

The economics of tobacco

Introduction

Smoking is a health problem, the costs of which include sickness, pain, grief and misery. But tobacco use also imposes a significant economic burden on society. In addition to the direct medical costs of treating tobacco-induced illnesses there are other indirect costs including loss of productivity, fire damage and environmental harm from cigarette litter and destructive farming practices. The total burden caused by tobacco products more than outweighs any economic benefit from their manufacture and sale.¹

Cost to smokers

In 2015, a 20-a-day smoker of a premium cigarette brand will spend about £3,000 a year on cigarettes. The price of tobacco has increased by 87% over the last ten years from 2004 to 2014, making it 30% less affordable.²

The Office for National Statistics estimates that the total UK household expenditure on tobacco in 2014 was to £19.4 billion.² However, the proportion of household expenditure on tobacco has decreased from 3.3% in 1985 to 1.8% in 2014.²

Smokers also pay with their health. The results from a 50 year study shows that half to two thirds of all lifelong cigarette smokers will be eventually killed by their habit.³ Death is usually due to one of the three major diseases caused by smoking lung cancer, chronic obstructive lung disease and coronary heart disease. Many who suffer from these diseases experience years of ill health and subsequent loss of productivity. One study concluded that smokers face a significantly higher chance of early retirement due to chronic disease.⁴ In 2013/14 there were approximately 1.6m hospital admissions in England among adults over 35 due to illnesses caused by smoking.²

Cost to society

Research commissioned by ASH has shown that the total cost to society (in England) is approximately £13.9 billion a year.⁵ This includes the cost to the NHS of treating diseases caused by smoking in England which is approximately £2 billion a year.⁵ Other costs include:

- loss in productivity due to premature deaths (£4bn)
- cost to businesses of smoking breaks (£5.8bn)
- smoking-related sick days (£979m)
- social care costs of older smokers (£1.1bn)
- costs of fires caused by smokers' materials (£259m)

Spending on tobacco control measures can help reduce these costs. The report of an inquiry by the All Party Parliamentary Group on Smoking and Health recommended that Government expenditure on tobacco control be increased by an additional £100m a year, which could deliver a return on investment of almost 1100% over 5 years and nearly double the rate of decline of smoking.”⁶

In the 2012-13 financial year the Government spent £87.7 million on the stop smoking services in England plus an additional £58.1m on medicinal aids (e.g. nicotine replacement therapy).⁷ Expenditure on mass media health campaigns on smoking in 2012-13 was £8.21 million.⁸

Fires

Cigarettes and other smoking materials are the primary cause of fatal accidental fires in the home. In 2013-14, smokers' materials accounted for 85 deaths in Great Britain - over a third of all accidental dwelling fire deaths.⁹ Fatalities from this source have fallen by 44% from a peak of 151 in 2001-02.

Smokers' materials are also the third biggest cause of non-fatal casualties in dwelling fires (after cooking materials and other electrical appliances). In 2013-14, there were 673 casualties from smokers' materials and a further 150 non-fatal casualties from cigarette lighters and matches.⁹

International studies

A study commissioned by the US tobacco company Philip Morris examined the economic impact of smoking on the Czech Republic. It concluded that tobacco smoking provided a net benefit to the economy, largely because of "reduced health care costs" and "savings on pensions and housing costs for the elderly" that would not have to be paid since smokers die earlier than non-smokers. In fact, the smoking costs were shown to be 13 times greater than the 'benefits'.¹⁰ A Danish study has shown that tobacco imposes a net cost to society even when taking life expectancy into consideration both in direct and indirect costs¹¹ while a study of the economic effects of a decline in smoking prevalence in New South Wales, Australia, found that the only sector that would be seriously affected would be the tobacco industry.¹²

A World Health Organization study found that 7.4 million lives are likely to be saved as a result of global tobacco control measures.¹³ The biggest impact was found to be increasing cigarette taxes to 75% of their price which should avert 3.5 million premature deaths while smoke-free air laws are expected to save 2.5 million lives. Another study estimated that, in low and middle-income countries in particular, tripling excise taxes on tobacco would reduce consumption by about a third while also increasing tobacco revenues by about a third.¹⁴

Tobacco taxation

The Treasury received £9.5 billion in revenue from tobacco duties in the financial year 2013-2014 (excluding VAT).¹⁵ This amounts to about 2% of total Government revenue. Including VAT, total tobacco revenue is around £12.3bn annually.¹⁶

In 1993, Kenneth Clarke MP was the first Chancellor to explicit state that he intended to raise the tax on tobacco for health reasons, noting that it was "the most effective way to reduce smoking".¹⁷ Since then, apart from the period 2001-2008, successive UK governments have increased tobacco duties above the rate of inflation. (For more information on duty rises, year-by-year see the ASH briefing: [ASH analysis of tobacco tax increases in the United Kingdom](#))

A cost benefit analysis of the effects of increasing tobacco taxation commissioned by ASH found that a tobacco price rise of 5% would result in net benefits to the economy as a whole of around £10.2 billion over 50 years. The economic benefits in the first five years would be around £270m per year on average.¹⁸

VAT on stop smoking aids

In the 2007 Budget, the Chancellor reduced the VAT on nicotine replacement products to the minimum level of 5%, initially for one year.¹⁹ In 2008 this lower rate was extended indefinitely.²⁰

Tobacco smuggling

The price of tobacco is one of the most important factors affecting tobacco consumption. Increasing levels of tax on cigarettes reduces consumption because people respond to the price signal by giving up, cutting down or never starting. However, this policy can be undermined by the illegal importation of tobacco which is sold at reduced rates on the black market.

The illicit trade in tobacco reached a peak in 2000-2001 in the UK when the market share of illicit cigarettes was estimated to be 21%.²¹ However, since then, largely as a result of the Government's strategy to tackle tobacco smuggling, it has fallen to about 10% of the market (mid-point of range of estimates).²² The black market in hand-rolled tobacco has also dropped from an estimated 63% of the market in 2000-01 to about 35% in 2014-15. For further information on tobacco smuggling see [ASH Fact Sheet: Illicit Trade in Tobacco](#).

The tobacco industry

British American Tobacco, the world's second largest tobacco company is based in Britain although virtually all of its products are now manufactured outside the UK. In 2014, BAT produced 667 billion cigarettes worldwide (down from 676 billion in 2013) and reported an operating profit of £4,546 million, a decrease of 17.7% from 2013.²³ The two principal UK tobacco companies - Imperial Tobacco and Gallaher (the latter owned by JTI) - control around 85% of the UK market. For further information see: [ASH Fact Sheet: The UK Tobacco Industry](#).

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