

# Analysis of the market with tobacco products in the Czech Republic

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**1 EUR = 25,5 CZK**

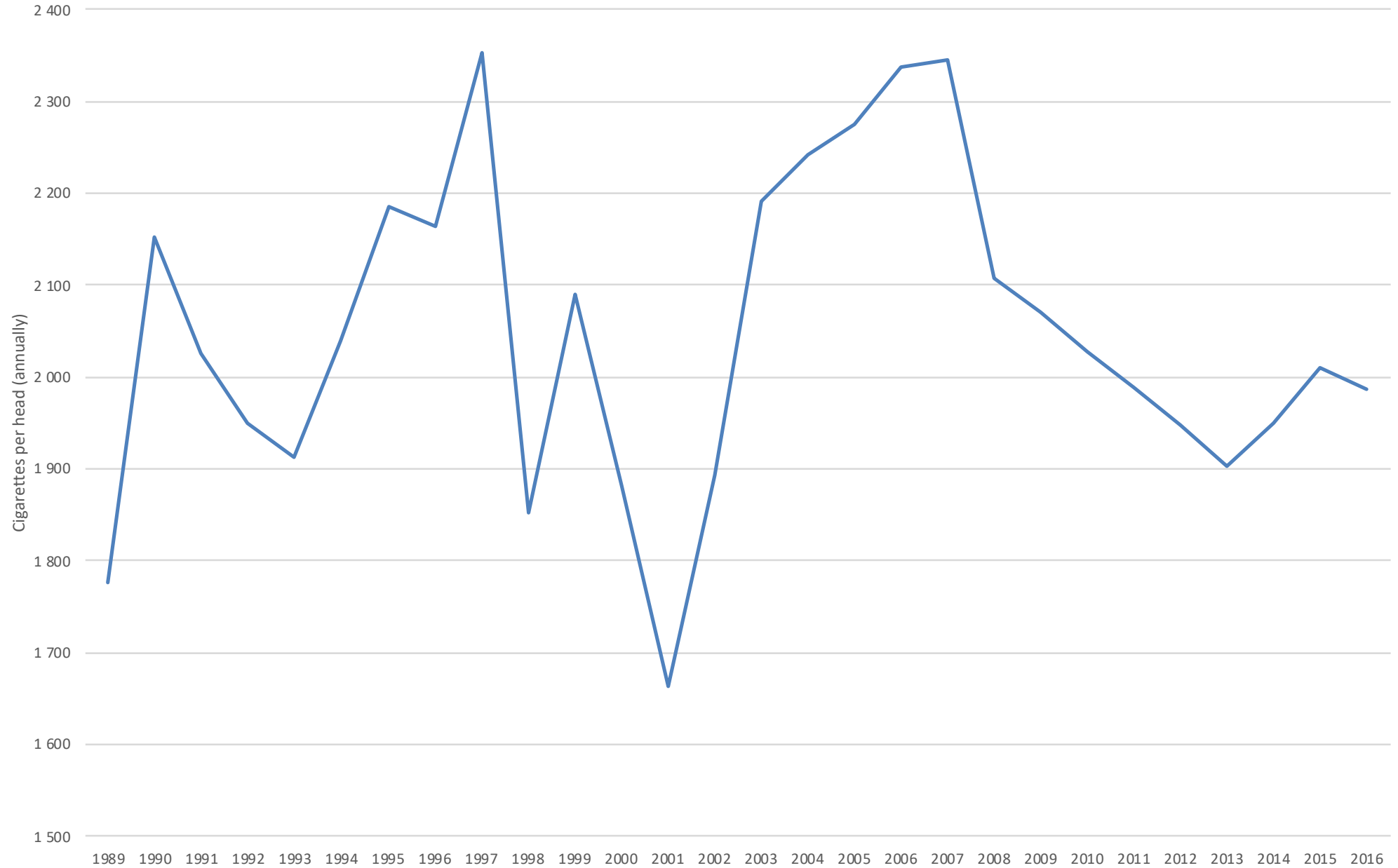
**1 USD = 21,4 CZK**

# 1. Market description

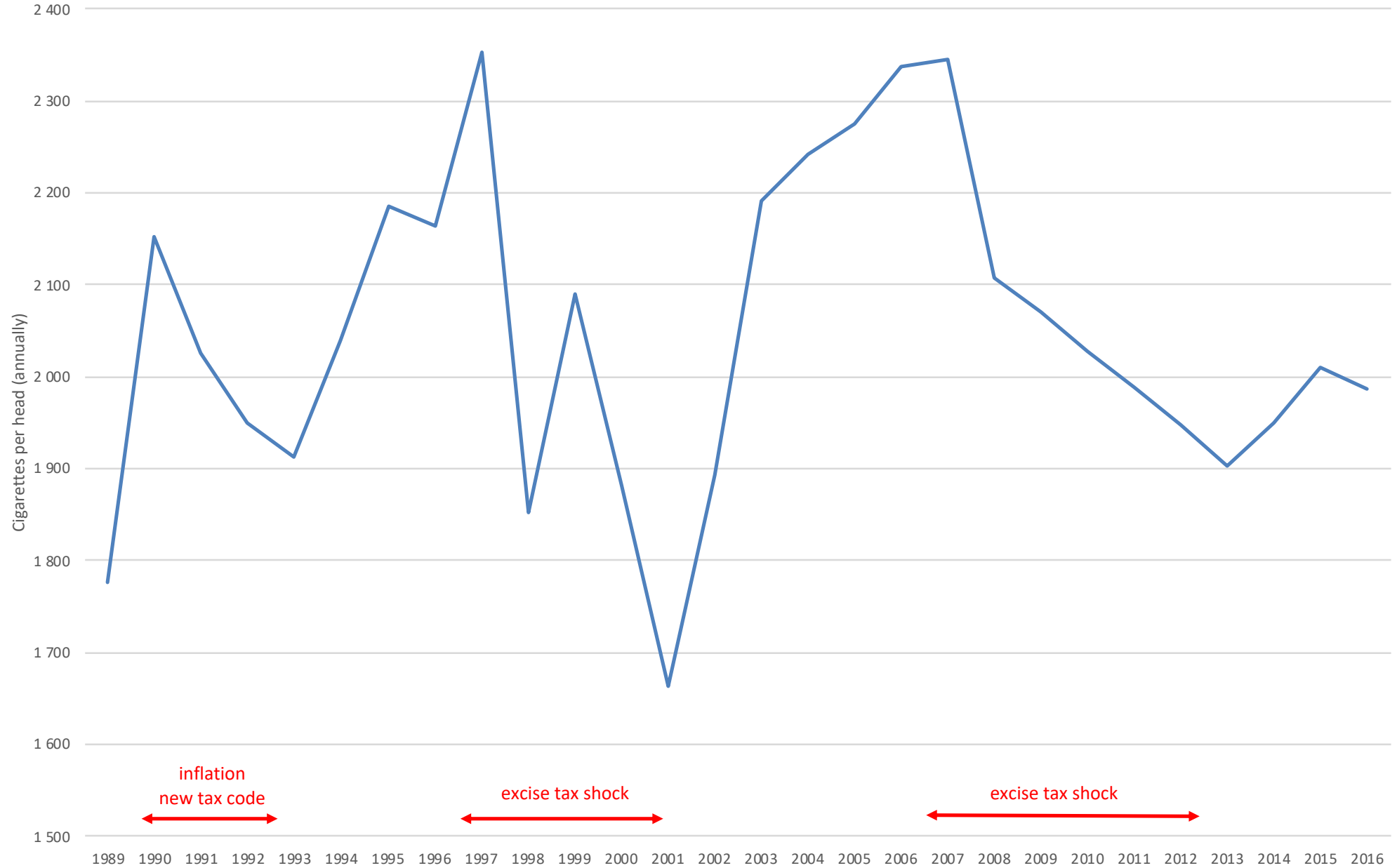
# Pillars of tobacco consumption

- 5 main pillars - CHIPR:
  - **Culture:** A “pub culture” oriented on alcohol and tobacco consumption (a beer and a cigarette as a symbol of the Czech tradition).
  - **Healthcare:** A public healthcare insurance causes a moral hazard of smokers (a better care is “for free” for everyone).
  - **Ignorance:** Smokers are ignorant to information about negative impacts of tobacco consumption (a filter made on certain information channels).
  - **Prevalence:** A society is very tolerant to smoking (smoking habits are transmitted to younger generations as a threshold of adulthood).
  - **Rose-tinted glasses:** Smokers notice only good or idealized examples so their view is unrealistic (my friend had smoked the whole life and died in 95, so...).

## Czech Republic: Consumption of cigarettes per capita (1989 - 2016)



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# Main market characteristics

- The Czech market with tobacco products is characterized by:
  - Stability and conservatism in behavior of consumers
  - Price shock absorptions (in 1-3 years cycles)
  - Strong interest groups and lobby influencing decision makers
  - Social stratification of smokers correlating with income and political orientation
  - Linking tobacco and alcohol consumption to national culture of “pubs” as centers of social networking
  - A very low level of shadow transaction and illicit trading (transit country)
  - Efficient strategies of tobacco producers reacting on regulation
  - A very strong factor of so called downtrading (buying cheaper cigarettes)

# Tobacco expenditures of households

- Spending of households on tobacco products rises in time
- This trend is supported by economic growth and wage increase, downtrading and also by a new generation of smokers
- A trend of tobacco expenditures per head is growing as well

