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# **United Kingdom**

## **Tobacco and Products**

### **Annual**

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#### **Report Highlights:**

UK production of cigarettes is forecast to remain at 150 billion pieces in CY2001, of which over two thirds are expected to be exported. As such, UK import demand for unmanufactured tobacco remains under pressure. Around 30 percent of the UK's adult population, or 15 million people, smoke with a total annual duty-paid expenditure of around USD18 billion. With the high taxes on tobacco in the UK allegedly fueling a tobacco black market, it is estimated that taxes are not paid on an estimated 33 percent of all cigarettes smoked. Indeed, the success of the black market is such that while consumption of duty-paid cigarettes is in sharp decline, total consumption of cigarettes increased in CY2000, the first rise in 10 years.

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Includes PSD changes: Yes  
Includes Trade Matrix: Yes  
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## Explanatory Notes

### Stocks

The format of the production, supply and demand (PSD) tables for cigarettes featured in this report makes no allowances for stocks. The trade information is, therefore, distorted when it is reported in the PSD and in turn affects the supply and distribution totals. To remedy this problem the actual market conditions are described in separate tables within the body of the text. References to market data therefore relate to these tables and not the traditional PSD tables which for cigarettes can be found in the statistical appendix.

### Exchange Rates

This report refers to sterling's competitiveness against other currencies. The following table provides yearly average exchange rates for sterling against the U.S. Dollar and the European Currency Unit (ECU) which was replaced by the Euro on 1 January, 1999.

From 1996 through 1999 sterling appreciated in value relative to the ECU/Euro and the U.S. dollar. However, a decline in sterling's value against the dollar, starting in 1999, has been followed by a loss of value against the Euro in 2001. This has gone some way to increasing the competitiveness of UK tobacco products on export markets in recent times.

EXCHANGE RATES		
Year	ECU per BPS	USD per BPS
	(Euro per BPS	
	for 1999 and 2000)	
1994	1.2897	1.5316
1995	1.2070	1.5785
1996	1.2286	1.5610
1997	1.4431	1.6393
1998	1.4789	1.6570
1999	1.5192 (1)	1.6179
2000	1.6419	1.516
2001 (2)	1.588	1.4541
(1) Euro superceded ECU from January 1, 1999		
(2) January - April 2001 average		
Source: Bank of England		

Note: Throughout this report the rate of exchange used is BPS 1 = USD 1.45

## Executive Summary

The structure of the UK tobacco industry is dominated by three national companies – Gallaher Ltd, Imperial Tobacco Ltd and Rothmans (UK) Ltd. All three, which predominantly produce cigarettes but also manufacture hand rolling and pipe tobaccos and cigars, are increasingly looking to develop their overseas sales. Rothmans achieves this through its foreign arm, British American Tobacco, which manufactures cigarettes in the UK for export but does not sell domestically.

This report focuses on unmanufactured tobacco and cigarettes, the two most important elements in the UK tobacco market. Although the UK imports all of its tobacco leaf, it is a substantial exporter of finished tobacco products, mainly cigarettes, to the Far and Middle East and Eastern Europe. In CY2000 the UK tobacco export market was worth over BPS1 (USD1.45 ) billion. Imports of unmanufactured tobacco have fallen in recent years, in line with the parallel decline in cigarette production. This has followed the decline in export demand in the late 1990s following the economic downturn in the Far East and the reduction in domestic demand for duty-paid cigarettes. Although the UK's main export markets are now showing some recovery, UK cigarette production is expected to remain at around 150 billion pieces in CY2001 with any increase in export demand being met from the large stocks of cigarettes held in the UK. As such, imports of unmanufactured tobacco will remain under pressure.

