

From "denormalisation" to nationalisation of the tobacco industry?

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With a reduction in smoking as the goal, the fight against tobacco has led to increasingly heavy taxation and ever-tighter restrictions on the sale and consumption of cigarettes. If the public authorities continue along this path aimed at "denormalising" the tobacco industry, the question of prohibition¹ or nationalisation is likely to end up sooner or later as the heart of the debate.

Imposing generic packaging — something that has gone into force in Australia and is contained in proposed legislation, particularly in France — amounts to nothing less than "nationalisation" — in all but name — of cigarette packaging. The idea of nationalising the tobacco industry will come to appear less preposterous as anti-tobacco groups bring it up openly, and which is in any case an old tradition in France.

The existence of a nationalised tobacco industry is not the solution to smoking-related health problems. A measure of this type will not make tobacco consumption go away, and it is economically inefficient.

A REGULATORY ARSENAL THAT FACILITATES NATIONALISATION

The current fight against tobacco has hardened considerably since 2005 and the coming into force of the WHO's Framework Convention on Tobacco Control.² Moving beyond very high taxes, it marshals a regulatory arsenal that now seeks to make it unprofitable for tobacco to be supplied legally. The aim, says Yves Bur, a member of the French National Assembly, is the "denormalisation" of the tobacco industry.

An industry "denormalised" in this way would become easy prey for nationalisation.

One of the measures in this anti-tobacco arsenal, namely the imposition of generic cigarette packaging, plays a major role in this movement.³ Why?

The disappearance of the right to use a logo, colours, images, graphics and so on, indicating the existence of a brand of cigarettes, will clearly have an impact on tobacco company profitability. This risks putting the weaker firms into a tight spot and causing even greater concentration in this sector. Needless to say, it is easier to nationalise a highly concentrated industry.

A nationalised industry could more easily handle the production and marketing of cigarettes with generic packaging since private producers would be unable to compete by differentiating themselves or their products.



Several other measures penalising the tobacco industry have emerged. This is true of the obligation to "sell under the counter," advocated by the WHO, or the tax on tobacco company turnover, proposed in France,⁴ even though taxes already account for more than 80% of the retail price.

Furthermore, the idea of eliminating cigarette makers' profits has been a driving force for anti-tobacco activists and their suggestion of simply nationalising the tobacco industry and imposing a more or less broad public monopoly to handle the production and marketing of cigarettes.⁵

They state that the main problem with tobacco — the fact that people start smoking or that smokers are unable to quit — stems from the profits the companies make. The thinking is that nationalising the industry would "eliminate the profit motive from tobacco sales."⁶

1. This Economic Note is the second in a series of studies aimed at analysing the consequences of the current fight against tobacco. The first Note, titled "What if tobacco were simply prohibited?" (February 2012), is available at: <http://www.institutmolinari.org/what-if-tobacco-were-simply-1266.html>.

2. "WHO Framework Convention on Tobacco Control," WHO, 2003, available at http://www.who.int/tobacco/framework/WHO_FCTC_english.pdf. At the end of 2011, it had been signed by 174 countries, including France.

3. This measure has been in force in Australia since 2012. Similar legislation has been proposed in other countries, notably in France.

4. This applies, for example, to the report from Yves Bur to the French minister of labour, "Proposition pour une nouvelle politique de lutte contre le tabac," February 2012, available at: http://www.sante.gouv.fr/IMG/pdf/rapport_Y_Bur_nouvelle_politique_de_lutte_contre_le_tabac.pdf (see Recommendation No. 2).

5. See Cynthia Callard, Neil Collishaw and Dave Thompson, *Curing the Addiction to Profits*, Canadian Centre for Policy Alternatives (Physicians for a Smoke-Free Canada), Ottawa, 2005. See also Peter Fowler, "Nationalizing Big Tobacco," *Newsroom America*, 21 June 2010, available at: http://www.newsroomamerica.com/story/25488/opinion:_nationalizing_big_tobacco.html.

6. See the press release "Take tobacco out of the hands of business corporations — report," Canadian Centre for Policy Alternatives, 20 June 2005, available at: <http://www.policyalternatives.ca/newsroom/news-releases/take-tobacco-out-hands-business-corporations-report>.