	Index	2010	2011	2012	2013	2014	2015	2016
Wage median	CZK per year	257 439	261 384	263 964	267 192	274 128	284 712	299 208
<i>annual change</i>	<i>y/y %</i>	-	1,5	1,0	1,2	2,6	3,9	5,1
Household consumption expenditures	CZK per year	116 214	117 882	118 819	120 827	122 049	122 467	125 947
<i>annual change</i>	<i>y/y %</i>	-	1,44	0,79	1,69	1,01	0,34	2,84
Household tobacco expenditures (from total consumption expenditures)	% from total	4,2	4,2	4,3	4,4	4,3	4,5	4,5
Tobacco expenditures per head	CZK per year	1 609	1 665	1 645	1 605	1 708	1 753	1 743
<i>annual change</i>	<i>y/y %</i>	0,69	3,48	-1,2	2,43	6,42	2,63	-0,57



# Main market characteristics II.

- There is no continuity in tobacco consumption decline.
  - Price shocks are absorbed, economic cycle matters
- Czechs have first experience with tobacco at very young age.
  - 30% of 16yo smoke n last 30 days, 66% smoked, 16,4 % smoke daily, 4,5 % smoke +11 cigarettes daily, average age of first experience 11,9 yo, (ESPAD 2015)
- About 30 % of society smoke cigarettes, 71,4 % are non-smokers (NIPH 2017).
  - Men more than women (35 % vs. 22,5 %)
  - 19,6 % of people smoke daily, 9 % occasionally (men more than women)
  - Most of smokers prefer commercially produced cigarettes (manually wrapped 4 %)
  - Most of smokers are from the age group 15-24
  - Smoking prevalence decreases as a level of education increases (34,1 % vs. 20,5 %)

# Smokers vs. non-smokers

<b>2016</b>	<b>Total</b>	<b>Male</b>	<b>Female</b>
Smokers	28,6%	35,0%	22,5%
- daily	19,6%	23,8%	15,6%
- occasionally	9,0%	11,1%	6,9%
- occasionally (ex-daily)	3,6%	4,2%	3,0%
- occasionally (ex-never)	5,4%	6,9%	3,9%
Non-smokers	71,4%	65,0%	77,5%
- ex-smokers	15,3%	16,3%	14,4%
- daily	7,1%	8,7%	5,5%
- occasionally	8,3%	7,6%	8,9%
- never smoking	56,1%	48,8%	63,1%

# Smokers - characteristics

	Whatever tobacco product	Whatever cigarettes	Comercially produced	Manually wrapped	Other products
Total	28,60%	26,80%	24,70%	4%	4,40%
<b>Sex</b>					
- Male	35%	33,20%	30,30%	5%	6,50%
- Female	22,50%	20,80%	19,30%	3,10%	2,40%
<b>Age</b>					
- 15-24	34,60%	32,50%	31,60%	3,40%	9%
- 25-44	30%	28,20%	25,90%	4,20%	4,40%
- 45-64	30,80%	29,10%	26,30%	5,10%	4%
- 65+	18,60%	17,20%	15,30%	2,50%	2,20%
<b>Residence</b>					
- City	28,60%	26,80%	24,40%	4,10%	4,50%
- Countryside	28,60%	26,90%	25,70%	3,90%	4,10%
<b>Education</b>					
- Primary	34,10%	32,50%	29,10%	6,20%	4%
- Secondary (graduation)	25,10%	22,60%	20,70%	3,10%	3,80%
- Tertiary	20,50%	19,90%	18,80%	2,00%	3,10%

## 2. Tobacco market regulation

# Regulatory tools

- Regulatory tools applicable on the Czech market:
  - Prohibitio ordinem tools (age, location, advertisement, vouchers use...)
  - Excise tax (specific (fixed) excise tax, ad valorem tax)
  - Value Added Tax (VAT)

	2010	2011	2012	2013	2014	2015	2016	2017	2018
Ad valorem tax (in %)	28	28	28	27	27	27	27	27	27
Specific fixed tax (CZK/pc)	1,07	1,07	1,12	1,16	1,19	1,29	1,39	1,42	1,46
Minimum excise tax (CZK/pc)	2,01	2,01	2,1	2,18	2,25	2,37	2,52	2,57	2,63
Minimum excise tax per pack (CZK/20 pcs in pack)	40,2	40,2	42	43,6	45	47,4	50,4	51,4	52,6

