



The Tobacco Tax Directive Reform and Inflation: A Modest and Temporary Effect

Policy Brief

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Why is inflation a concern?

The revision of the Tobacco Tax Directive (TTD) is being discussed in a context where inflation remains politically sensitive. After the post-pandemic surge and the energy shock, inflation has gradually declined but remains salient in public debate. Recent tensions in the Middle East also illustrate how quickly energy-related price pressures could re-emerge. In such an environment, policies that affect consumer prices are likely to attract scrutiny.

Inflation matters because it affects household purchasing power and because it influences monetary policy. When inflation rises, central banks typically respond by increasing interest rates to slow price growth. Higher interest rates make borrowing more expensive for firms, households and governments.

The European Commission estimates that EU-wide inflation, as measured by Eurostat's Harmonized Index of Consumption Prices (HICP), could increase by up to **0.55 percentage points** under their July 2025 TTD proposal. This figure has been cited in public hearings as evidence that the reform may carry non-negligible inflationary consequences.

However, the significance of such an estimate must be assessed in context. It needs to be considered relative to prevailing baseline inflation rates and, most importantly, in terms of whether the reform would generate a sustained increase in inflation or merely a temporary price adjustment.

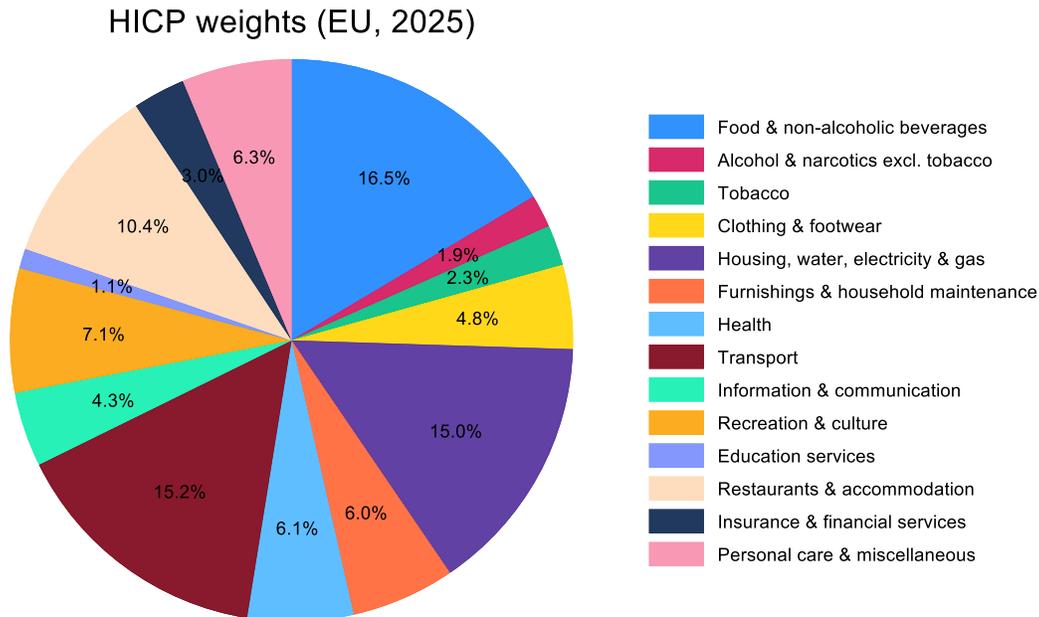
Answering this question requires understanding how the HICP is constructed and the role that tobacco plays within the overall consumption basket.

The importance of tobacco in overall inflation

Any assessment of the inflationary impact of the TTD reform must start with a simple fact: **tobacco represents a very small share of the consumption basket.**

As shown in Figure 1, across the EU, tobacco accounts for approximately **2.3 percent** of the HICP basket. By comparison, food and non-alcoholic beverages account for 16.5 percent, housing-related items for 15.0 percent, and transport for 15.2 percent. Within tobacco, the weight is further concentrated. Cigarettes account for roughly **1.85 percentage points** of the total HICP basket, while cigars represent **0.04 percentage points**, and other tobacco products about **0.43 percentage points**.

