Journal of Economics, Business, and Commerce (JEBC)

ISSN: 3007-9705 (Online)

Volume 2 Issue 2, (2025)

https://doi.org/10.69739/jebc.v2i2.1120

https://journals.stecab.com/jebc

Published by
Stecab Publishing

Research Article

Impact of Inflation on Firm Profitability: Evidence from Local Companies in Lusaka, Zambia

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About Article

Article History

Submission: October 12, 2025
Acceptance : November 17, 2025
Publication : November 27, 2025

Keywords

Cost Components, Firms' Profitability, Firms' Revenue, Inflation, Pricing, Strategies

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ABSTRACT

The study aimed at analysing how inflation affects the profitability of Zambian local companies. The objectives were anchored on establishing the effects of inflation on firms' revenue, cost components and the strategies used by local companies to minimize the effects of inflation on the profitability of firms. Using Mixed-Methods Approach of qualitative and quantitative, 108 different firms from different industries were engaged in Lusaka, Zambia and analysed using Megastat. The results of the study showed that 96.3% of firm's' revenue is not significantly influenced by inflation. The findings of the study revealed a non-statistically significant association between inflation rate category and firms' average revenue as confirmed by the chi-square test results (x^2=7.94. df=6, p=0.2427). The findings of the study demonstrated a significant impact of inflation on firms' cost of component, with 96.4% of firms reporting to have increased cost components as a due to the increase in inflation. The chi-square test results confirmed an extremely highly statistically significant association between inflation rate category and the firms' average total cost (x^2=39.86, df=6, p=4.85E-07). 78.7% of firms reported that price adjustment is often used as the most effective strategy in mitigating effects of inflation on firms' profitability (x^2=22.63, df=6, p=0.0009). The findings of the study concludes that firms can effectively reduce the impact of inflation on firm profitability through price adjustment strategies. Therefore, it is recommended that local companies in Lusaka, Zambia prioritize price adjustments and regular price reviews to maintain firms' profitability.

Citation Style:

Tembo, B. H., & Silwimba, P. (2025). Impact of Inflation on Firm Profitability: Evidence from Local Companies in Lusaka, Zambia. *Journal of Economics, Business, and Commerce, 2*(2), 260-269. https://doi.org/10.69739/jebc.v2i2.1120

1. INTRODUCTION

1.1. Background of the Study

In sub-Saharan countries, especially in developing ones like Zambia, inflation has caused a lot of struggles in recent years (Prudence, 2024; Mweene, 2020; Kabwe, 2019). Zambia's history of inflation show that it has been volatile between 10% and 20%, with a peak rate of 22.9% in 2016 (BOZ, 2020). The changes in inflation have led to serious economic implications, especially for the local companies in Zambia (Chikazunga, 2018).

Some studies show that inflation can reduce the profitability of firms, especially for manufacturing and retail sector which is more vulnerable to inflation (Kasonse, 2019). Retail firms in remote areas suffer a huge impact from the changes in inflation (Lubinda, 2023). Established literature on the effects of inflation on firms' profitability have revealed mixed findings, suggesting a comprehensive understanding of the underlying causes of the disparity between firms in the local economy (Nugraha *et al.*, 2021).

A study by Chipili (2019) argued that the local companies in Zambia face significant challenges due to the changes in inflation which may include increases on cost components, exchange rate fluctuations and infrastructure constraints such as inadequate transportation networks and energy supply chains (Kasonde, 2019). Firms operating in Lusaka face competition from imported goods and regulatory challenges (Sakala, 2020). These challenges pose a big threat to the competitiveness, profitability and sustainability of local firms in Zambia.

However, despite the side effects of high inflation on firms' profitability in Zambia, other studies established a positive impact attributing to the companies' market power to adjust prices and effective supply chain optimization techniques (Prudence, 2024), suggesting an in-depth investigation on the sources and effects of this discrepancy.

1.2. Problem Statement

Despite the significant impact of inflation on firms' profitability, an observed research gap was noted, aimed at understanding why some companies survive and thrive in Zambia's high inflation environment while others fail (Sakala, 2020, Chipili, 2019). Limited research has explored specific strategies, characteristics and mechanisms that enable some firms to alleviate the negative effects of inflation and maintain profitability, but these findings have been mixed (Kasonde, 2019), an investigation this study seek to address. By understanding the factors that contribute to the resilience and survival of the local companies in Lusaka, Zambia.

