

Globalization of tobacco industry and its impact on Indian revenue

Ashish Samarpit Noel

Sr. Lecturer, Amity School of Business, Amity University, Noida , U. P.

Abstract

Globalization is a multifaceted phenomenon. This subject has assumed great significance in the light of recent changes in the global business environment and national economy. Globalization means adopting a global outlook for the business and business strategies aimed at enhancing global competitiveness. Globalization has made tobacco industry prosperous. The scope of tobacco industry in India is higher as compared to other sectors. Even though the medical issues are negative related to the mentioned sector and the media is always attempting to curtail its growth, the same is indispensable to the economic life of our nation. In India the consumption of addictive has undergone significant transformation from its royal usage to reaching homes of common people. Ethical and medical concerns are many, yet potentiality of tobacco industry is phenomenal and India in this sector could be World's leading player. The paper presents empirical data on the revenues being earned at present due to tobacco industry and highlights the possibility of its enhancement in a much greater magnitude. In accordance with the existing status of the sector its impact on Indian revenue is unveiled in this paper.

INTRODUCTION TO GLOBALIZATION

Globalization is concerned with the application of business practices and processes to take a business or a product global. More specifically, globalization refers to the process of internationalization and localization. Globalization is a multifaceted phenomenon. This subject has assumed great significance in the light of recent changes in the global business environment and national economy. Globalization means adopting of global outlook for the business and business strategies aimed at enhancing global competitiveness.

- **Political and economic level:** At the top political and economic level globalization is the process of denationalization of markets, politics and legal systems, i.e. the rise of so called global economy. The consequences of this political and economic restructuring on local economies, human welfare and environment are the subject of an open debate among international organizations, governmental institutions and the academic world.
- **Business level:** At business level globalization is mainly talked about when companies decide to take part in the emerging global economies and establish themselves in the foreign markets. First of all the linguistics and cultural requirements of the final user is to be studied and thereafter adapted in the products and services of the business. The advantage of online

connectivity with a multilingual corporate website can establish a virtual presence on the international market place.

Although there is much debate in academic and policy circles about the meaning of globalization, the principal argument supporting the idea that globalization comprises a new era in world politics include the following:

- Rapid economic transformation, in which states are no longer closed units and cannot control their economies;
- Electronic communications have fundamentally revolutionized our perception of the social groups we live and work in;
- A global shared culture is emerging;
- The world is becoming more homogeneous with differences between people diminishing;
- A global polity is emerging, which is characterized by traditional social and political movements;
- A cosmopolitan culture is developing people are starting to “think globally and act locally”;
- A risk culture is emerging with the realization that many problems are global and that states cannot deal with these problems on their own.

INTRODUCTION TO TOBACCO INDUSTRY IN INDIA AND REVENUE EARNED

There has never been a name more appropriate than the GOLDEN LEAF for tobacco. Many countries are trying to harness the potential of tobacco. India is one of them. India has just the sun and soil and skills to become among the players in the International market for tobacco. It has the ability to grow the world's most sought after Virginia and Burly tobaccos, that too at a cost no other country could offer. Tobacco was an indispensable economic lifeline of 26 million people in our country during the year 1997-98. Tobacco grows best in dry lands without any irrigation, which means more opportunities for more farmers.

ECONOMIC ANALYSIS OF TOBACCO MANUFACTURING ENTERPRISES

It is estimated that over 2.3 million persons depended on this sector for their livelihood. The annual wage bill in these enterprises averaged Rs 4 300 million, and annual wages per worker varied from Rs 8 400 in bidi factories to Rs 55 730 in cigarette, cigar and cheroot factories. The total net value added by all enterprises averaged Rs 15 000 million per annum, of which bidi factories contributed 41.2 percent, and cigarette and allied industries 34.3 percent. The total annual wage bill in the cigarette and allied industries, despite wages per worker being substantially higher, was only 4 percent of its gross value of output, compared to 16 percent in the bidi factories, because bidi manufacturing is more labour intensive. Bidi manufacturing is estimated to provide employment to more than 4.4 million workers, a large number of whom are women and children. If the forward and backward economic linkages are taken into account, bidis generated 1 310 million workdays, whereas cigarettes generated 340 million workdays