THE MISUNDERSTOOD CAUSALITY BETWEEN PROFIT AND TOBACCO CONSUMPTION

Can it reasonably be supposed that cigarette makers' profits are the cause of tobacco consumption, as supporters of the industry's nationalisation have argued?

Contrary to this belief, the profit motive does not explain the consumption of tobacco — or of any other good on the market, for that matter. The causality, in fact, runs in the opposite direction: consumption, determined by the preferences of consumers and by their subjective evaluations of the products and services offered, is what explains whether efficient producers can find opportunities for profits.

Regardless of the sector, and the tobacco sector is no exception, it is consumers who are the ultimate deciders when it comes to consumption. The only enduring way to make tobacco disappear would be for consumers to decide on their own to change their lifestyle and to quit smoking. This is something they can do at any time, irrespective of whether the industry is in public or private hands.

And would a public tobacco industry allow a decline in tobacco consumption, much less a long-term disappearance? Theory, like experience, shows that a key argument of neo-nationalisation supporters has no real basis in fact.

A NON-SOLUTION FOR ENDING TOBACCO CONSUMPTION

Logically, two scenarios are possible, with the same end result in terms of consumption.

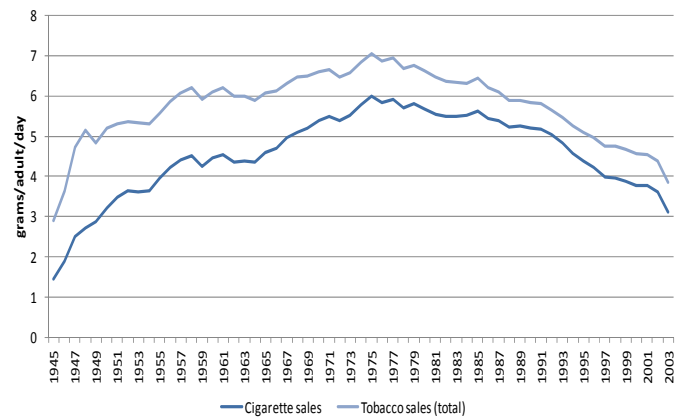
Strong political pressure could be exerted on the nationalised industry, under the sway of anti-tobacco lobbies in particular, with the stated aim of artificially reducing the legal cigarette supply. Alternatively, the nationalised industry could simply fail to meet demand or prove incapable of adapting to consumers' preferences. Regardless of whether a reduced legal supply for smokers results from policy or from a nationalised company's incompetence, this will create plenty of new opportunities that a already highly dynamic black market (because of current taxes and regulations) will not hesitate to seize.

It will then directly boost expansion of illicit supply and will end up having little impact on tobacco consumption, which would then rely on the illegal market. This would create adverse effects in terms of health (contraband cigarettes are generally more harmful) and of public finances (lower tax receipts).⁷

If, on the other hand, there was a weakening in political pressure

Figure 1

Changes in cigarette and tobacco sales per person (age 15 and higher) per day in France, 1945-2003



Source: Catherine Hill and Agnès Laplanche, 2003, *op. cit.*, p. 17-18.

for drastic cuts in smoking, the nationalised industry — a substantial generator of tax receipts — would imitate private companies to satisfy demand and meet consumers' preferences. Evidently, in this case also, the impact of nationalisation on smoking would be negligible or non-existent, with public supply of cigarettes replacing private supply.

Experience shows that, in general, this second scenario has largely prevailed.

THE FRENCH AND INTERNATIONAL EXPERIENCE

The idea of nationalising the tobacco industry is not new. The growing of tobacco and the manufacture and marketing of tobacco products have been under public monopoly in many countries in the past. The sharp rise in smoking in the 20th century, especially after the Second World War, occurred, paradoxically, when the tobacco industry in many countries was under public monopoly.

In France, the state monopoly on tobacco production and marketing tobacco was handled during this period through the *Service d'exploitation industrielle des tabacs et des allumettes* (SEITA), which dates back to 1926.⁸ Part of this tobacco monopoly was challenged under European Economic Community provisions, particularly in 1976.⁹ This French public producer was not, in fact, privatised until 1995.