1.3. Research Objectives

1.3.1. General Objective

The purpose of this study was to analyse the effects of inflation on firms' profitability of local companies operating in Lusaka, Zambia.

1.3.2. Specific Objective

To achieve the main goal of the study, specific objectives were established which is;

1. To establish the correlation between inflation and firms' revenue in Lusaka, Zambia.
2. To evaluate the effects of inflation on firms' cost components in Lusaka, Zambia.
3. To examine the effectiveness of the strategies used by the local companies to mitigate the effects of inflation on firms' profitability in Lusaka, Zambia.

1.4. Research Questions

i. What is the correlation between inflation and firms' revenue for local companies in Lusaka, Zambia?

ii. How are the changes in firms' cost components influenced by the changes in inflation for the local firms in Lusaka, Zambia?

iii. How effective are the mitigating strategies in managing the impact of inflation on firms' profitability of Zambian local companies?

1.5. Conceptual Framework

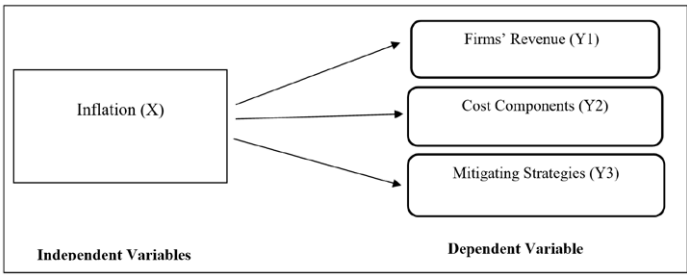

Figure 1. Conceptual Framework

1.6. Significance of the study

The significance of this study is considered highly significant because it focuses on the effects of inflation on firm's profitability, adding to the current body of knowledge, providing new insights and perspectives to policy-makers, businesses and investors. The results generated from this study will help businesses, employees, corporate companies and the government to develop effective strategies to overcome the negative impacts of inflation on firm profitability, enabling them to make informed decisions on pricing, cost management, and stability in order to achieve profitability.

1.7. Scope of study

The study under investigation was conducted from the field of Business and Economics and was necessitated for the fulfillment of a bachelor's degree in Economics and Finance. Much of the attention for this study was centered on analyzing the effects of inflation on the profitability of local companies in Lusaka, Zambia, with a specific focus on the manufacturing, retail, wholesale and financial sector. The key variables of interest included inflation, firms' profitability, firms' revenue, cost components, strategic measures for mitigating inflation and firms' specific characteristics such as company size, years of operation, ownership and industry type to explain the factors associated with these effects.

2. LITERATURE REVIEW

2.1. Inflation and Firms' Revenue

Nugraha *et al.* (2021) in his study of inflation, leverage and company size and their effect on profitability in Indonesia found

that inflation simultaneously affect firms' profitability. Inflation negatively affects firm profitability, especially those with high leverage, as it increases nominal interest rate and reduces firm value (Knox & Timmer, 2024). Firms in concentrated industries are more vulnerable to inflation (Weber & Wasner, 2023). Isma *et al.* (2023) also found that inflation negatively affects firm value. However, Fabiani *et al.* (2025) argued higher leverage firms experience larger stock returns after positive inflation surprises, driven by long-term leverage. A firm can adjust its pricing strategies to account for inflation, leading to increased revenue (Haar, 2024)

Market risk is one of the main drivers that significantly affect corporate performance of financial institutions and other service-oriented firms in the world (Daniel *et al.,* 2023), supported by the findings of Sutisman *et al.* (2024) who found that inflation does not significantly affect stock prices and firm value. It is therefore recommended that to minimize the negative effect of inflation on firms' revenue, firms need to increase their earnings quality (Isma *et al.*, 2023).

Inflation's effect on firms' profitability have been researched in early literature with no consensus around the relationship. Scemeleva *et al.* (2023) investigated how inflation affects firm's financial performance of Central and Eastern Europe (CEE) countries and found mixed results. While studies have revealed contradictory findings on the impact of inflation on companies' revenue, studies in Zambian context found inflation to have a significant impact on Zambia's local economy, ultimately leading to a decrease in firms' revenue (Chidothi & Sheefeni, 2013).