There are currently some 15 million adult smokers representing about 30 percent of the adult population in the UK. Total duty paid consumer expenditure on tobacco products reached BPS12.5 (USD18.125 ) billion in CY2000, this being spent on 56 billion cigarettes, 2,100 tons of hand rolling tobacco and 900 million cigars. However, these figures may mask the true total UK expenditure on and consumption of tobacco products as many consumers turn to personal or black market imports. For example, officially reported UK cigarette sales to the trade have declined 38 percent since 1993. In reality cigarette consumption has remained fairly steady at around 84 billion with non-duty paid consumption of cigarettes on the increase. Indeed, CY2000 consumption of non-duty paid cigarettes is thought to have accounted for around a third of the total with the availability of cheaper non-duty paid cigarettes actually leading to a slight rise in cigarette consumption, the first in 10 years.

UK taxes on tobacco products, which generated almost BPS10 (USD14.5) billion in CY2000 amounting to over 3 percent of all UK Government taxation, keep cigarettes in the UK well above prices in the rest of the EU (and nearly four times as high as some). While government initiatives to stop smuggling may curb the illegal imports somewhat, tobacco price differentials between the UK and other EU countries will continue to provide incentives to smugglers and UK tobacco product consumers. Government anti-smoking initiatives may eventually reduce domestic consumption but these figures are not expected to decline by much in the near future.

## Unmanufactured Tobacco

### PSD Table

PSD Table						
Country	United Kingdom					
Commodity	Tobacco, Unmfg., Total				(HA)(MT)	
	Revised	1999	Preliminary	2000	Forecast	2001
	Old	New	Old	New	Old	New
Market Year Begin		01/1999		01/2000		01/2001
Area Planted	0	0	0	0	0	0
Beginning Stocks	34814	124814	25352	105352	35000	83000
Farm Sales Weight Prod	0	0	0	0	0	0
Dry Weight Production	0	0	0	0	0	0
U.S. Leaf Imports	4339	4339	4500	3764	0	4000
Other Foreign Imports	132844	132844	131000	104663	0	100000
TOTAL Imports	137183	137183	135500	108427	0	104000
TOTAL SUPPLY	171997	261997	160852	213779	35000	187000
Exports	33745	33745	30000	10944	0	10000
Dom. Leaf Consumption	0	0	0	0	0	0
U.S. Leaf Dom. Consum.	4000	4000	3750	3500	0	3750
Other Foreign Consump.	108900	118900	92102	116335	0	116250
TOTAL Dom. Consumption	112900	122900	95852	119835	0	120000
TOTAL Disappearance	146645	156645	125852	130779	0	130000
Ending Stocks	25352	105352	35000	83000	0	57000
TOTAL DISTRIBUTION	171997	261997	160852	213779	0	187000

UK imports of unmanufactured tobacco fell 21 percent in CY2000, down for the fifth year running largely as a consequence of reduced production of cigarettes. The high cost of cigarettes in the UK due to tax policy has somewhat slowed domestic demand for tobacco products. Brazil, Zimbabwe, India and Italy remain the UK's greatest suppliers with most of Italy's leaf being transhipped product from Sri Lanka and India. Leaf imports from the U.S. fell a further 13 percent in CY2000 to 3,764 tonnes and are expected to remain about the same in CY2001.

UK exports of unmanufactured tobacco remain small. After CY1999, which unusually saw Germany featuring as a major destination for exports and boosting the export volume, CY2000 saw a return to a more traditional picture with just under 11,000 MT exported. France and Italy were the major destinations. CY2001 is expected to see a continuation of this trend.

UK consumption of tobacco leaf fell just 3 percent in CY2000, reflecting the stabilizing of cigarette production in the UK. With cigarette production forecast unchanged and imports expected to remain down in volume,

CY2001 will see a further draw down in stocks of unmanufactured tobacco.