Many factors, as noted above, account for tobacco consumption,

7. On this subject, see Valentin Petkantchin, "What if tobacco were simply prohibited?", Institut économique Molinari, Economic Note, February 2012, available at: <http://www.institutmolinari.org/what-if-tobacco-were-simply-prohibited.html>.

8. See, among other items, Nicole Lussion-Lerousseau, "La S.E.I.T.A. depuis la loi du 2 juillet 1980," *Politiques et management public*, Vol. 1, No. 4, 1983, pp. 55-88. This company was renamed the *Société d'exploitation industrielle des tabacs et des allumettes* in 1980. State monopolisation of the tobacco market in fact dates back to 1674 when "the sale and distribution of tobacco became a monopoly reserved for the monarchical state." On this subject, see the Ministry of the economy, industry and employment, "Les monopoles: SEITA," available at: http://www.finances.gouv.fr/directions_services/cedef/monopoles/2-1.html.

9. See Nicole Lussion-Lerousseau, 2003, *op. cit.*, p. 57.

but it is interesting to note that the rise in smoking coincided with the period when the industry was, in fact, public.¹⁰ The absolute sales record for cigarettes and tobacco per adult came in 1975, the year before the tobacco market was partly opened to competition (see Figure 1).

Nationalised tobacco companies still exist. China, for example, has by far the greatest number of smokers in the world. According to the WHO, they number about 350 million,¹¹ more than the combined populations of the 17 euro zone countries (about 330 million¹²).

The Chinese tobacco market is however under the control of a state monopoly, the China National Tobacco Corporation (CNTC),¹³ and it continues to expand (the volume of cigarette sales is expected to grow by 14% a year between 2010 and 2015), even though China is a signatory to the WHO Framework Convention on Tobacco Control. In 2010, the CNTC made a profit higher than the combined profits of the three largest private tobacco companies, Philip Morris International, British American Tobacco and Altria — (see Figure 2).¹⁴

While public authorities in Western countries pursue drastic policies that could give rise to new public entities in the tobacco sector, according to a Chinese report, in contrast, "breaking the tobacco monopoly is a top priority" in China.¹⁵

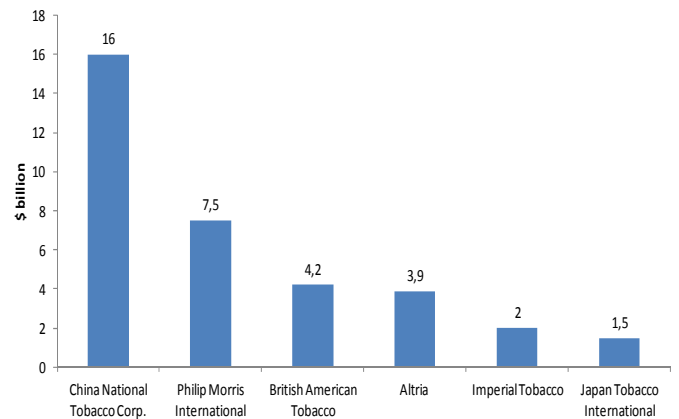
The alcohol market, where similar public health considerations were advanced, especially in North America, provides further evidence of what would happen in case of nationalisation, even when public health is the explicit goal.

The example of Quebec and other parts of Canada is especially



Figure 2

Profits of the CNTC and the five other largest tobacco companies, 2010



Source: Michael Eriksen et al., *The Tobacco Atlas*, 4th edition, 2012, p. 58.

enlightening in this regard.¹⁶ While efforts were made to end alcohol consumption through outright prohibition in the United States (which was a failure and the source of many adverse effects), in Canada the public authorities used nationalisation of the liquor trade in their efforts to control consumption.

For example, the *Société des alcools du Québec* was established in 1921 with the aim of promoting temperance and controlling alcohol consumption. The existence of a monopoly and nationalisation of the retail side obviously did not put an end to alcohol consumption. Paradoxically, consumption increased more in Quebec than in another Canadian province, Alberta, where the retail trade in liquor was privatised in 1993. According to Statistics Canada, alcohol sales per adult rose by 21.7% in Quebec between 1993 and 2011 but only by 8.3% in Alberta.¹⁷

Evidently, nationalising an industry does not mean that consumption of the good in question will decline or will be lower than elsewhere.

