

How are the costs of adapting to Covid reflected in prices?

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In the Monthly Business Survey (MBS) carried out at the end of February/beginning of March 2021, business leaders were asked about the organisational costs associated with COVID and their ability to pass them on to their selling prices. These costs may be high for some sectors but their ability to pass them on to prices appears to be generally limited. Ultimately, the direct and indirect impact on the general level of consumer prices should therefore be small, between 0.1 and 0.3 percentage point, but these costs could affect the margins of some companies.

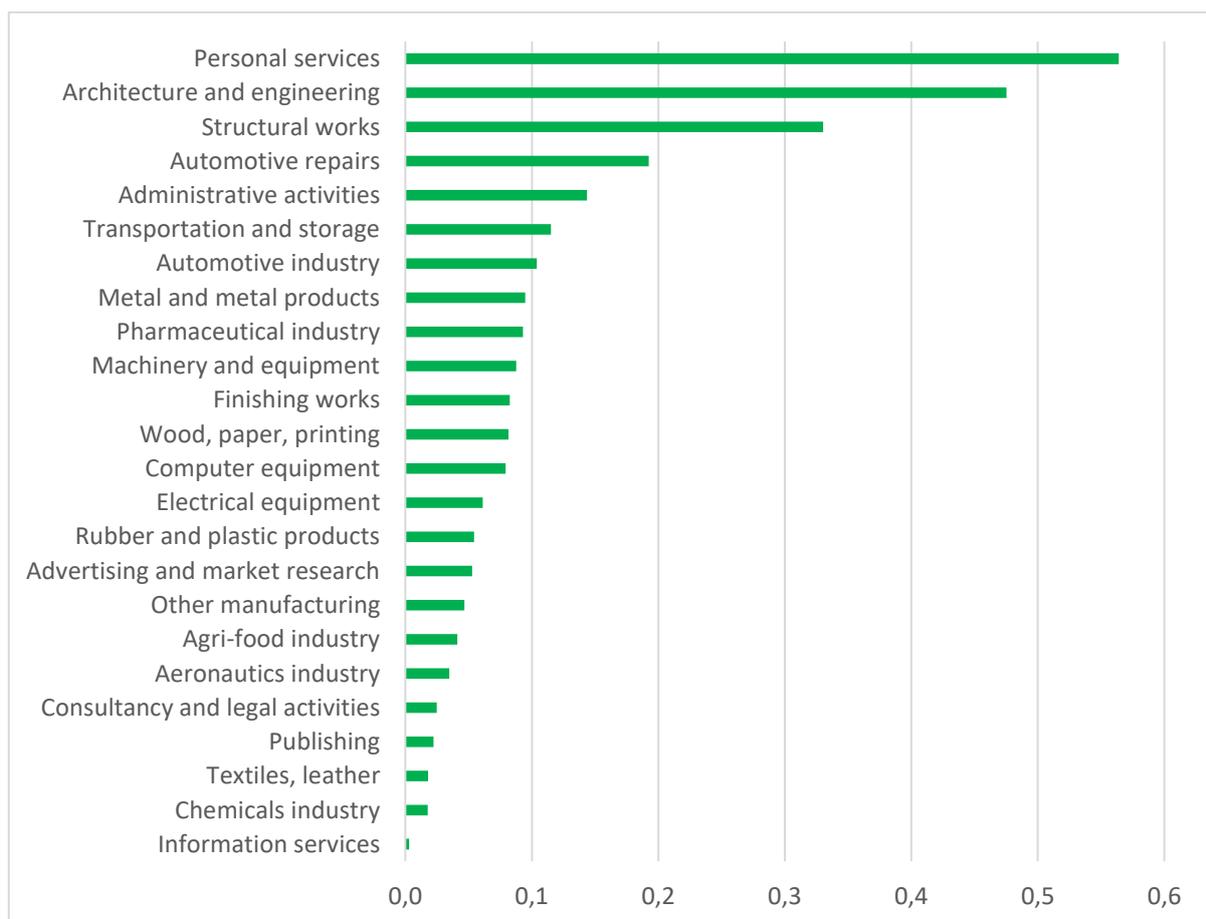


Chart 1: Direct impact on selling prices of the additional costs generated by the health measures

Source: The Banque de France's monthly business survey

Note: In personal services, the average impact of additional costs generated by health measures on the final price paid by customers is 0.56%.