# Cigarette pack tax calculation – EXAMPLE 1

- **Price 74 CZK per 20 pcs.** ( $\approx 2,90$  EUR  $\approx 3,46$  USD)
  - Tax calculation:
    - Ad valorem: 27 % from 74 CZK = 19,98 CZK
    - Specific tax:  $20 \times 1,46$  CZK = 29,20 CZK
    - Total: 49,18 CZK
  - Minimum tax test (2,63 CZK per 1 pc.):  $2,63 \times 20 = 52,60$  CZK ( $> 49,18$  CZK) **NOT OK**
    - Minimum tax 52,60 CZK is imposed here.
  - VAT (21 %): 12,84 CZK
- **TAX SUM TOTAL: 65,44 CZK** (3,272 CZK per 1 cigarette)

**Tax burden makes 88,4 % of the final price.**

# Cigarette pack tax calculation – EXAMPLE 2

- **Price 84 CZK per 20 pcs.** ( $\approx 3,29$  EUR  $\approx 3,92$  USD)
  - Tax calculation:
    - Ad valorem: 27 % from 84 CZK = 22,68 CZK
    - Specific tax:  $20 \times 1,46$  CZK = 29,20 CZK
    - Total: 51,88 CZK
  - Minimum tax test (2,63 CZK per 1 pc.):  $2,63 \times 20 = 52,60$  CZK ( $> 51,88$  CZK) **NOT OK**
    - Minimum tax 52,60 CZK is imposed here.
  - VAT (21 %): 14,58 CZK
- **TAX SUM TOTAL: 67,18 CZK** (3,359 CZK per 1 cigarette)

**Tax burden makes 79,97 % of the final price.**

# Cigarette pack tax calculation – EXAMPLE 3

- **Price 110 CZK per 20 pcs.** ( $\approx 4,31$  EUR  $\approx 5,14$  USD)
  - Tax calculation:
    - Ad valorem: 27 % from 110 CZK = 29,70 CZK
    - Specific tax: 20 x 1,46 CZK = 29,20 CZK
    - Total: 58,9 CZK
  - Minimum tax test (2,63 CZK per 1 pc.):  $2,63 \times 20 = 52,60$  (< 58,90 CZK) **OK**
    - Calculated tax 58,90 CZK is imposed here.
  - VAT (21 %): 19,09 CZK
- **TAX SUM TOTAL: 77,99 CZK** (3,899 CZK per 1 cigarette)

**Tax burden makes 70,9 % of the final price.**



# Other tobacco products

- Other products:
  - Cigars (tax rate per 1 pc = 1,71 CZK)
  - Fine cut tobacco (tax rate per 1 kg = 2236 CZK)
  - Heat tobacco products (tax rate per 1 kg = 2236 CZK since 1.1.2019)
  - E-cigarettes (no tax)