Prudence (2024) in her research study on factors affecting the profitability of Zambian Commercial Banks found that inflation negatively affected the returns, similar to the findings of Muyanga (2019) who found inflation to negatively affect stock market performance in Zambia, which can have a ripple effect on firms' revenue. Inflation can lead to decreased economic activity, particularly if it is driven by supply-side shocks, ultimately leading to reduced demand and affecting firm's revenue (Mishra *et al.,* 2024). Knotek and Zaman (2024) contended that firms with market power are able to adjust their prices and their supply chain making them able to maintain profitability during periods of high inflation.

2.2. Inflation and Firms' Cost of Components

Binici *et al.* (2022) found that post COVID-19 pandemic, global supply chain disruptions led to high inflation and increased costs for intermediate goods. After a series of price moderations, inflation emerge, characterized notably by the large increase in the price of tangible goods (Lane, 2022). Since 2020, the dynamics on the prices of goods have often been explained by a combination of an increase in demand and costs in the European market, mostly on energy prices and foreign input prices (Seiler, 2022, di Giovanni *et al.*, 2022).

Martin *et al.* (2023) established that inflation led firms especially in the manufacturing sector to be under scrutiny and exposed to foreign input cost and energy cost, and this behavior attenuate or amplify the downward transmission of these shocks to consumers. As inflation rises, firms face increases in labor costs due to higher wages and benefits, leading to reduced profit margin (Weber, 2022). Inflation can result in higher cost of raw materials and inputs, making it challenging for firms to maintain their profit levels (Rashid, 2022). However, Rashid (2022) argued that good corporate governance plays a key role in reducing the negative consequences of inflation risks on bank profitability in Pakistan. Firms that are able to adapt quickly to changing supply chain conditions are better able to manage the impact of inflation on firms' cost components (Baldwin & Freeman, 2022).

Inflation poses a significant threat on households, businesses and the government, making it difficult for firms to maintain profitability (Lubinda, 2023). Studies have shown that firms, especially those in the manufacturing sector are more vulnerable to inflation shocks due to increased production costs. It has further been established that firms that rely heavily on imported raw materials prove to be more susceptible to inflation shocks, particularly if they are denominated in foreign currencies (Knox & Timmer, 2025; Fabiani *et al.*, 2024; Muhammad *et al.*, 2023). A study by Haar (2024) offer contradictory findings arguing that the impact of inflation on cost component largely depend on firm specific factors and not inflationary driven.

Muhammad *et al.* (2023) in his study on the rising price of construction materials in Johor Bahru, found that inflation can have a positive significant impact on the cost of raw materials. Inflation can lead to increased cost of raw materials, as higher prices for goods and services can drive up production costs (Mishra *et al.,* 2024). The increase in inflation can result into an increase in the production costs which ultimately could lead to an increase in commodity prices, especially for firms that heavily rely on raw materials (Hamilton, 2009). However, Fabiani *et al.* (2024) argued that these increased costs can be attributed to the companies' specific factors and their ability to manage and diversify their supply chains. Firms that engage in commodity price hedging and supply chain management strategies find it effective in maintaining profitability (Harit, 2025).

Knox and Timmer (2023) found that inflation led to increased cost of raw materials where firms pass on higher prices to consumers. This is more pronounced in those industries that rely heavily on raw materials such as construction, textile and manufacturing companies (Muhammad *et al.*, 2023; Bhattacharya *et al.*, 2019). A study by the IMF (2020) established that a 1 percentage increase in inflation lead to 0.5% increase in material costs.

Fabiani *et al.* (2024) contended that firms with strong supply chain management practices are better able to manage firms' cost of components and mitigate its impact on inflation. The relationship between inflation and cost components can be influenced by various firm specific factors and macroeconomic indicators (Haar, 2024), providing the importance of understanding the repercussions of monetary policy on inflation and firms' revenue and its component costs.

According to a study by Muyanga (2019), it was observed that inflation can have a very significant impact on the cost of living and of doing business, ultimately affecting firms' profitability. For example, in the context of the stock market performance, Inflation is seen to have a negative effect on stock market performance, which can have a ripple effect on firms'

revenue, cost components and profitability, similar to a study by Prudence (2024).