### Trade Matrices

Import Trade Matrix			
Country	United Kingdom		
Commodity	Tobacco, Unmfg., Total		
Time period	Jan - Dec	Units:	MT
Imports for:	1999		2000
U.S.	4339	U.S.	3764
Others		Others	
Brazil	35728	Brazil	23292
Zimbabwe	24735	Zimbabwe	22539
Italy	13866	Italy	10151
India	11297	India	9573
Belgium Lux	7448	Belgium Lux	5541
Canada	5904	China	4445
Greece	5250	Spain	4072
Spain	4499	Argentina	3279
China	4395	Uganda	3066
Thailand	2479	Tanzania	3045
Total for Others	115601		89003
Others not Listed	17243		15660
Grand Total	137183		108427

Export Trade Matrix			
Country	United Kingdom		
Commodity	Tobacco, Unmfg., Total		
Time period	Jan - Dec	Units:	MT
Exports for:	1999		2000
U.S.	2	U.S.	2
Others		Others	
Germany	21918	France	4251
France	4764	Ireland	4022
Ireland	3477	Russia	600
Russia	987	Netherlands	318
Poland	615	Cote d'Ivoire	300
Spain	515	Canada	297
Netherlands	294	Spain	211
Italy	221	Germany	160
Canada	161	Rwanda	154
Senegal	146	Singapore	137
Total for Others	33098		10450
Others not Listed	647		492
Grand Total	33747		10944

## Cigarettes

	1998	1999	2000	2001 (f)
Opening stocks	198494	273215	648730	703513
Production	163547	155000	150000	150000
Imports	85536	382597	71801	70000
Exports	103862	100349	111006	871513 (1)
Duty-paid consumption	70500	61733	56012	52000
Private/Illegal Imports	13500	22000	28000	32000
Total consumption	84000	83733	84012	84000
Closing stocks	273215	648730	703513	0
(1) Total available to export/re-export during 2001				

## Production

UK cigarette production is estimated at 150 billion in CY2001, a cessation of the downward spiral in production which has been characteristic of the sector since 1997. Although domestic consumption of duty-paid cigarettes is forecast to continue to decline due to the ongoing high tax policy and anti-smoking campaigns in the UK, some recovery in export demand is forecast following the recovery of the Far Eastern markets, a major destination for UK produced cigarettes, and a depreciation of the pound relative to both the Euro and the U.S. dollar.

The cigarette market is dominated by three major companies who command more than 90 percent of the total market.

### UK Company Market Share (1999)

Gallaher	39.50
Imperial	38.00
BAT/Rothmans	13.75
R.J. Reynolds	2.25
Other	6.50

## Consumption



In recent years, the UK cigarette market has been characterized by down trading - as the price of duty paid cigarettes has risen, cigarette smokers have increasingly looked for alternatives to their usual brands. For many, this has meant down trading from premium to middle-priced brands although in many cases this has been a temporary move before the inevitable move to an economy or ultra-low price brand. The major companies have reacted to consumer demand for cheaper cigarettes by launching their own economy brands which have proved very successful. According to industry estimates, the lower priced sector accounts for 23 percent of the total market and is likely to keep growing. However, many trade down even further to smuggled cigarettes where premium brands cost just over half the price of the legal equivalent and nearly BPS1 (USD1.45) lower than the cost of the lowest ultra-low price brand. Indeed, such is the success of the cigarette black market that while consumption of duty-paid cigarettes continued its sharp decline in CY2000, total consumption of cigarettes increased, the first such rise in 10 years. Interestingly, those who trade down to hand rolled tobacco will likely be smoking smuggled goods - around 80 - 90 percent of the RYO market is allegedly accounted for by illegal imports.

The majority of cigarettes in the UK are sold in convenience stores (more than 65 percent) with a further 27 percent sold in the major retailers.

#### Top 10 Brands in the UK

Lambert & Butler KS
Benson & Hedges KS
Mayfair KS
Superkings
Rothmans Royals KS
Silk Cut KS
Regal KS
Marlboro Lights KS
Embassy No 1 KS
Sovereign KS

#### Trade

The UK maintains a positive trade balance in the cigarette market, exporting around two thirds of all production. The most important export markets for the UK in value terms are Belgium and the Netherlands in the EU, Singapore, Hong Kong and Taiwan in the Far East and Saudi Arabia in the Middle East. The financial difficulties in the Far East translated into a nearly 25 percent reduction in the value of cigarette exports into this region in CY1999. CY2000 saw some improvement and it is hoped by many in the trade that this trend will continue in CY2001 as the fortunes of many of the Asian economies recover. While UK manufacturers are not enjoying the same advantages they had in the early 1990's, due to the appreciation of the pound in more recent years, they continue to value the UK as a good base for exports.