Employment (formal + informal) in the bidi and cigarette industry, 1994/95

	Cultivator	Processor	Manufacturer	Wholesaler	Retailer	Total
Full-time equivalent						
Bidis	140 000	29 300	2 964 000	110 000	1 130 000	4 373 300
Cigarettes	124 000	2 200	10 620	110 666	886 066	1 134 128
Persons employed						
Bidis	290 000	44 000	4 461 000	83 000	757 000	5 635 000
Cigarettes	267 000	3 278	10 620	81 616	543 000	906 090
Workdays (million)						
Bidis	41.5	8.8	889.2	371.1	n.a.	1310.6
Cigarettes	37.1	0.7	3.2	299.0	n.a.	340.2

Note: n.a. = not available.

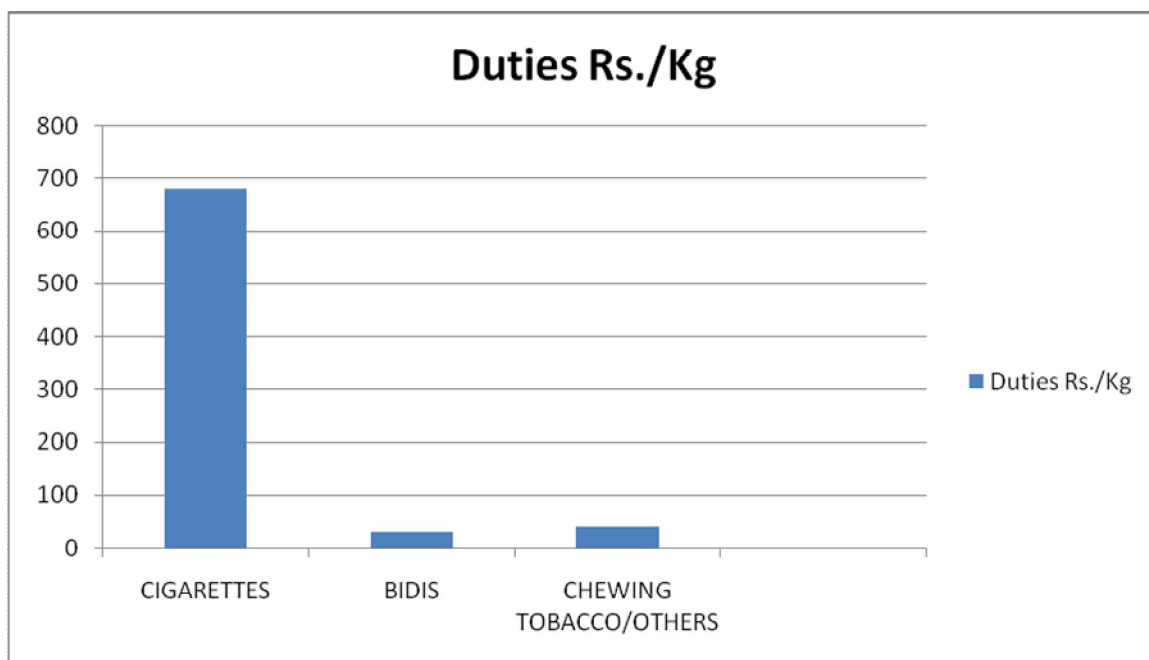
Source: Bidi and Cigarette Industry - A Comparative Status. Indian Market Research Bureau Report, 1996.