AN INEFFECTIVE AND RISKY MEASURE

Nationalised industries cause the waste of scarce resources, because private businesses no longer fulfill their economic coordination functions correctly.

It should not be forgotten that the tobacco industry covers a di-

10. See Catherine Hill and Agnès Laplanche, "Le tabac en France : les vrais chiffres," *La Documentation française*, Paris, 2003.

11. See WHO, "10 Facts on Tobacco and Gender in China," available at: http://www2.wpro.who.int/china/sites/tfi/wntd2010_facts.htm.

12. Source: Eurostat.

13. See the presentation on the Chinese government site, "State Tobacco Monopoly Administration," available at: http://english.gov.cn/2005-10/03/content_74295.htm.

14. See "China's Tobacco Monopoly Bigger by Profit Than HSBC," Bloomberg, March 6, 2012, available at: <http://www.bloomberg.com/news/2012-03-06/china-s-tobacco-monopoly-bigger-by-profit-than-hsbc.html>.

15. See the study by the China Research Center for Public Policy, "Tobacco Control under the Influence of Tobacco Monopoly in China," November 2011, available at: <http://www.changce.org/index.php/en/enproject/s83-tobacco-control-under-the-influence-of-tobacco-monopoly-in-china.html>.

16. On this subject, see Valentin Petkantchin, "Is government control of the liquor trade still justified?," Research Paper, October 2005, available at: <http://www.iedm.org/209-is-government-control-of-the-liquor-trade-still-justified->

17. Source : Statistics Canada, "Volume of sales of alcoholic beverages in litres of absolute alcohol and per capita 15 years and over," calculation by the author.

verse and varied set of activities: growing tobacco, storing and treating it, manufacturing cigarettes and other products, transporting and marketing them. Many economic choices have to be made regarding staff, salaries, status (whether or not they are civil servants), tobacco prices, storage costs, equipment, product ranges, etc.

These are areas where competition and the recording of private losses or profits are essential, playing a major role in terms of information and incentives. Without them, the public monopoly cannot be managed efficiently, even if it were to run at a 'profit'. Any such profit would be at the expense of consumers, who would have no choice and would have to content themselves with a reduced selection of products and prices.

When a nationalised industry faces competition, with private players allowed to function alongside it, these management decisions also represent an operating risk suffered by taxpayers in the end.

The case of SEITA clearly illustrates this risk. It operated in the red during much of the 1970s and 1980s. The opening to competition in 1976, in particular, "caused a rapid degradation" of its situation, a 20% loss in market share for cigarettes (its main production)¹⁸ and deficits that were "particularly high between 1976 and 1987," reaching the equivalent of more than 220 million euros in 1980.¹⁹

This sort of operating risk would clearly be out of place today, with the public authorities indicating an intention to halt the slide in public finances.

CONCLUSION

Nationalisation of the tobacco industry is not a solution to the health problems caused by smoking.

This would be true if the public authorities were to impose an artificial reduction in the legal tobacco supply, leaving the door wide open to the black market and its array of adverse effects on smokers' health and public finances.

Can it reasonably be supposed that cigarette makers' profits are the cause of tobacco consumption, as supporters of the industry's nationalisation have argued?

Alternatively, in the absence of political constraints on the nationalised industry, it would follow a commercial approach similar to that of private tobacco producers. The goal of reducing tobacco consumption would be compromised in this case as well.

Nationalised industries are an inefficient solution from an economic standpoint, because they penalise consumers by offering them a narrower product range, and they push their operating risks onto taxpayers.

These harmful effects should not be ignored if, with the growing impact of anti-tobacco lobbies, tobacco industry nationalisation were to be discussed more openly. The idea of imposing generic packaging should alert public authorities to a possible slide toward nationalisation of the entire industry.

18. See Nicole Lusson-Lerousseau, 2003, *op. cit.*, p. 58.

19. See Eric Godeau, *Le tabac en France de 1940 à nos jours: Histoire d'un marché*, Presse Paris Sorbonne, 2008, p. 311. The loss of 550 million francs showing for 1980 was converted to the 2011 euro equivalent.



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