Significant additional costs, particularly in certain sectors where the activity requires direct contact with customers

The first of the two additional questions asked at the end of February/beginning of March to the 8,500 business leaders responding each month to the [MBS](#) concerned the additional cost of the health measures in 2020. This additional cost, expressed in percentage points of 2020 turnover, includes direct costs (purchase of masks, gel, etc.) and indirect costs (compliance with public reception and physical distancing measures), but does not cover external costs (supply problems, drop in demand, raw material costs, etc.).

For most of the sectors covered by the survey, the average additional costs of health measures are estimated to be in the range of 1 to 3% of turnover (Chart 2). At 2% on average, they are much higher in personal services (6% of turnover on average) and in architecture, engineering and technical testing activities (5% of turnover on average), both of which are sectors where meeting the client is essential to the business. The additional costs reported are also more dispersed for these two sectors than for the others, a sign of the differences in the nature of the professions that make up these sectoral aggregates.

Although accommodation and food services fall within the scope of the MBS, they were not surveyed on these matters because they had to close for administrative reasons. However, it is reasonable to assume that these businesses are likely to face similar additional costs to those of the personal services sector because they receive customers.

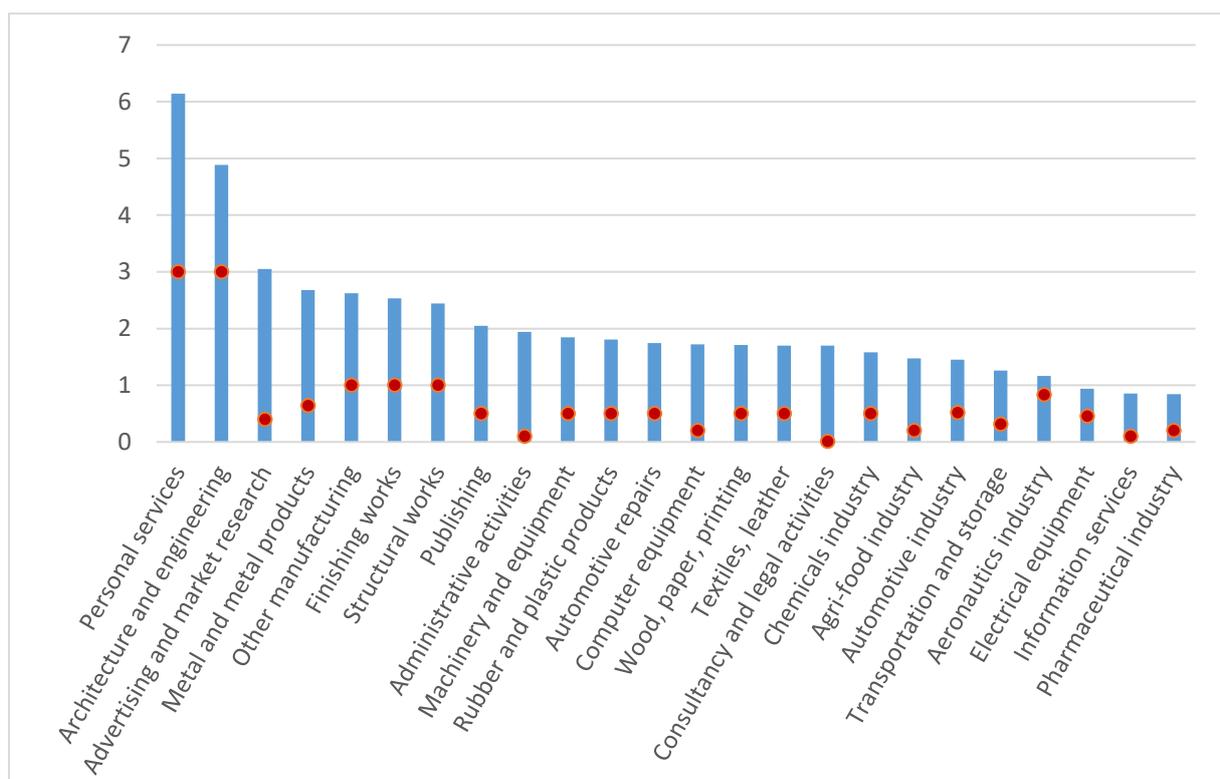


Chart 2: Additional costs of health measures (as a percentage of 2020 turnover)

Source: The Banque de France's monthly business survey

Note: In personal services, the average extra cost (blue lines) is 6% of turnover and the median extra cost (red dots) is 3% of turnover.

