

# **Lessons from Tobacco Tax Policy**

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# Background

- **Thai government owns Thailand Tobacco Monopoly (TTM) since 1943.**
- **No legal import of foreign cigarettes until 1991.**
- **Between 1973-1992 many proposals to increase tax-failed.**
- **“Tax for Health” policy adopted since 1993.**
- **Earmark tax dedicated for Health Promotion since 2001.**

# **Important players in Thailand Tobacco Policy**

- **The Government**
  - **Ministry of Finance**
  - **Ministry of Health**
  
- **Tobacco suppliers**
  - **TTM**
  - **Importers**

# **The two sources of the Thai government's revenue from cigarettes**

- **Profit sharing from sale of TTM products**
- **Revenue from taxes - tariff, excise tax, local tax and VAT -.**

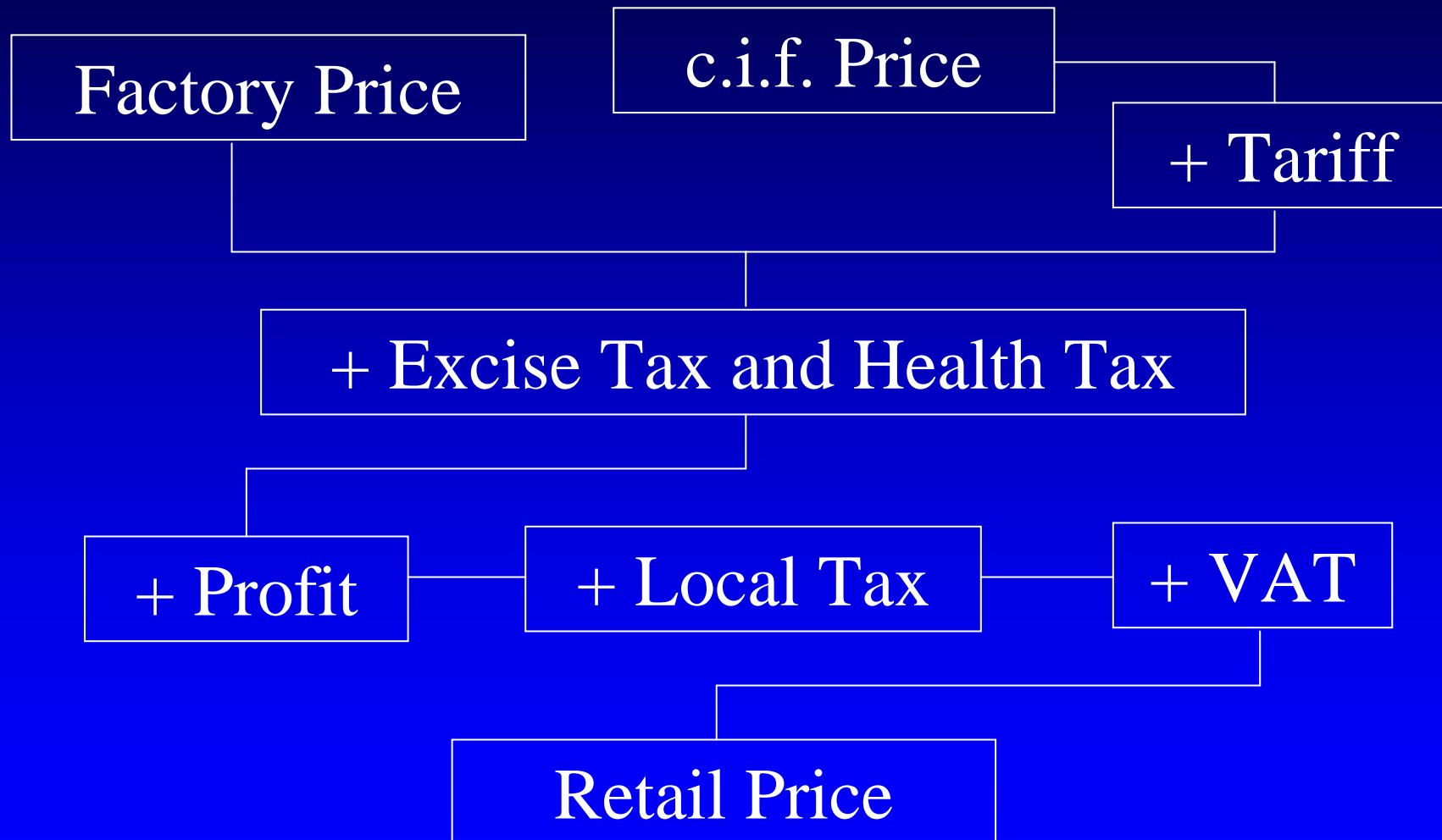
# Government's dilemma

- **Popularity and votes.**
- **Trade off between tax revenue and health impact.**

# Cigarette industry's concern

- **Profit.**
- **Market size and share.**

# Cigarette price structure



# Excise tax, cigarette sales and tax revenue

<b>Year</b>	<b>Tax(%)</b>	<b>Sales (million Pack)</b>	<b>Tax revenue(million Baht)</b>	
1992	55	2,035	15,438	
1993	55	2,135	15,345	
1994	60	2,328	20,002	
1995	62	2,171	20,736	
1996	68	2,463	24,092	
1997	68	2,415	29,755	
1999	70	1,810	26,708	
2000	71.5	1,826	28,110	
2001	75	1,727	29,627	
2002	75	1,716	31,247	2003
	75	1,904	33,582	
2004	75	2,110	36,326	
2005	79			



# Government's alternatives

- **Do not increase the tax rates and the real prices of cigarettes decrease in relation to inflation.**
- **Increase the tax rates.**

# Decision depends on elasticity of cigarette demand

- **Income elasticity.**
- **Own price elasticity.**
- **Substitution toward other goods.**

# Elasticity estimates in the case of Thailand?

- **Income elasticity around 0.70 (cigarette demand will increase by 0.70%, if income increase by 1%).**