Figure 1



Source: Authors' elaboration using data from Eurostat

Inflation effects are determined by two elements:

- (1) the change in the price of a given component, and
- (2) that component's weight in the consumption basket.

Even sizeable increases in tobacco prices therefore translate into relatively modest effects on inflation, simply because the category represents a small fraction of total household expenditure.

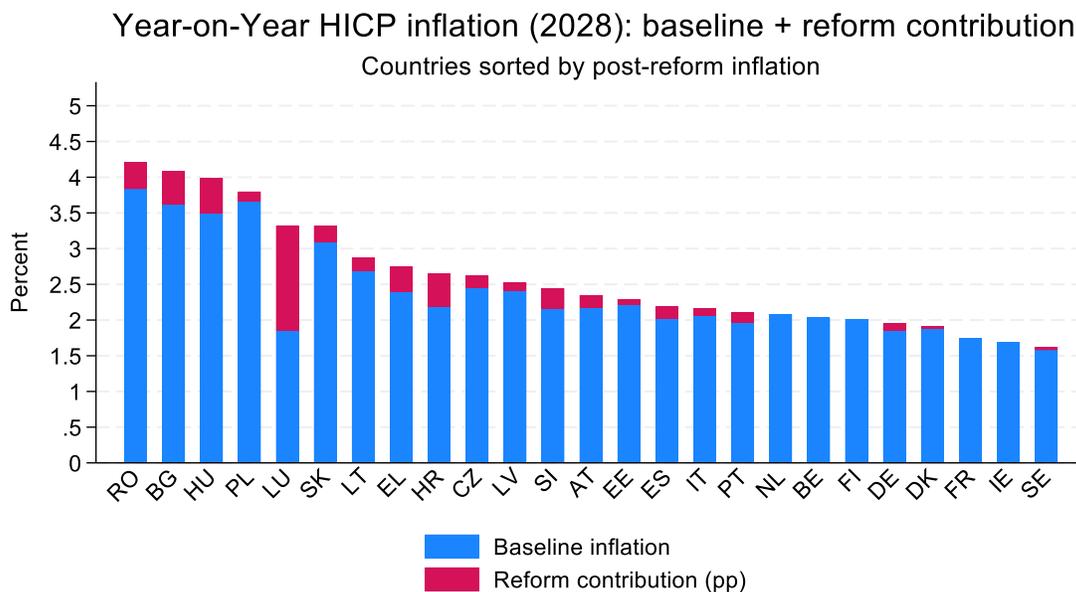
This arithmetic is central to interpreting the Commission’s impact assessment. The estimated increase in HICP reflects a price adjustment in a narrowly defined consumption category. It does not imply broad-based price pressures across consumers’ baskets.

The next section quantifies this effect under the reform scenario proposed in July 2025, examining its **relative magnitude, how it evolves over time, and how it differs across Member States.**

The effect on inflation of the European Commission’s TTD reform proposal

Figure 2 presents year-on-year HICP inflation in 2028, the intended date of enactment of the revision of the TTD. Countries are sorted by post-reform inflation. The blue bars represent baseline inflation (the inflation rate that would prevail in the absence of the reform), while the red segment shows the incremental contribution of the reform.

Figure 2



Source: Authors' elaboration using data from Eurostat, Euromonitor and European Commission

The reform effect is small relative to baseline inflation in the Member States that would need to raise tobacco taxes (there would be no inflationary effect in NL, BE, FI, FR and IE). Except in Luxembourg, the incremental contribution remains well below one percentage point. In most other cases, the contribution lies between 0.1 and 0.4 percentage points. Luxembourg appears as an outlier because tobacco has an unusually large weight in its HICP basket, reflecting high sales to non-residents, and the reform requires relatively large tax increases from a low initial level.

Table 1 reports the incremental contribution of the reform to year-on-year HICP inflation in 2028, 2029, and 2030. Because the tax reform is passed through to prices gradually, the effect is largest in 2028 and declines thereafter. The final column reports the cumulative increase in the HICP level over the 2028–2030 period. The pattern is clear: the effect is largest in 2028 and gradually fades thereafter.