Additional costs essentially absorbed through a reduction in firms' margins

The second additional question concerned the extent to which these additional costs will, by the end of 2021, be passed on to the selling price (the answer includes any price increases already passed on in 2020).

Chart 3 shows a median pass-through to prices of zero for all the sectors covered, which suggests that firms have very little capacity to adjust their selling prices. This lack of pass through to the customer implies that businesses absorb almost all of these additional costs by reducing their margins. In contrast, the average impact is strongly positive and stands at 5%, which implies that, for those companies reporting a non-zero pass-through, the impact on the price paid by the customer is relatively high. A maximum of 14% of the additional costs are passed on to the selling price on average in the construction sector; in contrast, in the computer and information services sector, business leaders report an average of zero pass-through, i.e. total absorption of costs through lower margins.

The sum of these two indicators shows the impact on the final price of the additional costs associated with the health measures (Chart 1). Across all sectors, the pass-through is around 0.1% on average (2% extra costs x 5% pass-through). This impact is relatively greater in personal services and architecture activities (due to comparatively higher additional costs), and in construction and automotive repair (due to a relatively higher pass-through rate).

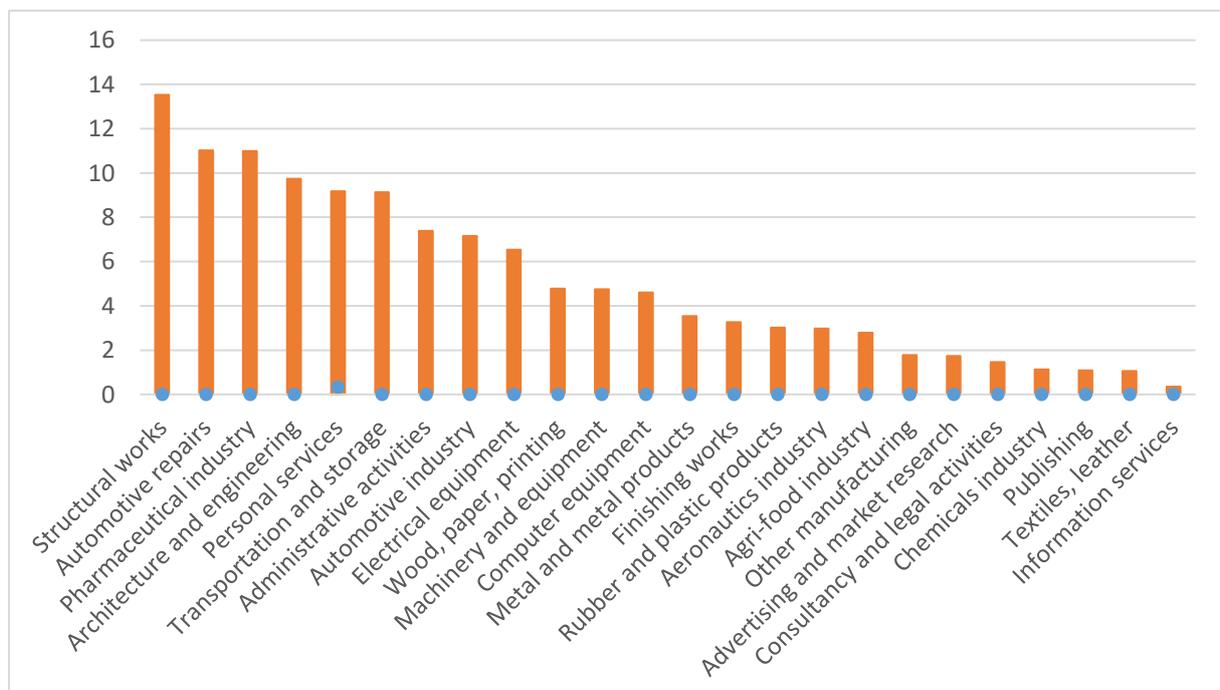


Chart 3: Pass-through rate of additional costs of the health measures to the selling price (%)

Source: The Banque de France's monthly business survey

Note: In structural works, the average pass-through to selling prices (orange lines) is 14%, the median additional cost (blue lines) is zero.