2.3. Strategies in Mitigating Effects of Inflation on Firms' Profitability

A study by Gagliardone *et al.* (2025) found that one of the main reasons why firms adjust output prices frequently is due to changing economic conditions which leads prices to shift from those that maximize profits. Kasonde (2019) in a similar context added, that firms also employ dynamic pricing, financial hedging and digital transformation to adapt to inflationary pressures. However, Knotek and Zaman (2024) argued that these strategies are complex and largely depend on various firm specific factors, suggesting that firms can pass on increased costs to consumers, similar to a study by Bekaert and Wang (2020).

Different studies have established different findings on the effects of inflation on firms' profitability and the strategies used in mitigating these effects. Torres and Salas-Fumas (2023) maintained that price adjustments are a common strategy for firms to curb the effects of inflation on firms' profitability. Nakamura *et al.* (2010) asserted that companies often use price adjustments to transfer increased costs to consumers in order to maintain profitability. Price adjustments are used to respond to changes in costs and demand, which can help mitigate the ripple effects of inflation on firms' profitability (Gopinath *et al.,* 2010). Firms may use cost-cutting measures, productivity enhancements, non-price strategies such as product innovation and quality improvements and supply chain optimization to reduce inflation's impact on firms' profitability (Cevik *et al.*, 2024).

Contrary to the established literature, Knox and Timmer (2025) argued that these strategies are not fixed and do not accommodate all firms in diverse industries, instead they depend on firm-specific factors. Akarsu *et al.* (2025) added that higher inflation expectations on the part of firms leads them to increase prices, increase demand for credit and reduce their employment and capital structure. However, when policy rates are constrained by the effective lower bound, demand effects become much stronger, leading firms to raise prices more and no longer reduce employment. In high-inflation environment, firms are especially attentive to macroeconomic developments, revising their inflation expectations and adjusting their financial strategies accordingly (Akarsu *et al.*, 2025).

3. METHODOLOGY

3.1. Research Design

This research study employed a Mixed-Method Approach (Qualitative and Quantitative) research design to investigate the effects of inflation on firm profitability in Lusaka, Zambia. Qualitative data from 108 firms on the inflation mitigating strategies, their effectiveness, price review and responsive measures were collected through purposive sampling technique and analyzed using Megastat. The data collected was integrated with the use of surveys (quantitative) and interviews (qualitative) to examine the level of consistency of findings from the respondents. To investigate the relationship between inflation and firms' revenue and cost components, regression analysis was used, and further tested using hypothesis. Parametric tests were used to confirm the statistical significance of the relationship between the variables in the study and the Chi-square was used to examine the association between inflation categories on average firms' revenue and average cost components, as well as the effectiveness of the strategies used in mitigating the effects of inflation on firms' profitability of local companies in Lusaka, Zambia.

3.2. Target Population

The target population for this study comprised of firms operating in Lusaka, Zambia. The targeted population included firms in diverse industries such as retail, wholesale, manufacturing and financial institutions, particularly those registered with PACRA. Firms that have operated for at least 5 years where stratified to ensure that the data collected is representative of the established study and align with the study's objectives.

3.3. Sample Size Determination

The determined sample size for this study was 108 companies operating in Lusaka, Zambia. Data was then selected through purposive and convenience sampling techniques, where respondents like managers, stakeholders, HR Managers etc. with available data and willingness to participate were selected. The sample size of 108 firms was considered sufficient for this study, given the complexity of the relationships being examined. According to Roscoe (1975), a sample size of 30 to 500 is considered sufficient for most research studies. Therefore, based on this, it was confirmed that the determination of this sample study was reasonable enough for analysis.

3.4. Data Collection Methods

108 companies in Lusaka, Zambia were administered for data collection. The questionnaires and interviews were assigned to each respondent in a particular manner to allow for simplicity and easy access. It consisted of both open and closed-ended questions, allowing respondents to provide detailed qualitative and quantitative responses. The questionnaires were designated to each respondent to ensure clarity and validity, and adjustments were made accordingly.

3.5. Data Analysis

The collected data was analyzed using Megastat. Descriptive and inferential statistics such as means, frequencies, regression analysis, ANOVA, hypothesis, p-values and Chi-squares were used to examine the relationships and associations between the variables in the study. Specifically, regression analysis was used examining the relationship between inflation and firms' revenue and cost components while the ANOVA was used to validate the results and compare the means across different firms. The Chi-square on the other hand was used to compare the associations between the categorical variables.