DEVELOPMENTS IN TOBACCO CONSUMPTION

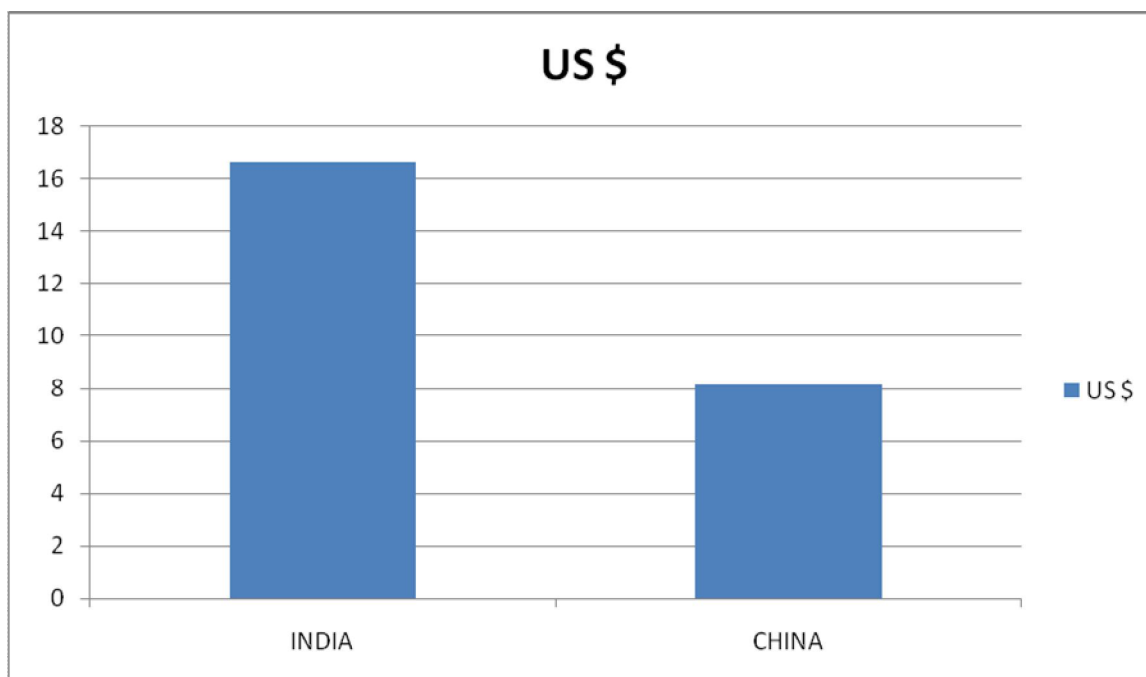
Total consumption of tobacco products has been increasing in India, as in many other developing countries, notwithstanding the increased awareness of negative health effects. Total tobacco consumption increased from around 300 000 tonnes in 1971/72 to 450 000 tonnes in 1998/99 - an increase of 1.6 percent annually. Only about 20 percent of the total tobacco consumed in India (by weight) is in the form of cigarettes. Bidis account for about 40 percent of tobacco consumption (about 950 billion bidis), with the rest divided among chewing tobacco, pan masala, snuff, hookah, zarada and other mixtures. Cigarette smoking is essentially an urban phenomenon: 80 percent of cigarette smokers are in urban areas, while 80 percent of bidi smokers are in rural areas.

Per capita consumption of cigarettes remains very low by international standards. This reflects the lower level of incomes and the substantial use of cheaper alternative tobacco products resulting from traditional habits that are supported by the very low or non-existent taxes on these products. Manufactured cigarettes, on which heavy excise duty is levied, remain unaffordable for many. Per capita consumption of cigarettes declined from 99 pieces in 1990 to 87 pieces in 1993. However, the reduction in taxation on small non-filter cigarettes in 1994 attracted more smokers to switch from bidis, and also encouraged downgrading, both of which have helped increase per capita consumption quite substantially in the latter half of the 1990s. Thus, per capita consumption had reached 108 pieces/year by 1997.