A cost shock also propagates along the production chain

The combination of costs and the pass-through thus results in a direct impact on the price for the company's customer. This can be a final customer (consumer, etc.) but also another company buying inputs. The initial shock will then propagate along the production chain. In order to assess this second channel, we use the symmetrical supply and use tables (SUT) produced by INSEE, which provide the balance between supply (output and imports) and uses (consumption, gross fixed capital formation, changes in inventories, exports) for all the products. These tables therefore make it possible to replicate the sequence of stages in the production process. They also allow us to consider a domestic cost shock, measured in the survey, but also to extend it to the case where our partners experience the same shock and pass it on to import prices.

Furthermore, the responses collected do not cover the whole economy. For most of the sectors not covered (non-market services, energy production, finance etc.), it seems reasonable to assume that Covid costs are zero or negligible. As no data is collected for the accommodation and food services sector, we assume an impact identical to that measured for services to households.

The impact on the general level of consumer prices is estimated to be between 0.1 and 0.3%

Overall, we conduct three assessments (see Chart 4): (i) direct impact; (ii) direct impact plus indirect impact through intermediate consumption; (iii) direct impact plus indirect impact through intermediate consumption and imports.

The direct shock on consumer prices is estimated at around 0.1%. This impact is expected to be concentrated in market services, in line with the raw survey data. Secondly, propagation through intermediate consumption and imports would logically mainly affect goods, thus increasing the potential overall shock to consumer prices to as much as 0.3%.

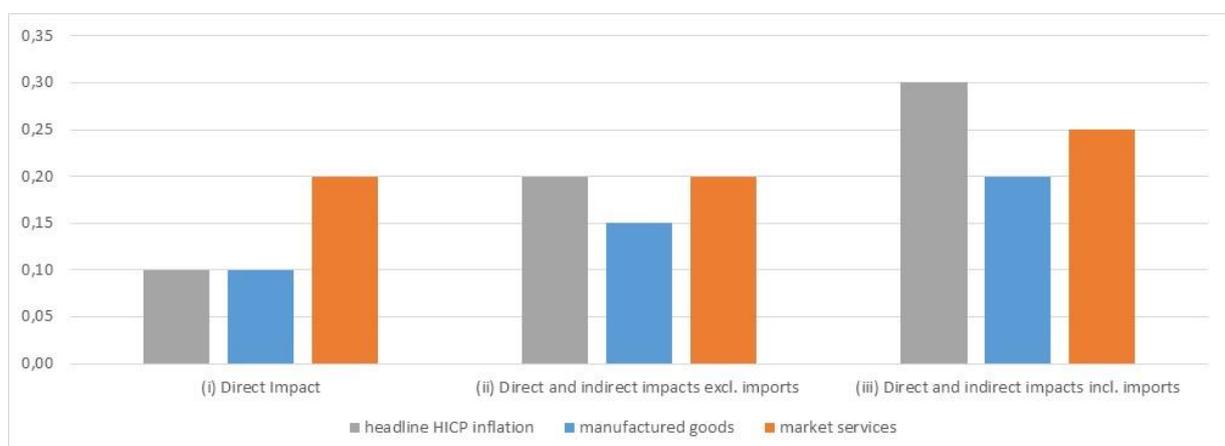


Chart 4: Impact on the level of the harmonised index of consumer prices in France (%)

Source: Authors' calculations.

A few words of caution are required regarding the significance of these results. First, since the questions asked relate to past and future costs, we cannot rule out the possibility that this pass-through to prices has already at least partly occurred. After the first lockdown in May 2020, for example, some atypical price increases were observed for certain services to households (garages, hairdressers etc.). Second, since the companies were surveyed at the beginning of March, we cannot preclude that Covid costs will increase further with the recent tightening of health restrictions. Conversely, it is possible that these costs will diminish in the medium term, assuming a return to "normal", which could then, in turn, temporarily limit price increases. Lastly, the scope of the question posed in the MBS and therefore in this post is deliberately limited to costs linked to the company's own activity (masks, reception conditions, etc.). We do not therefore cover in this post the upward pressure on costs and prices that will result from current price developments for a number of raw materials and, more generally, from the expected global economic recovery.