



RAISING TOBACCO TAXES BENEFITS MOST THOSE WHO HAVE THE LEAST

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- Raising the tobacco tax by \$1 additional peso per stick would raise the price of cigarettes from \$65 to \$110 pesos per pack.
- Increasing the tobacco tax by \$1 per stick would reduce consumption by 40 percent among the poor, while for the rich tobacco use would drop 33.6 percent.
- Adjusting only for inflation leads to slight changes in prices, consumption, and revenue. However, an increase in tobacco tax of \$1 peso per stick would have significant beneficial effects on health and provide greater funding for the public treasury.
- In Mexico, the poor smoke less than the rich. That means that the rich pay more tobacco taxes.
- Increasing tobacco taxes will improve equity in Mexico. Higher taxes on tobacco mean the poor pay less, relative to what the rich pay.

Introduction

Smoking has negative impacts on the economy, health, and public finances, and significant amounts are spent on treating diseases caused by smoking.

There is a global myth that increasing tobacco taxes has a negative impact on the poorest in society, or that they are regressive. This has been a significant factor in discouraging decision-makers from increasing taxes on tobacco. However, international evidence has shown that tobacco taxes can actually be progressive or benefit the poorest the most.

In Mexico, a 40 percent increase in the price of tobacco would considerably reduce consumption among those who have the least, while consumption patterns among the middle and higher classes would still see significant, but less dramatic change. Moreover, significant tobacco tax increases would significantly augment the amount of revenue available for the state to address other needs, like treating expensive smoking-related noncommunicable diseases (Chaloupka & Blecher, 2018).

Debunking the myth of regressivity

The myth of tobacco tax regressivity is based on a misconception about its impact on poorer smokers, as it is assumed that poor smokers will continue to use the same amount of tobacco, regardless of price, due to their addiction. Global evidence demonstrates this myth is wrong and low-income smokers are especially sensitive to price compared to wealthier peers.

In addition, in Mexico, those with lower incomes smoke less, with just four percent of households spending money on tobacco products, while this figure reaches 17 percent for high-income households (Huesca et al., 2021). The idea that increasing tobacco taxes negatively impacts the poor is not supported by the evidence.

Any tax reform that causes a substantial increase in the price of a pack of cigarettes would result in a greater cost for richer population groups. Furthermore, the most vulnerable groups would reduce their consumption by 40 percent, while smoking would also decline among high-income smokers, but to a lesser extent: by 33.6 percent.

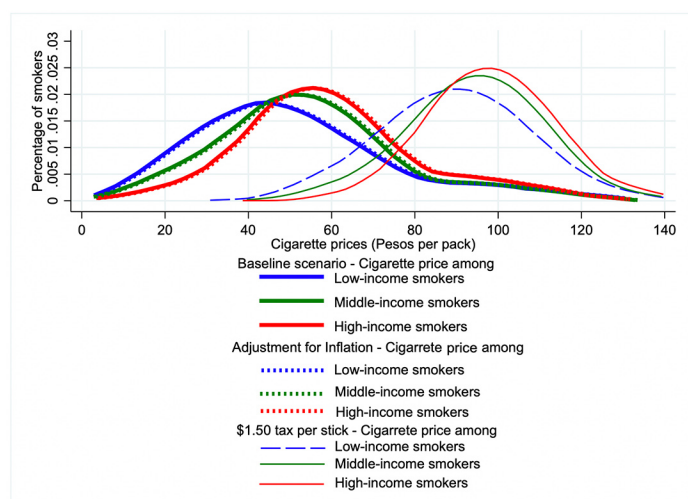
A society concerned about equity should be aware that increasing tobacco taxes in Mexico means shifting a higher proportion of these taxes onto the rich. Higher tobacco taxes allow the poor to pay less relative to the rich, improving equity in Mexico.

More progressive taxes

When the tobacco tax is adjusted for inflation (represented by the barely visible dotted lines in figure 1), cigarette price variation appears unnoticeable for all population groups (low, middle, and high-income). So simply adjusting for inflation does not affect the price paid. But research suggests this progressivity will become clearly noticeable when the tax is higher.

When cigarette taxes increase by 1 peso (so the specific tax per stick goes to 1.50 pesos), cigarette prices increase substantially for each income group (represented by the dashed lines in figure 1). All smokers would pay a higher price than in the baseline scenario, but even more importantly, the tax reform would reduce the price gap between income groups.

Figure 1. Prices paid for cigarettes and progressivity*



* Baseline and inflation scenarios are practically superimposed due to the minimal price variation in both cases.

Source: ENIGH 2018. Note: Income levels defined by terciles of the total population.

In other words, to reduce tobacco use substantially, the tax should increase in 1 peso per cigarette (so the specific excise tax will be 1.50 pesos per cigarette). This would benefit the poor the most, as consumption would decrease to a greater extent in low-income groups.

These changes benefit the poor, as they bring about a change in their pattern of consumption, while lowering their tax burden in relation to higher-income groups.

Conclusions

A significant increase in tobacco taxes would dramatically reduce tobacco consumption, having the greatest positive impact on low-income groups in Mexico. Only adjusting the excise tax on production and services (IEPS) for inflation is also a progressive policy, but it results in almost no increase in price and has little impact on consumption patterns.

Large tax increases would change tobacco consumption patterns, resulting in low-income groups decreasing their consumption and therefore, their tax burden. Meanwhile, high-income groups would also reduce tobacco use but will bear more of the tax burden. Furthermore, this increase in revenue means more money would be available to the public treasury.

This research recommends a tax increase that would bring the price of a pack of cigarettes up to around 110 pesos, in line with international standards promoted by the World Health Organization, whereby total tax should constitute at least 75 percent of the final retail price of a pack of cigarettes. This would generate a total of 63 billion pesos in revenue and translate into a better distribution of public finances and a decline in tobacco consumption. More specifically, the additional revenue could be used to build as many as 20 fully-equipped hospitals every year across the country, or to provide a little over one-year's supply of COVID-19 vaccines, both of which would directly result in a great social benefit in health care.

References

Chaloupka, F. J. and Blecher, E. (2018). "Tobacco & Poverty: tobacco use makes the poor poorer, tobacco tax increases can change that. *Tobacconomics Policy Brief*. Chicago, IL: Tobacconomics, Health Policy Center, Institute for Health Research and Policy, University of Illinois at Chicago.

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