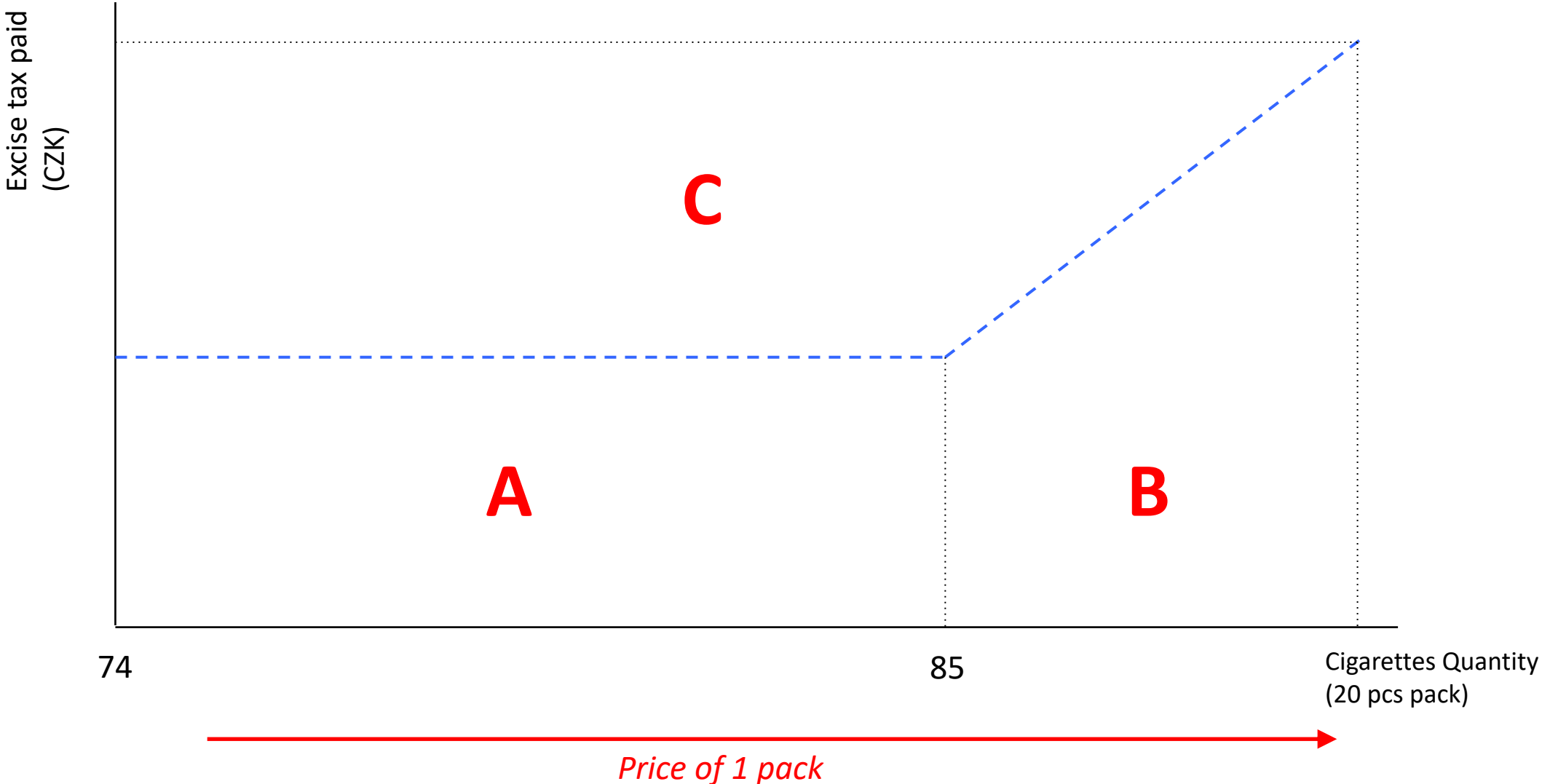
# Tobacco products - prescribed taxes

Time	Tax prescribed (mio CZK)	Tax paid (mio CZK)	Cigarettes consumed (mln. pcs)	Cig. boxes consumed (mln. pcs)
January	3099	3752	773,4	38,67
February	5250	5303	1310,2	65,51
March	4856	3183	1211,9	60,59
April	4859	5417	1212,6	60,63
May	3618	4930	902,9	45,15
June	4988	4157	1244,8	62,24
July	4132	3804	1031,2	51,56
August	6338	5747	1581,7	79,09
September	3970	4012	990,8	49,54
October	4099	6783	1023,0	51,15
November	3341	3141	833,8	41,69
December	5219	4186	1302,5	65,12
<b>Total 2016</b>	<b>53770</b>	<b>54416</b>	<b>13419,0</b>	<b>670,95</b>
January	3411	4207	812,5	40,63
February	5110	4108	1217,2	60,86
March	4689	3273	1117,0	55,85
April	4405	5206	1049,3	52,47
May	5199	4624	1238,4	61,92
June	5224	4674	1244,4	62,22
July	4957	5564	1180,8	59,04
August	5472	4932	1303,5	65,17
September	4863	4847	1158,4	57,92
October	4464	5821	1063,4	53,17
November	4570	4780	1088,6	54,43
December	5022	4184	1196,3	59,81
<b>Total 2017</b>	<b>57386</b>	<b>56219</b>	<b>13669,8</b>	<b>683,49</b>

