

## Higher Taxes Needed to Make Cigarettes Less Affordable and Increase Revenue

### Tobacco use has severe health and economic implications in Pakistan

- 31.6 million adults (age 15 +) or about 19.9% of adults currently use tobacco, including 17.3 million smokers.<sup>1</sup>
- Tobacco use is associated with more than 160,000 deaths every year in Pakistan.<sup>2</sup>
- The total estimated costs attributable to all smoking-related diseases and deaths are 1.6% of GDP annually.<sup>3</sup>
- More than 490,000 people will start smoking in Pakistan if tobacco taxes are not raised in 2025-26.<sup>4</sup>

### The 2023 tax increase led to reduced consumption and increased revenues

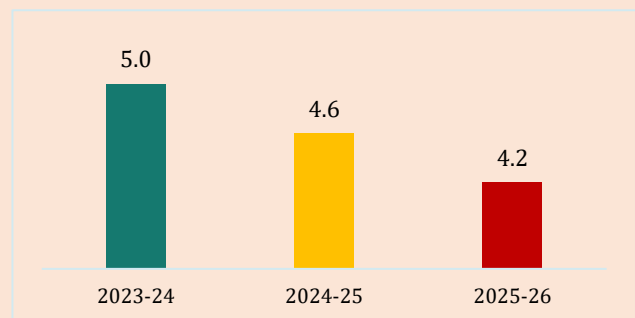
- After the excise tax increase in February 2023, 26.3% of smokers cut down on cigarette consumption due to price increases. Overall, cigarette consumption declined by 19.2%.<sup>5</sup>
- Revenue collection from the Federal Excise Duty (FED) on cigarettes increased by 66%—Rs 142 billion in 2022-23 to Rs 237 billion in 2023-24.

### A freeze on tax rates has made cigarettes more affordable

- FED rates on cigarettes have not increased since February 2023.
- From 2022-23 to 2024-25, per capita income increased by 12.5% and the average Consumer Price Index increased by 9.5%, but the average prices of cigarettes did not keep pace, increasing by only 2.7%.
- Consequently, cigarettes have become more affordable as 5% of per capita income was required to purchase 2000 cigarettes in 2023-24, which is expected to decline to 4.2% in 2025-26 (Figure 1).

- Cigarettes have become more affordable due to the tax rate freeze since February 2023.
- An excise tax increase of **Rs 39 per pack** will result in **263,000 fewer smokers**, a **6.9% reduction** in cigarette consumption, and an additional revenue of **Rs 67.4 billion**.

Figure 1: Percentage of per capita income required to purchase 2000 sticks of cigarettes\*



\* Affordability/Relative income price ratio.

Sources: Projections from IMF World Economic Outlook October 2024; Pakistan Bureau of Statistics, Government of Pakistan.

### It is necessary to reduce the tax rate gap, because it encourages consumers to switch to low-price brands instead of quitting

- Currently, the per-pack FED on premium cigarettes (Rs 330) significantly exceeds that on economy brands (Rs 101), resulting in a substantial difference of Rs 229, compared to the Rs 71 gap observed in 2021-22. In relative terms,

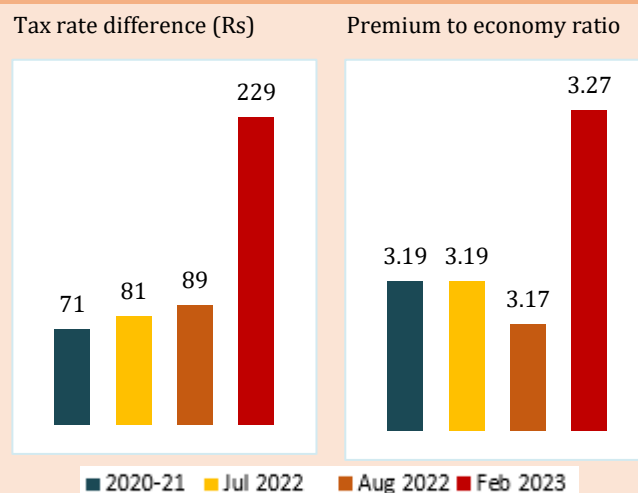
the tax rate on premium brands is 3.27 times that of economy brands (Figure 2).

- The tax rate gap results in large price variations, which allows smokers to opt for cheaper brands rather than quit.

### FED share in retail prices is low

- Despite a substantial increase in FED in 2023, the share of excise tax in retail price remains below the widely accepted benchmark of 70%, particularly for economy brands. Currently, the estimated share of FED in retail price is 54% for economy brands and 68% for premium brands.

**Figure 2: FED rates differentials**



Source: Finance Acts, Government of Pakistan.

## THE PROPOSAL

The tax proposal is based on two considerations: keeping the affordability at the level of 2023-24 and reducing the tax rate gap.

**It is proposed to increase the FED rate on economy brands from Rs 101 to Rs 140 per 20-cigarette pack. The same increase is proposed for premium brands.**

### Proposed tax rates for 2025-26

FED: Rs per 20-cigarette pack				
Price tier	Current	Proposed	Increase	% increase
Economy	101	140	39	38.6
Premium	330	369	39	11.8
Average				27.1

### Endnotes:

1. SPDC estimates based on GATS 2014 and population projection for 2024-25.
2. Institute of Health Metrics and Evaluation. Global Burden of Disease, GBD Compare. University of Washington, 2019.
3. Nayab, Durre, Nasir. M., Alam. J. & Siddique. M. (2021). The economic cost of tobacco-induced diseases in Pakistan. Pakistan Institute of Development Economics.
4. Estimated number of smokers will increase from 17.28 million in 2024-25 to 17.77 million in 2025-26.
5. Iqbal, M.A., Haroon Jamal, Muhammad Sabir & Naveed Aamir (2024). Consumption behaviour of cigarette smokers in Pakistan: The 2023 survey. Survey Report. Social Policy and Development and Development Centre (SPDC).

### Impact of the proposed tax increase

<b>263,000</b>	fewer smokers
<b>6.9%</b>	reduction in total cigarette consumption
<b>6.3%</b>	reduction in smoking intensity among adults
<b>264,000</b>	lives saved (reduction in premature smoking-attributable deaths)
<b>Rs 67.4 billion</b>	in additional revenue, including Rs 58.2 billion in FED and Rs 9.2 in GST—a total increase of 17.9%

### Beyond 2025-26, the Government must:

- Continue implementing substantial excise tax hikes to increase cigarette prices and reduce affordability steadily,
- Integrate an automatic inflation-adjustment mechanism into the tax policy to ensure taxes keep pace with rising prices, and
- Move gradually to a uniform federal excise duty for all cigarette brands to simplify the tax system and avoid brand category switching.
- Ensure that the implementation and enforcement of the Track & Trace System is extended to all cigarette manufacturing units/firms.