3.6. Limitations of Study

In any endeavor of this kind, limitations are always present. Therefore, not mentioning them becomes a horrendous act of negligence. This research study consists of several limitations that should be acknowledged. Firstly, the sample

size of 108 firms may not represent the entire population of local companies in Zambia. The study focuses only on firms in Lusaka, which may not be generalized to the other parts of the country. The study relies more on self-reported data from survey/questionnaires and interviews, which may be subject to biases and inaccuracies. Furthermore, the study only examines the effects of inflation on the financial performance and does not consider other/all factors that may influence this relationship.

3.7. Ethical Considerations

Since qualitative and quantitative research require direct interaction with respondents, the researcher will uphold the principles of honesty, integrity and mutual trust with the participants in order to yield objective and quality information. The researcher will furthermore assure the respondents regarding the data which will be collected and their identities that they will be kept under strict confidentiality and used for academic purposes only.

4. RESULTS AND DISCUSSION

4.1. Background Characteristics of the respondents

Under demographic information, four indicators were assessed and presented below.

4.1.1. Industry Type

The demographic analysis of the sampled firms reveals a diverse representation of industries in Lusaka, Zambia. The results show that retail firms dominate the sample, accounting for 63.0% of firms from the total sample of 108 firms. Manufacturing firms constitute 13.9%, while wholesale firms make up 12.0% firms. Financial institutions account for the smallest proportion, representing 11.1% of the sample.

This distribution suggests that retail firms are the most prevalent in the local economy, and their responses may have a significant on the overall findings of the study.

Table 1. Industry Type

Industry Type		
	frequency	**percent**
Manufacturing	15	13.9
Wholesale	13	12.0
Retail	68	63.0
Financial Institution	12	11.1
	108	100.0

4.1.2. Company size

Table 2 below shows the distribution of firms by company size revealing that the majority of firms (74.1%) are small firms with less than 50 employees. Firms with employee between 150 and 250 employees accounted for 3.7% while those with employees between 50 and 150 and more than 250 employees accounted for 11.1%. This distribution shows that small firms are more pronounced in the sample study.

Table 2. Company Size

Company size		
	frequency	percent
<50	80	74.1
50-150	12	11.1
150-250	4	3.7
>250	12	11.1
	108	100.0

4.1.3. Years of Operation

According to table 3 below, the distribution of firms by years of operation reveals a diverse range of business longevity. The results show that 39.8% of firms have been operating between 5 and 10 years, 30.6% of firms have been in operation within 10 and 15 years. Firms that have been operating for less than 5 years and those operating for more than 15 years each accounted for 14.8%. The distribution of respondents suggests a relatively stable business environment with a significant proportion of firms having established themselves over the years.

Table 3. Years of Operation

Years of operation		
	frequency	percent
>5Yrs	16	14.8
5Yrs-10Yrs	43	39.8
10Yrs -15Yrs	33	30.6
<15Yrs	16	14.8
	108	100.0

4.1.4. Ownership Structure

Table 4 below shows the distribution of firms by ownership structure revealing that foreign owned firms dominate the industries in the sample. The results of the respondenrs show that 62.0% of sampled firms are foreign-owned, while 38.0% are locally owned. This suggests that foreign ownership is more prevalent among firms operating in the local economy, as shown in table 4 below.

Table 4. Ownership Structure

Ownership Structure		
	Frequency	**percent**
Locally Owned	41	38.0
Foreign Owned	67	62.0
	108	100.0

4.2. Inflation and Firms' Revenue

4.2.1 Regression Analysis on Inflation and Firms Revenue

Table 5 on the regression analysis between inflation and firms' revenue revealed a negative relationship but with the p-value

suggesting a non-statistically significant relationship (β=-0.0692, p=0.7117) as shown below.

Table 5. Regression Analysis on Inflation and Firms' Revenue

Variables	Coefficients	std. error	t (df=106)	p-value	95% lower	95% upper
Intercept	3.0590	0.3930	7.784	4.96E-12	2.2798	3.8381
Inflation	-0.0692	0.1868	-0.371	.7117	-0.4396	0.3011

4.3. Inflation and Cost Components

4.3.1. Regression Analysis and Cost of Raw Materials

The regression analysis results for inflation on the cost of raw materials show the coefficient and the corresponding p-value indicating a statistical significance between inflation and material costs (β=0.3513, P=0.0356), as indicated in the table below.