TAX PAID ON TOBACCO PRODUCTS



TAX REVENUE EARNED PER 1000 CIGARETTES (In US \$)



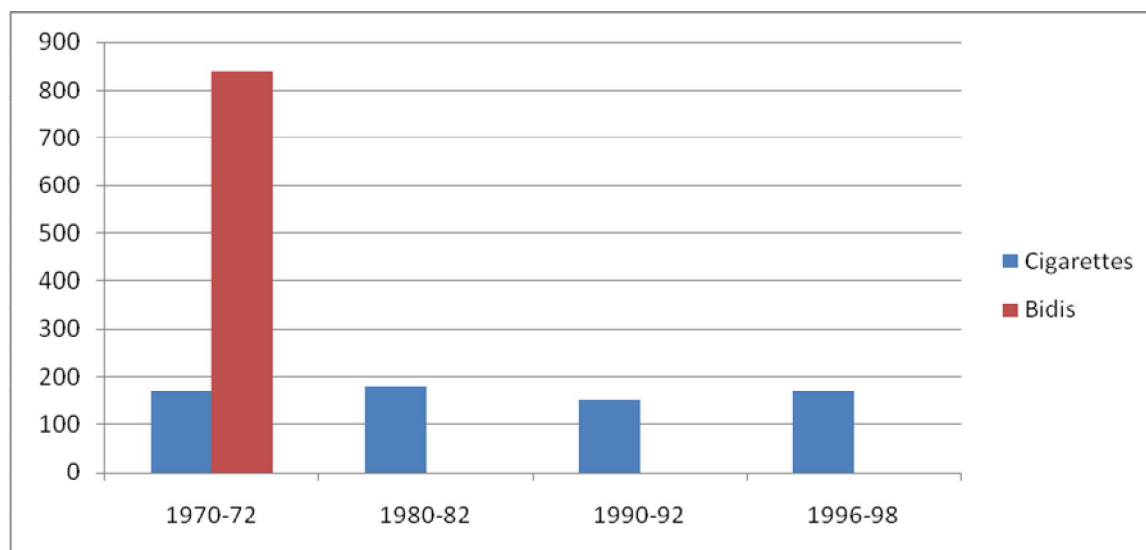
Annual average consumption of cigarettes per adult (aged 15+ years) increased from 170 pieces during 1970-72 to 180 pieces during 1980-82. However, it declined to 150 pieces during the next decade, but recovered to 170 pieces during the last three years. Annual average consumption per adult of bidi increased from 840 to 1350 during 1996-98 (Table 4.12). The increase in consumption in tobacco products in general has been due to population increase, especially the smoking population, higher per capita income in real terms, (which increased from Rs. 1650 in 1970/71 to Rs. 3780 in 1998/99), changing tastes accompanying increased income, changes in prices of various products over time, and, last but not least, government taxation policy. Data on the smoking population are not available except for a survey conducted by NSSO (1996), which provided information on tobacco users in terms of proportion of population. Based on this information, the tobacco using population is estimated to have increased from 201 million in 1986/87 to 203.7 million in 1993/94, or an increase of around half a million annually.

Annual consumption of cigarettes and bidis by adults

Period	Annual average number consumed per adult (aged 15+)		
	Cigarettes	Bidis	Total
1970-72	170	840	1 010
1980-82	180	1 130	1.310
1990-92	150	1 220	1 370

1996-98	170	1 350	1 520
---------	-----	-------	-------

Sources: WHO, 2000; ERC Statistics International, 1998.



The consistent growth of the bidi segment in the smoking market has been partly due to taxation being lower than cigarettes, which has given bidis a considerable price advantage. Other factors supporting rapid growth in demand for bidis include the traditional habit of bidi smoking in the family, which is passed on to the children; the relatively low income level of a large part of the population, especially among the rural masses; and increased use of bidis by women in rural areas in certain states, as there is no inhibition to their smoking. By contrast, the government taxation policy seems to have restricted growth of the cigarette market. From 1970/71 to 1997/98, cigarette taxes increased almost 15-fold (from Rs 31 to Rs 439 per 1 000 cigarettes). This resulted in smokers using more bidis. The Indian tobacco market is highly price sensitive. The price elasticity for cigarette consumption was estimated at -0.66 between 1967/68 and 1992/93, i.e. a 10 percent increase in price would result in a reduction in consumption of 6.6 percent. While increased prices have a constraining affect, the wide use of sponsorship of sport events, publicity and advertisement by the cigarette companies have helped introduce large numbers of young people to cigarette smoking (Vaidya, Vaidya and Naik, 1999).

