

TOBACCO TAX INCREASES

**CAN REDUCE
TOBACCO USE**



This Policy Brief was produced based on the background study for Mexico “Analysis of tobacco taxation and simulations in Mexico using LATINMOD”

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Introduction

In Mexico, smoking is estimated to cause around 117 deaths a day. Despite this, the number of smokers has increased in recent years, particularly among adolescents and women. Tobacco use remains a major public health problem as the cause of various diseases that incur high healthcare costs for the Government.

Revenue from tobacco taxes has never been sufficient to cover this financial burden. An increase in tobacco taxes is the best way to ensure that smokers reduce their consumption, while providing the Government with the necessary resources to offset a greater share of total healthcare expenditure.

Tobacco: higher taxes, lower consumption

Tobacco excise is the most direct way to increase the final retail price of cigarettes. In Mexico, between 2001 and 2011, various tobacco excise tax reforms were enacted, which increased the final retail price of a pack of cigarettes by 52 percent. Over the same period, cigarette consumption fell by 36 percent. The 2011 reform increased the fixed component of excise tax from 0.04 to 0.35 pesos per cigarette. However, this tax has remained unchanged until 2020, undermining its effect on reducing tobacco use.

Various countries, including Chile, Brazil, the United States, France, China, Moldova, and Ukraine have achieved a significant reduction in cigarette consumption through a substantial increase in excise taxes and final retail prices.

Increases in the retail price of cigarettes have a preventive effect by hindering access to tobacco products for the young, thus preventing early smoking initiation. An increase in the fixed excise tax per cigarette not only impacts the final price of a pack of cigarettes, but also the cost of loose cigarettes, more easily purchased by young people and people in lower income groups.

¿By how much should tobacco excise be raised?

Tobacco products are subject to two types of tax: Value-added Tax (at a rate of 16 percent) and the Excise

Tax on Production and Services - IEPS (at a rate of 160 percent plus a fixed component per cigarette). In 2019, the total tax burden for tobacco accounted for 68% of the final retail price. The World Health Organization recommends a total tax burden of 75% to achieve an impact on consumption (WHO, 2015).

Starting in 2020, the fixed component of the excise tax increased from 0.35 to 0.4944 pesos per cigarette to adjust for inflation. This change raised the total tax burden by just 2 percent, bringing it up to 70 percent of retail price.

However, this measure will prove inadequate to achieve any significant impact on consumption, as it remains far below the WHO recommendation. In order for the tax burden to represent 75 percent of the retail price, the fixed component of the excise tax needs to be raised to 1.35 pesos per cigarette. Assuming full pass through of the tax, this reform would result in a 49 percent increase in the price of a pack of cigarettes, which would go from 52 to 77.7 pesos (Figure 1).

Figure 1. Final price of a pack of cigarettes: Mexico.



Source: Own work using LATINMOD and ENIGH 2016.

An increase in the price of a pack of cigarettes leads to a decrease in consumption

In 2020, cigarette consumption is expected to fall by just 4.8% as a result of the tobacco excise reform (Reform 1 in Figure 2). By comparison, when the tax burden represents 75% of the retail price, consumption can be reduced by almost 34% (see Reform 2 in Figure 2).



The current increase in tobacco tax will reduce consumption only very slightly



The price of a pack of cigarettes can be compared across countries in international dollars: a unit of currency adjusted for purchasing power in each country. In 2016, the retail price of the most popular brand sold in Mexico was 5.67 international dollars, less than in other countries in the Americas such as the Bahamas (\$8.97), Canada (\$8.54), Chile (\$5.75), Ecuador (\$9.58), the United States (\$6.43), Panama (\$7.17), and Peru (\$6.63), to name just a few (PAHO, 2018).

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In Mexico, a tobacco tax reform equivalent to 1.35 pesos per cigarette

would reduce consumption by 34%

and increase revenue **by 38.2%**

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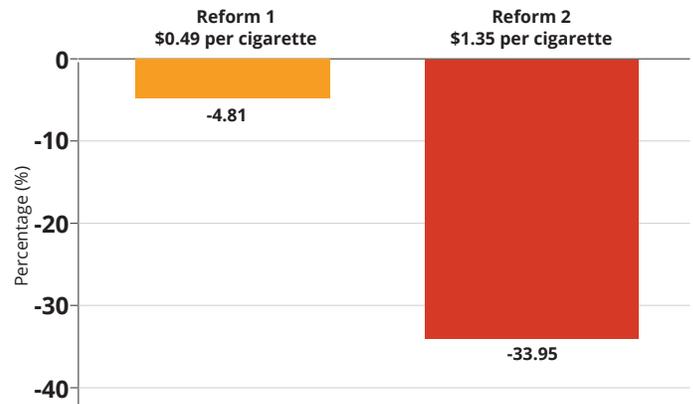
In Mexico, a large share of 12 to 65-year-olds would support such a reform. According to ENCODAT, 71.3 percent of the general public and 53.3 percent of smokers would agree with a tax increase. Similarly, 65.8% of adolescents in Mexico welcome higher taxes on cigarettes (Reynales et al., 2017).

There is, therefore, a favorable social environment to promote a reform of the fixed excise tax to increase cigarette prices as necessary to discourage consumption.

Conclusion

Cigarette consumption is an ongoing problem in Mexico and it is of utmost importance to fight it urgently with tax increases. The tax increase under the 2020 reform will reduce consumption by less than 5%. It is therefore necessary to take heed of the WHO recommendations.

Figure 2. Reduction in cigarette consumption in Mexico



Source: Own work using LATINMOD and ENIGH 2016.

This recommendation would not just align tobacco taxes and prices internationally, but would also bring about a swifter reduction in consumption. A tax reform bringing the fixed component of excise tax up to 1.35 pesos per cigarette would make it possible to reduce consumption by 34%.

This would save on public healthcare costs for tobacco-related diseases and raise Mexicans' standard of health, allowing Mexico to join the ranks of other countries.

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