Table 6. Regression Analysis on the Cost of Materials

Regression output					Confidence interval	
Variables	**coefficients**	**std. error**	**t (df=106)**	**p-value**	**95% lower**	**95% upper**
Intercept	2.0094	0.3472	5.788	7.32E-08	1.3211	2.6977
Inflation	0.3513	0.1650	2.129	.0356	0.0241	0.6784

4.3.2. Regression Analysis and Cost of Labor

The regression analysis results indicate a significant positive relationship between inflation rate and the cost of labor. The inflation rate coefficient suggests an increase in inflation with respect to a unit increase in labor cost with the p-value confirming statistical significance (β=0.7641, p=0.0001), as shown in the table below.

Table 7. Regression Analysis on Inflation and Cost of Labor

variables	coefficients	std. error	t (df=106)	p-value	95% lower	95% upper
Intercept	0.6701	0.3904	1.716	.0890	-0.1039	1.4441
Inflation	0.7641	0.1856	4.118	.0001	0.3962	1.1320

4.3.3. Regression Analysis and Cost of Energy

The regression analysis results indicate a positive relationship between inflation and the cost of energy. However, the p-value suggest that this relationship is not statistically significant (β=0.1744, p=0.2689).

Table 8. Regression Analysis on Inflation and Cost of Energy

Regression output					confidence interval	
variables	**coefficients**	**std. error**	**t (df=106)**	**p-value**	**95% lower**	**95% upper**
Intercept	2.0120	0.3300	6.096	1.79E-08	1.3576	2.6663
Inflation	0.1744	0.1569	1.111	.2689	-0.1367	0.4854

4.3.4. Regression Analysis and Cost of Transportation

The regression analysis results indicated a negative relationship between inflation rate and the cost of transportation, with the p-value indicating the relationship not to be statistically significant (β=-0.1359, p=0.4525).

Table 9. Regression Analysis on Inflation and Cost of Transportation

Variables	coefficients	std. error	t (df=106)	p-value	95% lower	95% upper
Intercept	2.7701	0.3791	7.306	5.37E-11	2.0184	3.5218
Inflation	-0.1359	0.1802	-0.754	.4525	-0.4932	0.2214

4.4. Strategies in Mitigating Effects of Inflation on Firms' Profitability

4.4.1. Strategies in Mitigating effects of Inflation on Firms' Profitability

Figure 1 of the results below indicate that in response to inflation, the majority of firms i.e., 78.8% opted for price adjustment, while 6.5% implemented cost reduction measures, and 14.8% focused on supply chain optimization.

Figure 1. Firms' Mitigating Strategies

4.5. Discussion Of The Research Findings

4.5.1. Inflation And Firms Revenue

The regression analysis results revealed a negative relationship between inflation and firms' revenue. However, the p-value suggested that this relationship is not statistically significant (β= -0.0692, p=0.7117). The findings of the study were validated by the parametric test that confirmed the non-statistical significance between inflation and firms' revenue (F=0.14, p=0.7117). The non-statistically significant shows that firms' revenue is not highly and directly influenced by inflation, instead concludes that other factors contribute to this negative relationship. The findings of this study remain consistent with the findings of Knox and Timmer (2024), suggesting a negative effect on firms' profitability, especially for firms with high leverage. Fabiani and Piersanti (2024) found similar results where inflation reduces firms' profitability. Similar findings by Muyanga (2019) found that the stock market performance of Zambian financial institutions was negatively affected by the increase in inflation. However, (Haar, 2024) argue that the impact of inflation on firms' revenue and stock market performance can vary depending on the industry type and sector, similar to a study by Blanchard (2022).

The implications of the negative effect of inflation on firms' revenue indicate that their other factors contributing to this negative relationship and this established relationship is due to chance, suggesting a thorough investigation of the factors involved.