Nearly all of the UK's recorded cigarette imports come from other EU countries. In addition to the legal import of nearly 72 billion cigarettes in CY2000 it is estimated that around 28 billion cigarettes entered the country as personal or illegal imports, the latter accounting for the bulk of this total. CY2001 is expected to see a further

increase in the smuggled volume at the expense of duty paid imports.

### Trade Matrices

Import Trade Matrix			
Country	United Kingdom		
Commodity	Tobacco, Mfg., Cigarettes		
Time period	Jan - Dec	Units:	Million pieces
Imports for:	1999		2000
U.S.	51	U.S.	2523
Others		Others	
Germany	316544	Germany	56262
Greece	49410	Greece	8224
Netherlands	9934	Netherlands	1596
Denmark	1664	Belgium-Lux	1092
Japan	1200	Denmark	1067
Switzerland	1195	France	740
Canada	862	Ireland	208
Belgium Lux	414	Austria	41
France	377	Switzerland	12
Sweden	360	Portugal	12
Total for Others	381960		69254
Others not Listed	586		24
Grand Total	382597		71801

Export Trade Matrix			
Country	United Kingdom		
Commodity	Tobacco, Mfg., Cigarettes		
Time period	Jan - Dec	Units:	Million pieces
Exports for:	1999		2000
U.S.	780	U.S.	523
Others		Others	
Singapore	13740	Dubai (UAE)	10844
Spain	11010	Singapore	10301
Hong Kong	7141	Greece	9142
Cyprus	6230	Hong Kong	5826
Netherlands	5648	Netherlands	5649
Belgium	5175	Kuwait	5554
Falkland Islands	5147	Cyprus	5404
Saudi Arabia	3672	Saudi Arabia	5402
South Korea	3604	France	5385
Taiwan	3290	Spain	5348
Total for Others	64657		68855
Others not Listed	34912		41628
Grand Total	100349		111006

## Policy Issues

### Tax Policy and Prices

UK Government policy towards tobacco taxes has remained largely unchanged since the early 1990's despite a change of administration: to reduce consumption (particularly in children under the age of sixteen) thereby reducing the burden on the national health service of smoking-related diseases and to increase revenue. With above inflation annual increases on tobacco taxes effectively becoming the norm, the UK tobacco sector is one of the most heavily taxed in the world and UK cigarette prices are the highest in the EU, with taxes accounting for around 80 percent of the retail cost of a typical packet of cigarettes. With prices approximately double those in nearby France, Belgium and the Netherlands, smuggling is a major problem.

Most Popular Price Category Cigarette across the EU (April 2001)  
(Package of 20)

	Retail Price	VAT	Ad Valorem	Specific	Total Tax	Tax Incidence
UK	433	64	95	185	344	79.5
Ireland	301	50	57	128	235	78.1
Denmark	265	53	56	101	210	79.1
Finland	247	45	124	19	187	75.6
Sweden	247	49	97	27	173	70.2
France	207	35	114	8	158	76
Belgium	179	31	82	19	133	74.1
Germany	183	25	40	61	126	68.9
Netherlands	169	27	35	62	124	73
Austria	166	28	70	24	121	72.9
Italy	134	22	73	5	100	74.5
Greece	136	21	73	4	98	72.4
Luxembourg	134	14	63	13	90	67.3
Portugal	114	17	30	43	90	78.6
Spain	110	15	59	4	78	71.2

Source: Tobacco Manufacturers Association

### Smuggling – Anti Smuggling Initiatives

The UK government estimates CY2000 revenue losses of BPS3.8 (USD5.5) billion up from BPS2.7 (USD3.9) billion the previous year due to smuggling activities. These figures take into account the value of excise duty and Value Added Tax (VAT) on the smuggled products and do not include revenue lost as a result of legitimate cross-border shopping. Estimates suggest that around a third of all cigarettes sold in the UK in CY2000 were non-duty paid. Much has been made of the losses to the retail trade as a result of smuggling.

