would mean a narrower assortment in stores and a potential decline in product quality, as producers would be forced to use cheaper inputs in order to preserve profitability. For the domestic economy, this carries the danger of increased reliance on cheaper imported products, because retailers will look for suppliers who can offer them lower purchase prices. The second major risk is investment uncertainty. Administrative interference in price formation creates an unpredictable and unstable business environment, which directly discourages longterm investment in agricultural production, processing capacity and the modernisation of the retail network. As the World Bank's comprehensive analysis confirms, price controls systematically undermine investment and economic growth because companies are less inclined to invest when there is a risk that the state will cap their ability to earn at any time. Finally, the measure

range of the leading European chains, which was 22.5 %. However, there are chains in Europe that operate with similar margins; for example, Ahold Delhaize at European level has a gross margin of about 27 %, which does not differ drastically from the margin of the same chain in Serbia (around 30 %).

Differences in gross margins between individual chains are not random but represent the direct result of their different business models, strategic choices and the specifics of national markets. Two dominant models explain most of the variation. The first is the discount model (e.g. Lidl), which is built on extreme operational efficiency and is characterised by a significantly limited number of items with a large share of private labels, which simplifies logistics, reduces waste and allows lower operating costs through smaller sales areas and a "nofrills" product presentation. The second is the traditional supermarket model, based on offering a wide selection, with a

not only fails to solve existing structural problems in the market but may even make them worse. If, as is assumed, there is a significant degree of concentration in Serbia's retail market, administrative measures do not resolve the underlying problem of asymmetric price passthrough. On the contrary, a fall in profitability could push some market players to reduce their operations in Serbia, which could lead to even greater market concentration and weaker competition in the future.

Given the negative experiences of neighbouring countries and the risks we have pointed out, the Government of Serbia should consider more effective and less harmful measures than general price controls. Instead of administrative measures that distort the market, the focus should be on addressing the fundamental causes of inflation. This primarily includes strengthening competition through more active work by antimonopoly bodies to prevent the abuse of dominant positions and addressing structural problems such as the low productivity of the food industry, which forces companies to operate with high producer margins, or the longstanding trend of wages growing faster than productivity. In addition, instead of general measures that benefit wealthier citizens as well, a fairer approach would be targeted support for the most vulnerable households through mechanisms such as direct financial assistance or food vouchers.

Since the Regulation is already in force, it is crucial to manage its risks. The measure was introduced without an open and constructive dialogue with the part of business most affected, which is the wrong approach. Therefore it is now vitally important for the measure to have a clearly defined and strictly limited duration. The experiences of Hungary and Romania show that temporary measures are often extended, which multiplies negative consequences. To avoid such a scenario, the Government should already have a prepared, gradual exit strategy, in order to avoid a painful price shock when the measure is withdrawn – of the kind seen in Romania with electricity prices. This is all the more important because, if retail chains operate at a loss over the next six months, once the measure is abolished they will have a strong incentive to make up for lost profits by raising prices aggressively, making the risk of a price shock even more likely.

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