4.5.2. Inflation and Cost Components

The regression analysis results for this study found a positive statistically significant relationship between inflation and cost of raw materials (β=0.3513, P=0.0356) as shown in table 6. The results were validated by the application of ANOVA, in which a statistically significant relationship between inflation and cost of raw materials was confirmed (F=4.53, P=0.0356). A statistically significant p-value indicates that the increase in the cost of materials is largely explained by the changes in inflation. Similar findings by Binici *et al.* (2021) found a positive relationship between inflation and cost of raw materials. Fabiani and Piersanti (2024) added that firms in the manufacturing sector are more vulnerable to inflation shocks due to increased production costs, suggesting that an increase in inflation leads to an increase in the cost materials. Contradictory findings by Blanchard (2022) argue that this increase in the cost of materials is attributed to monetary policy measures and not inflationary driven. Firms that are able to adapt quickly to changing supply chain conditions are better able to manage the impact of inflation on firms' cost of materials Baldwin and Freeman (2022). The implications of these findings show that an increase in inflation significantly increases the cost of raw materials making firms more vulnerable to the changes in inflation and experience the difficulties in achieving firms' profitability, highlighting the need for policymakers to improve on the macroeconomic policies that foster economic growth through firms' improvement on profitability margins.

The results of the study on the relationship between inflation and the cost of labor showed a positive correlation with a highly statistically significant p-value (β=0.7641, p=0.0001), as shown in table 7. The statistically p-value shows that the cost of labor is indeed influenced by the changes in inflation, suggesting that a 1% change in inflation results in a 0.7641 unit change or increase in labor cost, similar to the findings of Giovanni *et al.* (2022), who found that global supply chain pressures contribute to inflation, ultimately impacting firms' cost of labor. Contradictory findings emerge indicating that the relationship between inflation and labor costs is complex, adding that firms can adapt to inflationary environments in various ways (Fabiani & Piersanti, 2024), similar to a study by Babecky *et al.* (2010). It was established that in order to manage the impact of inflation on cost of labor, several factors such as the reduction in labor and input be minimized in both the short and long-run to maintain profitability.

The regression analysis results revealed a positive non-statistically significant relationship between inflation and the cost of energy (β=0.1744, p=0.2689) as shown in table 8. This non-statistically p-value shows that the changes in the cost of energy is not driven or highly determined by the changes in inflation, suggesting that other factors play a critical role in the cost of energy. Similar results by Brown and Yucel (2022) suggest a positive relationship between inflation and energy prices, particularly in the short run, where oil price shocks lead to increased inflation, considering that energy costs are a key component of production costs. These findings support the notion that inflation can lead to increased energy costs. However, Turin (2025) found contradictory results, indicating a non-statistically significant relationship between inflation and the cost of labor. Despite the consistence of a positive relationship between inflation and cost of labor with other studies, the findings of this study indicate that the relationship is not statistically significant highlighting the need for further investigation on the factors contributing to the changes in energy costs. The implications of the positive relationship between inflation and cost of energy on firms is that they do not operate effectively as they ought to, due to increased costs on machineries, especially in the manufacturing sectors that deal mostly with energy. It makes firms rely more on energy solutions forcing them to hike prices to maintain profitability,

ultimately causing a reduction in demand on the produced products, which eventually leads them to unsustainable profitability.

The regression analysis results revealed a negative but non-statistically significant relationship between inflation and the cost of transportation (β=-0.1359, p=0.4525). The non-statistically significant p-value suggest that firms' transportation costs is not directly influenced by the changes in inflation, similar to the findings of Hamilton (2009), suggesting that there could be other macroeconomic and firm specific factors contributing to this negative effect. However, research by the U.S Bureau of Labor Statistics (2025) showed that the Consumer Price Index (CPI) for transportation services has increased as a result of an increase in inflation, similar to a study by Branco *et al.* (2022) on the Portuguese firms who found that a rise in transportation costs, specifically tolls on highways led to 10.7% decreases in turnover and a 15% reduction in firm profits, contradicting the established findings of this study. The implications of these findings lie in the fact that the increase in transportation costs makes firms vulnerable to changes in inflation, making it difficult to maintain profitability, especially for firms operating in remote areas. However, with the non-statistically p-value, it was established that inflation is not the determinant factor explaining the changes in transportation costs, highlighting the need for further research.

4.5.3. Strategies in Mitigating Effects of Inflation on Firms' Profitability

The study's results indicate that in response to the increases in inflation, the majority of firms (78.8%) opted for price adjustments as the most effective strategy. On the other hand, the findings of this study revealed that 14.8% of firms in Lusaka, Zambia employ supply chain optimization while the minority of firms (6.5%) use cost reduction measures to reduce or mitigate the impact of inflation on profitability as shown in figure 1.