Across countries (population weighted average), the reform contributes:

- **0.13 percentage points in 2028**
- **0.09 percentage points in 2029**
- **0.08 percentage points in 2030**
- **A cumulative effect of 0.3 percentage points over 2028-2030**

Table 1. Incremental contribution of the reform to year-on-year HICP inflation

| | 2028 | Year 2029 | 2030 | Cumulative increase in HICP (2028-2030) |
|--|-------------------|--------------|-------------|--|
| | Percentage points | | | |
| ISO | | | | |
| AT | 0.17 | 0.12 | 0.09 | 0.37 |
| BE | 0.00 | 0.00 | 0.00 | 0.00 |
| BG | 0.46 | 0.28 | 0.15 | 0.87 |
| CZ | 0.17 | 0.12 | 0.16 | 0.43 |
| DE | 0.10 | 0.08 | 0.08 | 0.25 |
| DK | 0.03 | 0.03 | 0.03 | 0.09 |
| EE | 0.08 | 0.06 | 0.04 | 0.17 |
| EL | 0.36 | 0.26 | 0.19 | 0.79 |
| ES | 0.17 | 0.12 | 0.09 | 0.38 |
| FI | 0.00 | 0.00 | 0.00 | 0.00 |
| FR | 0.00 | 0.00 | 0.00 | 0.00 |
| HR | 0.46 | 0.32 | 0.23 | 1.00 |
| HU | 0.50 | 0.39 | 0.31 | 1.16 |
| IE | 0.00 | 0.00 | 0.00 | 0.00 |
| IT | 0.10 | 0.08 | 0.09 | 0.26 |
| LT | 0.18 | 0.13 | 0.09 | 0.39 |
| LU | 1.48 | 1.13 | 0.88 | 3.47 |
| LV | 0.12 | 0.08 | 0.06 | 0.25 |
| NL | 0.00 | 0.00 | 0.00 | 0.00 |
| PL | 0.13 | 0.09 | 0.07 | 0.28 |
| PT | 0.14 | 0.10 | 0.07 | 0.31 |
| RO | 0.37 | 0.27 | 0.21 | 0.81 |
| SE | 0.04 | 0.03 | 0.04 | 0.10 |
| SI | 0.28 | 0.20 | 0.14 | 0.61 |
| SK | 0.23 | 0.17 | 0.12 | 0.50 |
| Average | 0.13 | 0.09 | 0.08 | 0.29 |
| Source: Authors calculations using data from Eurostat, Euromonitor and European Commission | | | | |

These results highlight two aspects of the reform’s inflation profile.

First, the impact is quite limited in magnitude relative to baseline inflation rates.

Second, the effect is not persistent. It reflects a relative price adjustment in a narrow consumption category, with a distributed pass-through that diminishes over time. It does not generate sustained upward pressure on inflation.

Conclusions

The analysis presented in this brief suggests that the inflationary effects of the proposed revision of the Tobacco Tax Directive are limited in magnitude and temporary in nature. The reform produces a modest increase in year-on-year inflation in the first years following implementation, which gradually fades. Across countries, the average contribution amounts to roughly 0.13 percentage points in 2028, declining thereafter, with a cumulative increase in the price level of around 0.3 percentage points over the 2028–2030 period.

These results reflect a simple economic reality: tobacco represents a small share of the consumption basket used to compute the HICP. Even when taxes lead to noticeable increases in tobacco prices, the arithmetic impact on overall inflation remains modest. Moreover, the effect corresponds to a relative price adjustment within a specific product category rather than to broad-based inflationary pressure across the economy.

It is likely that the reform will continue to attract claims about its potential inflationary consequences. While concerns about inflation are understandable in a period where price developments remain sensitive, the available evidence does not support narratives of large or persistent inflationary effects.

A careful and transparent communication of these mechanisms is important. Acknowledging legitimate concerns about price developments while placing the expected effects in their proper quantitative context can help prevent misconceptions and ensure that the debate around the TTD reform remains grounded in evidence rather than in exaggerated fears of inflationary disruption.

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