Based on the NSSO (1998) survey data, the total population using tobacco was estimated at 203.7 million in 1993/94. Among these over 53 percent were smokers and the remaining 47 percent were using non-smoking tobacco products. Chewing tobacco was used by 34 percent of the tobacco using population. Around 12 percent used more than one product. Bidi smokers formed 78 percent of the smoking population.

Total annual private final consumption expenditure (PFCE), in current terms, on tobacco and tobacco products increased from Rs 8 billion in 1970/71 to Rs 236.7 billion in 1998/99. In real terms, based on

official sources (CMIE, 1999) and industry estimates, it increased from nearly Rs 19 billion to Rs 54 billion. The share of tobacco and tobacco products rose from 2.6 percent of PFCE in 1970/71 to 2.9 percent. The cigarette segment accounted for 37 percent of total consumer spending on tobacco, while the bidi segment contributed 30 percent. The corresponding figure for the non-smoking sector was 33 percent. However, while for cigarettes as much as 61 percent of the total consumer spending went towards government excise revenue, the corresponding figure for the bidi segment was 5 percent. Moreover, the figure for the non-smoking sector, which has the highest share in consumer expenditure, was also only 4 percent in 1998/99. The annual spending per tobacco user was Rs 1 150. Annual expenditure per smoker is estimated to have been Rs 2 750 for cigarettes and Rs 835 for bidis, while for non-smoking tobacco users it was Rs 906.

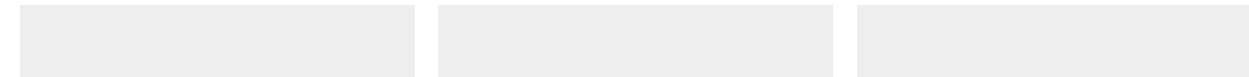
Government policy regarding consumption of tobacco products applies mainly to its taxation measures and a limited control on use of tobacco products. The motivating rationale for tobacco taxation seems to be fiscal (i.e. to maximize the excise revenue). Measures to control the use of tobacco on health grounds seem to have had only a small impact, partly because only a few control measures are in place, and those are not fully implemented. These measures include bans on advertising cigarettes, but applied only on television and commercial radio stations; a single health warning on cigarette packets; and bans on smoking in public places, but in only three States.

Budget over the years

Budget 2004-05	Budget 2005-06	Budget 2006-07
Increase in excise duty on matches made in the mechanised/semi-mechanised sector from 8% without Cenvat credit to 16% with Cenvat credit	Specific rates on cigarettes raised by 10% Surcharge of 10% imposed on ad valorem duties on other tobacco products including gutka, chewing tobacco, snuff and pan masala Excise on matches made by mechanized or semi-mechanized sectors reduced from 16% to 12%.	Excise duty on cigarettes increased by 5%. Excise on unbranded other smoking tobacco and unmanufactured tobacco and tobacco substitutes at 16%. Tariff rate of excise duty on bidis increased. Excise exemption to small-scale smoking tobacco and

However, no excise on tobacco substitute
hand made matches. manufacturers restricted
to Rs 1 m.

Excise duty on all types of
pan masala rationalized at
66%.



FINDINGS

KEY POSITIVES

- Habitual industry: Despite high government intervention and campaigns against smoking along with high tax rates, the industry continues to thrive. Also, ban on smoking in public places and restrictive advertising has not stopped this industry from growing.
- Excise an easy pass on: Since it is a habit industry, companies find it comparatively easy to pass on excise duty hikes. Last year, the government increased excise by 10%, but it was easily passed on to consumers, without demand being affected.
- Per capita consumption ridiculously low: The per capita consumption of cigarettes in India is merely a tenth of the world average. Thus, as disposable incomes increase, people might shift from bidis to cigarettes and hence there lies a huge potential to convert. Being the No. 1 player in the segment, ITC is likely to be a big beneficiary of this change.