A study by Luca *et al.* (2025) show similar results adding that firms adjust prices very often due to the simultaneous dynamic economic conditions and firm structure, ultimately leading prices to shift temporarily from those that wish to maximize profits. However, Knotek and Zaman (2024) argued that the strategies in mitigating the effects of inflation on firms' profitability is complex and largely depends various firm-specific factors. Knox and Timmer (2025) added that these strategies are not fixed and do not accommodate all firms in diverse industries, instead they depend on firm-specific factors and characteristics, highlighting the need in understanding the complexities and factors that contribute to the effects on inflation on firms' profitability, and their effectiveness.

5. CONCLUSION

The study on the effects of inflation on firms' profitability used a mixed methods approach, incorporated with an evaluative research type in which 108 companies from the total target population of 130 companies in diverse industries such as manufacturing, retail, wholesale and financial institutions in Lusaka, Zambia were used in the sample for data collection. It was found that the retail industry emerged to be a dominant and significant factor in explaining the variations of inflation on firms' profitability, represented by 63.0% as shown in table 1. The majority of firms were found to have less than 50 employees, represented by 74.1%, while in terms of firm's longevity, the study found that the majority of firms had been in operation for more than 5 years to 10 years, represented by 39.8% as shown in table 3.

The Chi-square test revealed a non-statistically significant association between inflation category and firms' average revenue (x^2=7.94, df=6, p=2.427), suggesting that firm's average revenue is not directly influenced by the changes in inflation and firms within these industries may need to adopt tailored and effective strategies to manage the impact of inflation on their profitability. Additionally, the Chi-square test revealed an extremely highly statistically significant association between inflation and average total cost (x^2=39.86, df=6, p=4.85E-07), indicating that the changes in inflation highly contribute to the changes in the firm's cost components. The Chi-square test revealed a highly statistically significant association between firms' mitigating strategies and their effectiveness (x^2=22.63, df=6, p=0.0009), highlighting the need for frequent price adjustments for firms to maintain profitability during periods of high inflation. The findings of this study provide significant outcomes for businesses, policymakers and stakeholders that wish to understand the impact of inflation on firms' profitability, as well as the strategies used to mitigate the effects of inflation on firms' profitability of local companies in Zambia.

RECOMMENDATIONS

Inflation and Firms' Revenue

a. Further research should aim at examining the impact of inflation on sector-specific impacts and analyze their characteristics.

b. Further studies should consider collecting data from firms on different characteristics in order to understand the complexities associated with inflation and profitability

c. Further studies should also consider exploring the impact of macroeconomic variables like interest rates, exchange rates, and economic growth when analyzing the impact of inflation on firms' revenue.

Inflation and Cost Components

a. Firms should have a variety of suppliers from different regions to enhance their supply chain in order to reduce to impact of inflation on the cost components.

b. Firms with less or no market power should consider adjusting their cost structures to account for an increase in profitability.

c. The Government and/or policymakers should consider investing in the manufacturing industries, especially where raw materials are concerned to reduce dependence on foreign imports to help firms manage the cost increases that comes with the increases in inflation.

Strategies in Mitigating Effects of Inflation Firms' Profitability

a. Firms should frequently adjust their prices to maintain or increase profitability in a competitive market.

b. Firms should consider optimizing their supply chains and

improve operational efficiencies to enhance their profitability margin.

c. Firms in the same industries should consider each other as partners instead of mere competitors so as to support each other amidst high inflation to enhance profitability.

d. Firms should consider conducting regular market research and reviews to monitor the impact of inflation on the profitability.

e. Firms, especially managers should be updated on the Monetary Policy Committee (MPC) announcements in order to predict the economy's growth so as to manage their prices, supply chains and operations effectively without surprises.

f. The Government should provide support to firms by proving subsidies, tax breaks, offer building training programs and development programs to enhance the growth capacity for firms.

g. Firms should regularly conduct and attend exhibition events on specific industry market research to understand customer behavior and preferences, thereby identifying the areas of adjustments for improvement and growth.

ACKNOWLEDGEMENT

The authors would like to acknowledge the Information and Communications University in Zambia for allowing them to publish part of the thesis in the international journal. This allowed for the findings to be appreciated at a wider global scope and subject them to further refinement.

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