

Economic Outlook and Tax Changes in 2025

January 2025

As we enter 2025, several major tax changes are set to impact both individuals and businesses in Estonia. These reforms include increased income taxes, a new car tax, VAT hikes, and rising excise duties, all of which will shape the financial landscape of the country. Additionally, the ongoing inflationary pressures and wage growth will contribute to the evolving economic environment.

Income Tax Increases

Starting 1 January 2025, Estonia's income tax rate will rise from 20% to 22%. This increase will affect both individuals and businesses. In addition, from 2026, a "security tax" of 2% will be introduced, deducted from all income, including pensions and other social benefits, further raising the tax burden.

For businesses, the tax rate on profit distributions will also increase to 22% from the previously lower rate of 14%. This adjustment will apply to all profit distributions made from January 2025 onwards. Additionally, credit institutions will face a higher advance tax rate, which will increase from 14% to 18%.

VAT Changes

The Value-Added Tax (VAT) rate will rise from 22% to 24% starting 1 July 2025. This change will affect a wide range of goods and services, increasing the cost for consumers. Specifically, accommodation services will see VAT increase from 9% to 13%, while media outlets will experience an increase from 5% to 9%. These hikes will likely result in higher prices for consumers in these industries.

Introduction of the Car Tax

A significant new policy for 2025 is the introduction of an annual motor vehicle tax, which will apply to all vehicles registered in Estonia. The base amount will be EUR 50, but the final amount will depend on factors such as CO2 emissions and vehicle weight. Vehicle owners will also face a new registration fee when registering their cars for the first time.

Increased Excise Duties

Excise duties will also rise in 2025. Gasoline excise duties, unchanged since 2018, will increase by 5% annually for the next four years. The first increase will take effect on 1 July 2025, with an additional 6.3 cents per litre added to the price of gasoline.

Excise taxes on alcohol and tobacco will also increase. Alcohol excise duties, previously scheduled to increase by 5% in both July 2025 and January 2026, will now see a delay in the July increase due to border trade concerns. The alcohol excise duties will still increase by 10% in January 2026. Tobacco excise duties will continue to increase as they have in recent years. On 1 January 2025, a new higher excise duty on tobacco will come into effect and on 1 July 2025, the tobacco excise duty will increase by a further 5%.

Inflation and Wage Growth

In 2024, Estonia saw a 4.1% increase in consumer prices compared to the previous year, partly due to tax hikes like the VAT increase. Despite this, the labour market remains relatively strong, with wage growth expected to continue at around 6-7% annually. However, inflation is projected to stay around 4-4.5%. Although the annual price increase of 4.1% is lower than in the previous three years (12.0% in 2021, 17.5% by the end of 2022 and 4.3% by the end of 2023), it is still significant. Price increases in the euro area are lower, and those of our neighbours Latvia, Lithuania and Finland are also well below ours.

Land Tax Changes

Land tax will also see significant adjustments in 2025. The maximum rate for residential land will increase from 0.5% to 1%, while for business or industrial land, it will rise from 1% to 2%. These changes will increase the financial burden on property owners, particularly those with high-value land.



Conclusion

The tax increases and new duties scheduled for 2025 will create financial challenges for both consumers and businesses in Estonia. While the economy remains relatively stable, with wage growth expected to continue, the rising cost of living, fuelled by tax hikes and inflation, will require individuals and businesses to adjust. The introduction of the car tax and increased excise duties will impact personal finances and industries like transportation and hospitality. Nevertheless, Estonia's strong labour market and resilient economy offer hope that the nation can navigate these changes and maintain growth in the coming years.