A new action plan to mitigate inflation: the key points

At the end of 2022, the government approved a new decree to mitigate the impact of inflation in 2023, which is expected to remain high (with an annual average of 4.5% according to our forecasts). The plan will cost 10 billion euros (0.7% of GDP), although it will not lead to any upward revision of the budget deficit forecasts for 2023 since the Budget Plan already reserved 10 billion for additional measures to tackle the high inflation (without specifying how it would be spent). In this article, we take a deep dive into the plan's three pillars, namely, the measures proposed to support households, those to support the productive sector and those aimed at reducing electricity bills.

Households: the key new development is the cut in VAT on food and the elimination of the universal discount of 20 cents per litre on fuel

Firstly, VAT is cut from 4% to 0% on essential fresh foods (specifically: bread, flour, milk, cheese, eggs, fruit, vegetables and cereals) and from 10% to 5% on pasta and oil. This measure will be in place until 30 June 2023, but from May onwards it would be eliminated if core inflation in March or subsequent months were to fall below 5.5%. It is estimated that the fiscal cost of this measure, which applies to all consumers, but includes neither meat nor fish, could be around 650 million in the form of lower tax revenues.

Secondly, the most substantial measure focused on low-income households is a 200-euro cheque for families whose total income in 2022 was below 27,000 euros and whose net worth at the 2022 year end was less than 75,000 euros excluding their main residence. Neither pensioners nor those receiving the minimum vital income (IMV) benefit are eligible to receive this aid. This is the same measure as that implemented in 2022, with the difference that the number of beneficiaries is increased: in 2022 the threshold was a household income below 14,000 euros and net worth of less than 43,000 euros. It is estimated that up to 4.2 million households could potentially be eligible for the new scheme, and it will cost around 1.2 billion euros. It will be essential to expedite the bureaucratic procedures involved and spread awareness of this aid as widely as possible in order to prevent a repeat of what happened in 2022, when less than 30% of the 2.7 million potentially eligible households actually received it.[1] Depending on the persistence of the inflationary pressures, it may be desirable to increase the amount of this aid in the future, since it is focused on the households that feel the impact of high inflation the most. This will be accompanied by an increase in non-contributory pensions and in the minimum vital income amounting to 15% in 2023, with a total cost of 280 million euros.

Thirdly, with regards to public transport, between January and June the government will apply a 30% discount to public transport provided by regional (autonomous community) and local authorities, provided they contribute to increase the total discount to at least 50%. The total cost of this scheme will be 380 million euros, which is in addition to a further 655 million euros not part of this plan but already included in the 2023 General State Budget to provide free multi-trip passes on local and mid-distance train networks throughout 2023.

Finally, regarding the real estate market, the plan includes the previously announced 2% cap on rent increases in the absence of an agreement between the parties, which will be applicable throughout 2023. Additionally, up until 30 June, a six-month extension may be requested with the above conditions if the rental contract ends.

On the other hand, the universal 20-cent-per-litre fuel discount, which had an annual fiscal cost of around 5.7 billion euros, is eliminated and is replaced by measures focused on supporting the productive sectors hardest hit by the rise in fuel prices.

Productive sector: targeted aid focused on mitigating the rise in fuel prices

In terms of transport, the 20-cent-per-litre fuel discount for all users is eliminated and is replaced by a new 20-cent-per-litre discount up until 31 March, followed a 10-cent-per-litre discount between 1 April and 30 June, for professional haulers using diesel (the discount will be provided through a monthly refund in the hydrocarbon tax). These new discounts are also accompanied by direct aid (107 million euros in total) for holders of a transport licence (buses, taxis, ambulances, vehicles for hire with a driver and goods transport drivers) for their estimated consumption over a six-month period, which will range from 300 to 3,690 euros.

The primary sector will also benefit from fuel discounts of 20 cents per litre up until 30 June for both agricultural and livestock farmers (total funding: 240 million euros) based on their fuel consumption in 2022. In addition,

1. Data from the Ministry of Finance, collated by the main media outlets.

direct aid totalling 300 million euros will be granted to the agricultural sector to assist with the rise in the cost of fertiliser. Moreover, direct aid will be granted to the fisheries sector for a total of 120 million euros. The amount of this aid will be determined in each case based on an estimate of the vessel's diesel consumption in order to cover each fishing company's additional costs arising from the rise in fuel prices.

Finally, as far as industry is concerned, for gas-intensive industries a specific line of government-backed loans managed by the Official Credit Institute (ICO) has been approved with a budget of 500 million euros, offering guarantees of up to 90% to help mitigate their current liquidity problems and support the sector's decarbonisation. This is in addition to the direct aid totalling 450 million euros for the ceramics sector.

Electricity market: the tax cuts for electricity and gas will be extended throughout 2023

The main measure in this sphere is the extension throughout 2023 of the tax cuts on electric bills: VAT on gas and electricity is cut from 21% to 5%,[2] excise duty on electricity (IEE) is cut from 4.11% to 0.5% and the value tax on electricity production is suspended. The bulk of this plan's 10-billion budget is concentrated in these cuts. Indeed, while no estimate has been given for 2023, the reduction in tax revenues in 2022 due to the electricity tax cuts (i.e. not counting gas) up to November amounted to 6.1 billion euros according to the Spanish Tax Agency. Also, the cap of 19.55 euros on the price of butane cylinders remains in place until 30 June 2023, while the prohibition on cuts in essential supplies, as well as the reductions under the social electricity discount scheme for vulnerable consumers, are extended into 2023.

This is an action plan that will need to be tweaked as prices evolve. Its biggest cost in budgetary terms will continue to come from the tax cuts on electricity and gas. In addition to this are measures focused on reducing VAT on food, in an effort to address the persistent inflationary pressures affecting this component in recent months. This is accompanied by measures focused on lower-income households and on the productive sectors hardest hit by the rise in fuel prices.

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2. The VAT cut affects consumers with a contracted capacity of less than or equal to 10 kW. Virtually all households will benefit from the decrease in this levy. The VAT rate of 5% will also apply to 72.5% of business electricity supply contracts (non-domestic businesses).