According to industry sources, without a change in UK tax policy, the trend toward an increase in cigarette smuggling will continue. The industry's position is that the high incidence of smuggling has made low priced cigarettes widely available (black market prices range from BPS2.00-2.50 per pack) and therefore reduced the effectiveness of UK tax policy in curbing smoking. Indeed, they argue that the UK tax policy is exacerbating the switch by many consumers to non-duty paid cigarettes, thereby reducing the tax revenue collected.

In CY2000, UK Customs & Excise seized 2.1 billion illegal cigarettes. An increase in the number of officers, the introduction of mobile scanners and the installation of "catsclaw" systems which burst the tyres of fleeing vehicles is under way at some ports but Customs accepts that its short term aim is to simply slow the growth in smuggling which is increasingly being linked to organised crime. Additionally the UK Government is endeavouring to increase the publicity of the problem through advertising and the introduction of duty-paid marks on cigarettes and other tobacco products (see below).

### **Anti-smoking initiatives**

The UK government has made reducing the incidence of smoking a key health objective. In addition to its policy of high taxes, it has supported wholeheartedly various EU directives to curb smoking.

In December 2000, the UK government announced it was considering a blanket ban on all tobacco advertising following the collapse of the EU directive on the same. At present the proposal is going through Parliament. Once implemented, the new regulations would take three months to take effect. The most likely outcome is a total ban on tobacco branding or advertising within retail outlets, such as price lists, posters on windows, sponsored blinds or displays.

The UK Government has also introduced a duty paid mark on cigarettes and hand rolling tobacco, the two smuggling problem areas, but opinions are divided on the effectiveness of this scheme. As of July 1, 2001 no packs without the mark can be legally sold in the UK.

## **Other Products**

### **Roll Your Own (RYO)**

The RYO market is the second most important tobacco market in the UK growing in popularity as duty-paid cigarette prices have skyrocketed. The same manufacturers are producing this product with Gallaher's Samson and Imperial's Drum among the most popular brands. It is estimated that almost 80 percent of the RYO products on the UK market in CY2000 were non-duty paid, having been smuggled into the country. Unofficial estimates suggest that of the total 9,425 tons consumed, just 2,100 tons was duty paid. The RYO market is expected to continue increasing in popularity as long as UK cigarette taxes remain high.

### **Cigars**

The UK cigar market is worth approximately BPS500 (USD750) million, with consumption in CY2000 totalling approximately 900 million cigars. Overall cigar consumption has been declining for the past 5 years in the UK. However within the sector, small cigars have become particularly popular with approximately 25 percent of all sales. Gallaher's Hamlet brand commands 50 percent of the market here competing with Imperial's Classic and King Edward Coronets and with Henri Winterman's Slim Panatellas.

### **Pipe Tobacco**

There are an estimated 500,000 pipe smokers in the UK who consumed between 700-800 MT of tobacco in CY2000. This market was estimated to be worth £90 million in CY2000. Pipe smoking is a niche market and is not expected to grow.

## Appendix

### Cigarettes PSD

PSD Table						
Country	United Kingdom					
Commodity	Tobacco, Mfg., Cigarettes				(MIL PCS)	
	Revised	1999	Preliminary	2000	Forecast	2001
	Old	New	Old	New	Old	New
Market Year Begin		01/1999		01/2000		01/2001
Filter Production	154750	154750	149750	149750	0	149750
Non-Filter Production	250	250	250	250	0	250
TOTAL Production	155000	155000	150000	150000	0	150000
Imports	43872	29082	47500	45018	0	54000
TOTAL SUPPLY	198872	184082	197500	195018	0	204000
Exports	115372	100349	115500	111006	0	120000
Domestic Consumption	83500	83733	82000	84012	0	84000
TOTAL DISTRIBUTION	198872	184082	197500	195018	0	204000