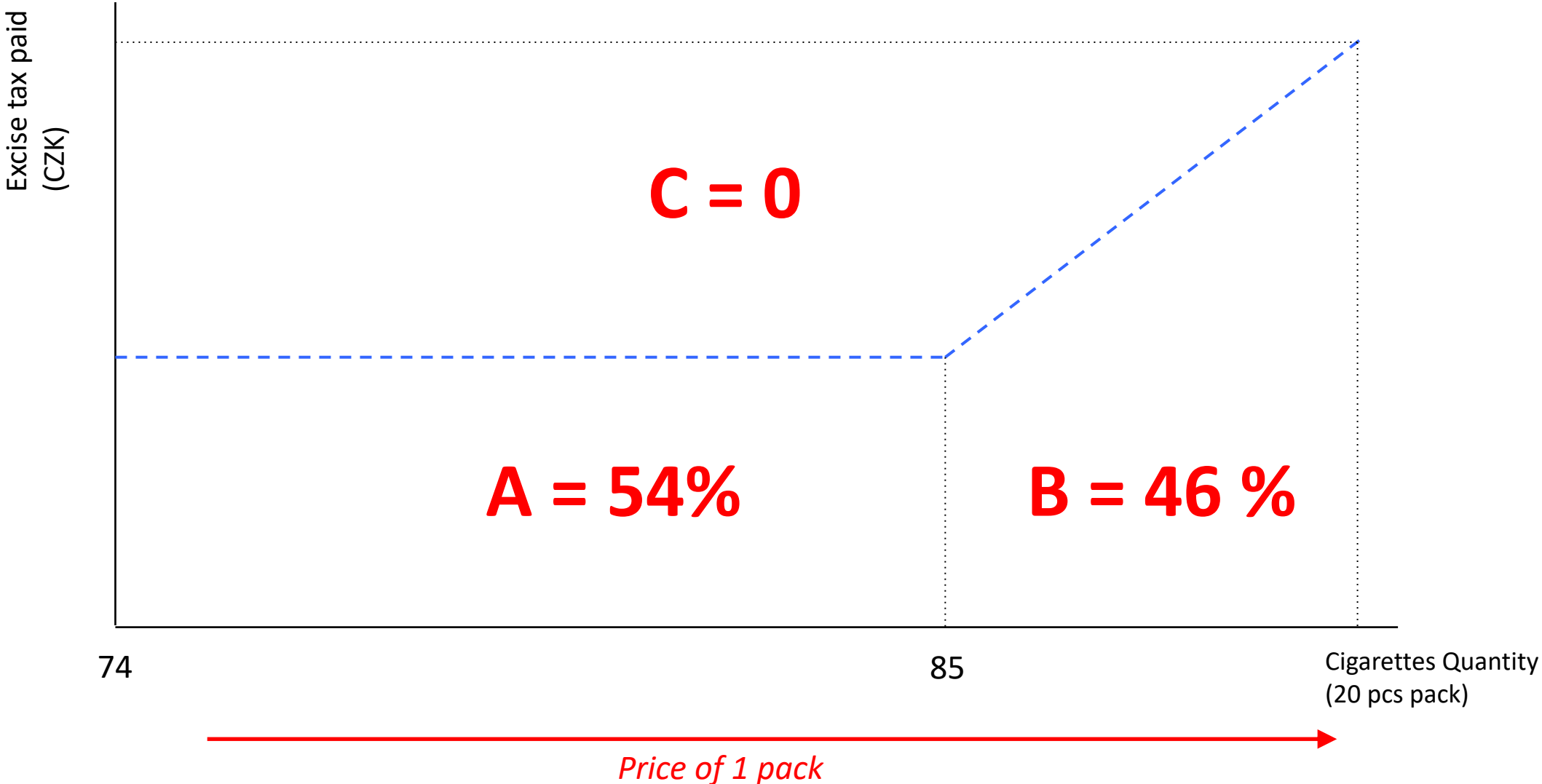
**Prescribed tax between 2017 and 2016 increased by 9 %, however a tax rate increased only by 2,3 %.**