  - **Own price elasticity around -0.40 (the demand will decrease by 0.40%, if price increase by 1%).**
  - **Cross price elasticity and degree of substitution are very low.**
- \* It should be noted that these estimates are based on the year 2000 data.**

# **Use Thailand's tax increase as an example!**

- **Between 2000-01, excise tax rate increased from 71.5% to 75%, i.e. +4.90%.**
- **Cigarette demand decreased from 1,826 to 1,727 million packs, i.e. -0.54%.**
- **Consumption expenditure increased from 2,754 billion Baht to 2,925 billion Baht, i.e. +6.23%.**
- **Tobacco tax revenue increased from 34,390 to 36,235 million Baht, i.e. +5.37%.**

# **The importance and power of a demand analysis (1).**

- **Tax rate increased by 4.90% (from 71.5% to 75%)**
- **Retail price should increase by 12.29% (the actual increase was 13.67%)**
- **According to the elasticity, this caused demand to decrease by 4.92%**

## The importance and power of a demand analysis (2).

- But income increased by 6.23%
- This caused demand to increase by 4.36%
- Total theoretical decrease in demand should be  $4.36 - 4.92 = -0.56\%$
- Actual decrease was  $-0.54\%$  !!!!

## **The importance and power of a demand analysis (3).**

- **Because of the increase in tax rate, price and demand, the excise revenue should increase by around 12%.**
- **The AFTA decrease in tariff from 22.5% to 10% led to a 6% decrease in tax revenue.**
- **Thus, tobacco tax revenue should increase by  $12 - 6 = 6\%$**
- **The actual tobacco tax revenue increase was 5.36%!!!**

# Differences between tobacco products and alcoholic beverages

- **Tobacco products are more homogeneous.**
- **Substitution between tobacco products is low why those between alcoholic beverages is high.**
- **Cigarette prices are controlled why those of alcoholic beverages are market determined.**
- **Only one cigarette producer why there are many alcoholic producers.**