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The Changing Political Environment for Tobacco—Implications for Southern Tobacco Farmers, Rural Economies, Taxpayers, and Consumers: Discussion

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ABSTRACT

This paper is a discussion of the Brown, Snell, and Tiller article. The economic accuracy, conciseness, and organization is noteworthy with the major strength being the analysis of the tobacco system with the absence of a Federal program. The base paper discusses economic consequences of the U.S. tobacco program, within-industry structural differences, and recent/potential future changes such as the buy-out, industry uncertainty, and the possibility of program elimination.

Key Words: price-support program, tobacco industry, tobacco program.

The Brown, Snell, and Tiller paper is highly comprehensive and a major accomplishment for the tobacco industry. From an economic standpoint, this paper is accurate, concise, and well organized.

The introduction was most appropriate for this industry as the discussion moved rapidly from the early history to the 1997 Tobacco Agreement. As this author and Dewitt Gooden, Extension Agronomist, Clemson University, have reported in several extension publications/meetings just after the agreement: "The tobacco industry underwent non-reversible changes when they signed the landmark Tobacco Agreement . . . this is the case, regardless of whether there is a Tobacco Settlement or not" (Sutton). Although the statement is true, no one was aware of the magnitude of the change.

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The discussion of the U.S. tobacco program and especially quota/rent issues is factual and comprehensive. The quota market, except for Tennessee, is a separate market for each county. Most of the tobacco states have within-state county markets that are quota surplus or quota deficit (Loyd and Bradford). Although no one paper can be all encompassing, a simple extension of the economic rent figure (Brown, Snell, and Tiller; Figure 3) would be beneficial.

The administration of the Federal tobacco program is unusual for a current price support/quantity control system. The program is very inflexible and is essentially micro-managed by Congress. This is significantly different from most other Federal programs such as other commodity programs and marketing orders. Apparently, it has remained this way either because it was traditional or because the producers/decision makers felt they had more influence through such a process. The latter is puzzling since the two major program changes during the 1980s came under severe pressure from opponents. Even during recent discussions and one bill under the tobacco agreement which would have changed this structure, several producers and leaders still preferred the current system of administration. This means there are major difficulties changing the program to make it more market oriented.

The reviewed paper raises some important points about the structural differences between flue-cured and burley tobacco. A producer group is currently calling for a reduction in support price for flue-cured tobacco, which is consistent with the base paper analysis of the marginal cost of producing burley being higher than that of flue-cured. If this change in support price were to take place, what would be the substitution effect between these types of tobacco? For example, the make-up of domestic leaf used for cigarettes in the early 1960s was about 61 percent flue-cured, 38 percent burley, and one percent Maryland (USDA). As mentioned in the base paper, the early 1980s price support formula for flue-cured came under much pressure because it was increasing rapidly as stabilization stocks or unsold quantities were building to massive levels while burley had low-to-no surplus stocks (Capehart). During this period, the make-up of leaf changed to 50–51 percent for flue-cured, 46–47 percent for burley, and 2–3 percent for Maryland (USDA). Once the formula changed and price relationships returned to previous levels, the composition began to move back toward the earlier values. In addition, there was/is also a significant amount of imported tobacco substitution. Although only the manufacturers know the substitutability, there is evidence of at least a moderate level of substitution effect when price relationships change.

Two minor corrections/explanations seem to be in order. The first issue is regarding immediate future Federal excise taxes for cigarettes. Based on 1997 legislation (U.S. Code Annotated), the Federal exercise tax on cigarettes is scheduled to increase from 24 cents per pack to 34 cents per pack on January 1, 2000 (taxes on other tobacco products will also increase). In addition, this same legislation increased the cigarette excise tax by another five cents to 39 cents per pack on January 1, 2002. Second, the late 1998 cigarette price increase was 45 cents per pack but it should be pointed out that this was at the wholesale level. Retail prices were reported to have increased by another five to 10 cents per pack. This is slight and does not hinder the Brown, Snell, and Tiller analysis but, in fact, strengthens their arguments.

The immediate concern with the current tobacco program is the administration of the farmer trust fund and the economic impacts because of inability to make adjustments in the Federal tobacco program. The program is administrated at the Federal level but the funds will be managed at the state level. This means that in the absence of linked Federal legislation (which seems likely), payments will be made to quota holders and producers for lost quota without any changes in the program. Some grower groups are highly concerned with this as they have long advocated that any payout should include a movement of quota into the hands of the growers. There has been discussion within South Carolina and other states of some scheme to have a tiered payout with the quota owners receiving even more if they sell their quota in accordance with program guidelines. It is unfortunate that a program which is supposed to be designed to administer a production system has such limitations in capability to respond to supply/demand conditions.

Health advocacy group involvement with the interest, understanding, and support/nonsupport of the tobacco program has been a significant change from the past. With mostly health group support for the program in exchange for specific anti-smoking initiatives, as explained in the base paper, most of the producers in South Carolina have been positive in acceptance. Although no data are available, it is thought that at least a significant number or possibly a majority of producers would be neutral to positive concerning this alliance. What would be interesting would be a legislative proposal such as a reduction in flue-cured price support levels. Would this alliance hold, change, or dissolve?

If the tobacco program were eliminated, there would be a massive transfer in annual income from quota owners to consumer surplus. The more than 500 million dollar transfer value in the Brown, Snell, and Tiller paper is consistent with past research (Fulginiti and Perrin). For flue-cured, rental arrangements are mostly whole-farm and involve other crops/enterprises. Nearly all of these arrangements are because of tobacco and the leasing arrangement requirements of the program. The actual reduction in annual income to flue-cured quota owners would likely be much larger.

In light of the recent political activity and the uncertain future of tobacco, the Brown, Snell, and Tiller paper should be closely studied regarding the economic fundamentals of tobacco production with or without a program.

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