## 3. Specifics and challenges

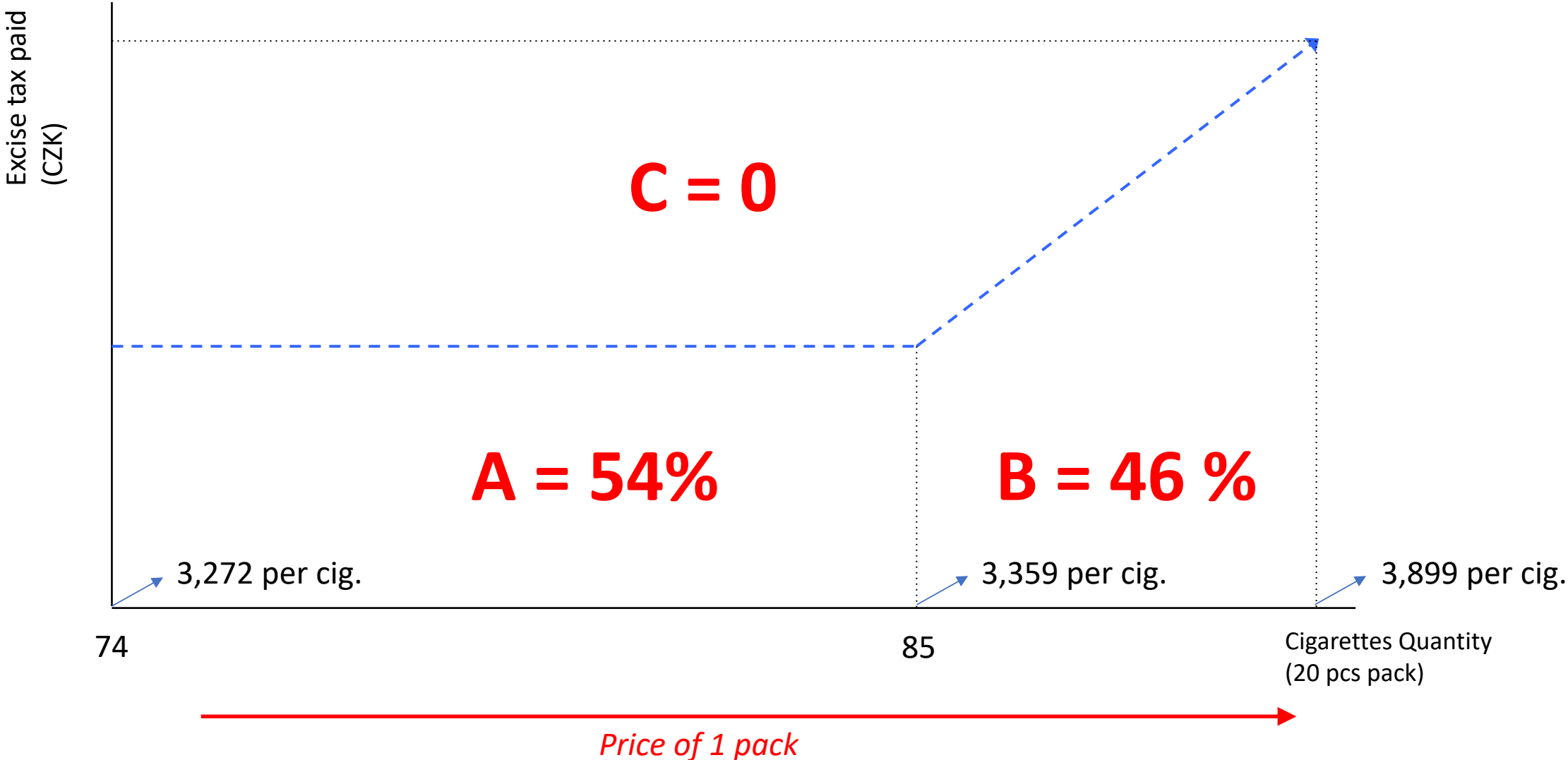
# Tax burden - cigarettes



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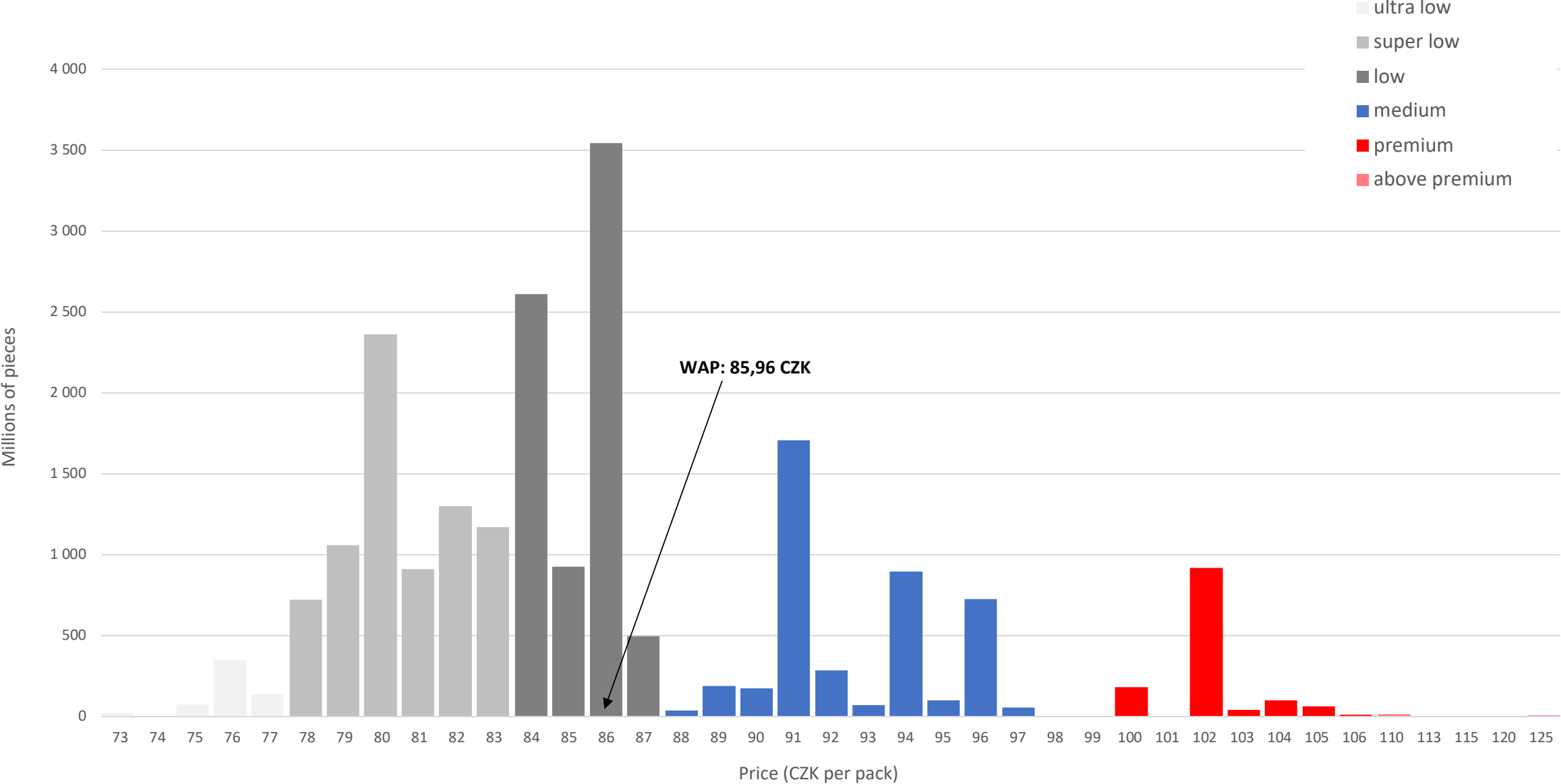


