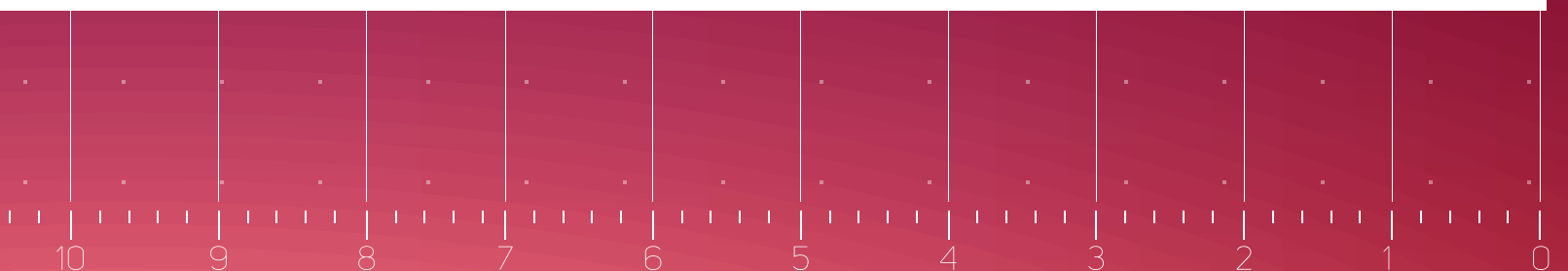




# TOBACCO TAX PASS-THROUGH IN MONTENEGRO



### KEY FINDINGS:

- The tobacco industry's pricing tactics differ across market segments of tobacco products, which enables them to keep a wide price gap between premium and cheaper products.
- The results show that the industry does not significantly change the price of the cheapest products when excise taxes increase, but instead transfers the costs to the premium and most expensive brands.
- Slim cigarettes on average have lower prices, so are more affordable compared to other types of cigarettes, and their prices increase less than excise tax increases ("under-shifting").
- The tobacco market in Montenegro is still characterized by low prices of cigarettes, with the average price of the most-sold brand being in the range of 2.3 to 2.7 euros in the last five years.

### BACKGROUND INFORMATION

The tobacco industry employs a variety of pricing strategies and tactics to balance their business and profits. These tactics vary in relation to the different market segments of tobacco products, balancing between volume and price, which enables them to keep generating high profit margins. To understand the overall pricing policies, the main objective of this research is to estimate the extent that tobacco tax changes are passed through to smokers in Montenegro. To achieve this goal, ISEA's study uses price data from the Tobacco Agency on manufactured cigarette brands traded in Montenegro between 2010 and 2022.

The tobacco market in Montenegro depends on imports, and currently there are approximately 100 different brands available with only limited variation in price. The weighted average price of cigarettes (WAPC) increased gradually in recent years, reaching 2.8 euros in 2023. Taxes have changed semi-annually in the years 2022 and 2023. As of the end of 2023 the specific excise tax is 49 euros per 1,000 sticks of cigarettes, and the ad valorem tax is 24.5 percent of the retail price. With the minimum excise tax (as of July 1, 2023) of 83.5 euros per 1,000 cigarettes, Montenegro is still below the European Union Tax Directive minimum threshold of 90 euros per 1,000 cigarettes and the average tax burden in the European Union.

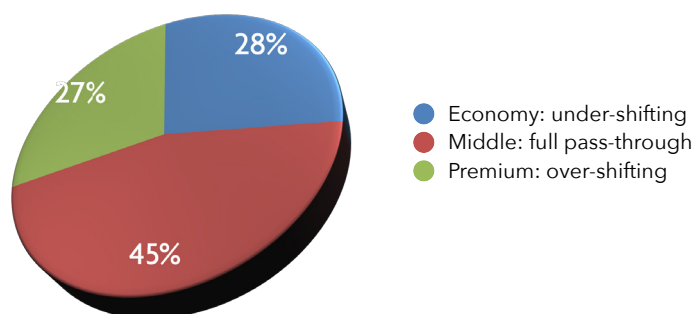
### RESULTS:

The tobacco industry's most utilized strategies are under- and/or over-shifting tax increases, meaning that the tobacco industry increases the price of tobacco products less/more than the tax increase requires, often affecting the effectiveness of tobacco control tax policy. The available data on prices in Montenegro shows higher variability in prices of premium brands compared to the most-sold and economy brands. This is why the analysis based on prices of those brands incorporates the market segmentation.

- To maintain or increase profits, the tobacco industry's strategy is to keep the price of the cheapest products at a low level while increasing the price of more expensive brands (Figure 1). The excise tax increase as a cost for the industry is mostly passed on to the consumers of premium brands, who are typically less sensitive to changes in price, which enables the tobacco industry to keep generating high profits. The estimates suggest that the prices of cheaper cigarettes are not increased beyond the tax increase. The same results are obtained when the analysis is conducted by three market tiers (Panel A: economy, mid-price, and premium) or 11 quantiles (Panel B).

**Figure 1. Pass-through of excise taxes on market segments**

Panel A

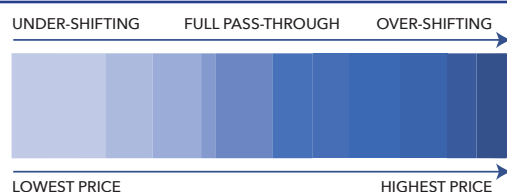


**Under-shifting:** the prices are increased less than the excise tax increase.

**Over-shifting:** the prices are increased beyond the excise tax increase.

**Full-pass through:** the cost of tax increase is fully passed to consumers.

Panel B



- Cigarettes in Montenegro continue to have low prices. In general, there is a small difference (measured in cents) between prices in the economy and mid-price segments, which combined make up more than 70 percent of the market share.
- Because 84.8 percent<sup>1)</sup> of smokers who consume slim cigarettes—most of which are relatively less expensive—are female, this result is in line with studies showing that the industry's current strategy is focused considerably on females and youth.
- Slim cigarettes are mostly consumed in the economy and mid-price segments. In the segment with the cheapest products (economy tier), the share of slim cigarettes increased from 32 percent in 2010 to 54 percent in 2022.

## RECOMMENDATIONS FOR PUBLIC HEALTH-PROMOTING POLICY CHANGE:

- Instead of gradual tax increases, which have a more limited effect on consumption, the Government of Montenegro should implement accelerated change with higher specific excise tax increases. It is difficult for companies to absorb larger increases, and this will serve to raise prices across all market segments beyond the tax increase. This would lead to lower affordability of tobacco products, which is especially important in reducing consumption by consumers of cheaper brands.
- Tobacco tax policies typically work best in combination with other proven interventions. One key proven policy is to make cigarette packaging visually less appealing, with the most effective strategy being the introduction of plain/standardized packaging. The existing evidence shows that the industry often replaces the removal of descriptors with a variety of colors that give the perception of safety and/or healthier products (such as using the color blue to evoke lightness). Logos are also widely recognized even by small children and subtly promote these harmful products.
- Government should launch anti-smoking campaigns to raise awareness of smoking's adverse effects, including among females and young people, who are the current main targets of tobacco marketing. This non-price measure represents a very strong tool to combat high prevalence of tobacco use. At the same time, it is vital to strongly enforce existing bans on tobacco advertising, promotion, and sponsorship.

1) [Dataset] institute for socio-economic analysis. Data from: survey on tobacco consumption in montenegro, 2022.



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