KEY NEGATIVES

- Heavily penalized through punitive taxation policies: Cigarette companies pay roughly 50% of their revenues as excise. As a result, the share of cigarettes in total tobacco consumption has declined from 21% in 1981-82 to a mere 14% in 2004.
- Domestic cigarette companies suffer a double whammy: On the one hand, they are barred from sponsoring sports and cultural events and on the other hand, contraband cigarette volumes continue to thrive. Net result, volume growth is sluggish. In the last 20 years, tobacco consumption in non-cigarette varieties has increased especially in the chewing format by 68 m Kgs, and reduced in the cigarette format by 21 m Kgs.

CONCLUSION

Tobacco production is an important source of income for India's farmers. While alternative crops are available in terms of agronomic suitability, in general a move away from tobacco production would result in reduced income and food security for a considerable number of farmers. Manufacturing, particularly of bidis, is also a source of employment and hence of income for a large number of people. Thus any attempts to control the use of tobacco would need to take into account the economic impact on these sectors.

To be effective, measures to control the use of tobacco would need to address all forms of consumption, not only cigarettes. In particular, this would mean dealing with the economic and political difficulties of taxing, or otherwise controlling, bidis and other non-cigarette forms of tobacco consumption.

REFERENCES

- Vaidya, S.G., Vaidya, J.S., & Naik, U.K. 1999) Results of a national study in India: sport sponsorship by cigarettes companies influences the adolescent children's mind and helps initiate smoking. *Journal of the Indian Medical Association*, 97(9): 354-356, 359.
- CMDR (Centre for Multidisciplinary Development Research). 2000. Economics of shifting from tobacco cultivation, 1997-2000. CMDR, Dharward, Karnataka. Study sponsored by Research in Tobacco Control, IDRC, Canada.
- CMIE (Centre for Monitoring the Indian Economy). 1999. National Income Statistics, November 1999. Economic Intelligence Service, CMIE.
- CTRI (Central Tobacco Research Institute). 1999. Status Report on Research Programme on Alternative Crops to Tobacco. CTRI, Indian Council of Agricultural Research, Rajahmundry, Andhra Pradesh.
- Kiremath, G.K. 2000. Economics of bidi vs competing crops. Paper presented at the Tobacco Seminar. 29-30 November 2000, CMDR, Dharward, Karnataka.
- DES (Directorate of Economics and Statistics, Ministry of Agriculture). 2000. Cost of Cultivation of Principal Crops in India.

- ERC Statistics International Plc. (1998). India. pp. 1-38, in World Cigarette Report, 1998.
- NCAER (National Council of Applied Economic Research). 1994. Export potential of the tobacco sector. Study, including sample survey carried out through the Rapid Rural Appraisal technique, sponsored by the Tobacco Institute of India, New Delhi.
- NSSO (National Sample Survey Organization). 1996. Survey on household consumer expenditure. SARVEKSHANA, No. 69 (October-December). Department of Statistics, Ministry of Planning and Programme Implementation, Government of India.
- NSSO. 1998. A note on consumption of tobacco in India. NSS 50th Round (1993-94). SARVEKSHANA, 21(3). (No. 74, January-March)
- Panchamukhi, P.R. 2000. Economics of shifting from tobacco: an action-cum-basic research study. In: CMDR, 2000, q.v.
- Rath, G.K., & Chaudhry, K. 2000. Cost of tobacco-related diseases. Paper presented at the WHO International Conference on Global Tobacco Control Law: Towards a WHO Framework Convention on Tobacco Control. 7-9 January 2000, New Delhi.
- WHO (World Health Organization). 1997. Tobacco or health: a global status report. Geneva: WHO.