# Tax burden - cigarettes

- 53,7 % of tax revenues come from the 1<sup>st</sup> price decile
- 54,5 % of cigarettes (pieces) are consumed at the 1<sup>st</sup> price decile
- Tax burden imposed on cigarettes is very progressive (+ 98 % diff.)
- There is a substantial space for increasing minimum taxes.
- A revenues (minimum taxes) + B revenues (ad valorem taxes) are recent revenue, while C revenues create potential for more efficient tobacco consumption policies.



# Cigarette segments 2017



# Market share of tobacco brands 2008 - 2016

Geography	Category	Brand Name (GBO)	2008	2009	2010	2011	2012	2013	2014	2015	2016
Czech Republic	Cigarettes	Red & White (Philip Morris International Inc)	9,7	12,6	12,9	13	11,5	11,3	10,9	10,4	10
Czech Republic	Cigarettes	Viceroy Special (British American Tobacco Plc)	12,1	12,3	13,7	10,6	8,1	7,3	6	6	6
Czech Republic	Cigarettes	Moon Red (Imperial Brands Plc)	-	-	-	-	-	-	-	-	4,9
Czech Republic	Cigarettes	Petra Klasik (Philip Morris International Inc)	-	-	-	-	-	1,2	3,9	4,4	4,4
Czech Republic	Cigarettes	Marlboro Gold (Philip Morris International Inc)	4,6	3,8	3,8	4,2	4,3	4,4	4,5	4,4	4,2
Czech Republic	Cigarettes	Chesterfield (Philip Morris International Inc)	0,4	0,4	0,4	0,6	1,4	1,9	2,6	3,7	4
Czech Republic	Cigarettes	L&M Blue (Philip Morris International Inc)	2,8	3,1	3,4	3,3	3,4	3,5	3,7	3,8	3,9
Czech Republic	Cigarettes	L&M Red (Philip Morris International Inc)	2,4	3	3,3	3,3	3,4	3,5	3,6	3,8	3,8
Czech Republic	Cigarettes	Benson & Hedges (Japan Tobacco Inc)	-	-	0,1	1,4	2,5	3,5	3,6	3,7	3,7
Czech Republic	Cigarettes	Viceroy S-Line (British American Tobacco Plc)	-	-	0,2	1,9	3,3	3,5	3,8	3,7	3,7
Czech Republic	Cigarettes	Phillip Morris (Philip Morris International Inc)	1,1	0,9	1	2	2,5	3	3,5	3,6	3,7

# Challenges for the market

1. To reduce tobacco consumption
  - Action plan of the Czech Government set the goal to decrease a consumption about 8 % between 2015 – 2018 (not real, data shows only a slight decrease at the best). It's necessary to crash through information barrier (bubble) of smokers.
2. To set a new tax matrix
  - It is necessary to increase minimum taxes, to limit a progressivity of the system and follow a purchasing power increase with tobacco policies
3. To stop downtrading
  - A progressivity of the system (see above) generates a trend of downtrading – people systematically buy cheaper cigarettes, which is reflected by strategies of tobacco industry (new, attractive brands for local markets).

# Challenges for the market

4. To catch up with new tobacco products
  - HNB tobacco products are without excise taxes as well as e-cigarettes and vaporizers.
5. To reflect fine-cut tobacco price' advantages
  - Fine-cut tobacco products get just 4 % of the market with a
6. To control illicit trade
  - Czech shadow market is relatively low ( $\approx 5\%$ ), because we are transit country to Germany and Austria (2 EUR/pack price premium).
  - A sharp increase of prices without anti-illicit trade policies can create an impulse for shadow market expansion
  - Tax avoidance trends increase with more tax exceptions and special regimes

# Thank you for your attention.

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