



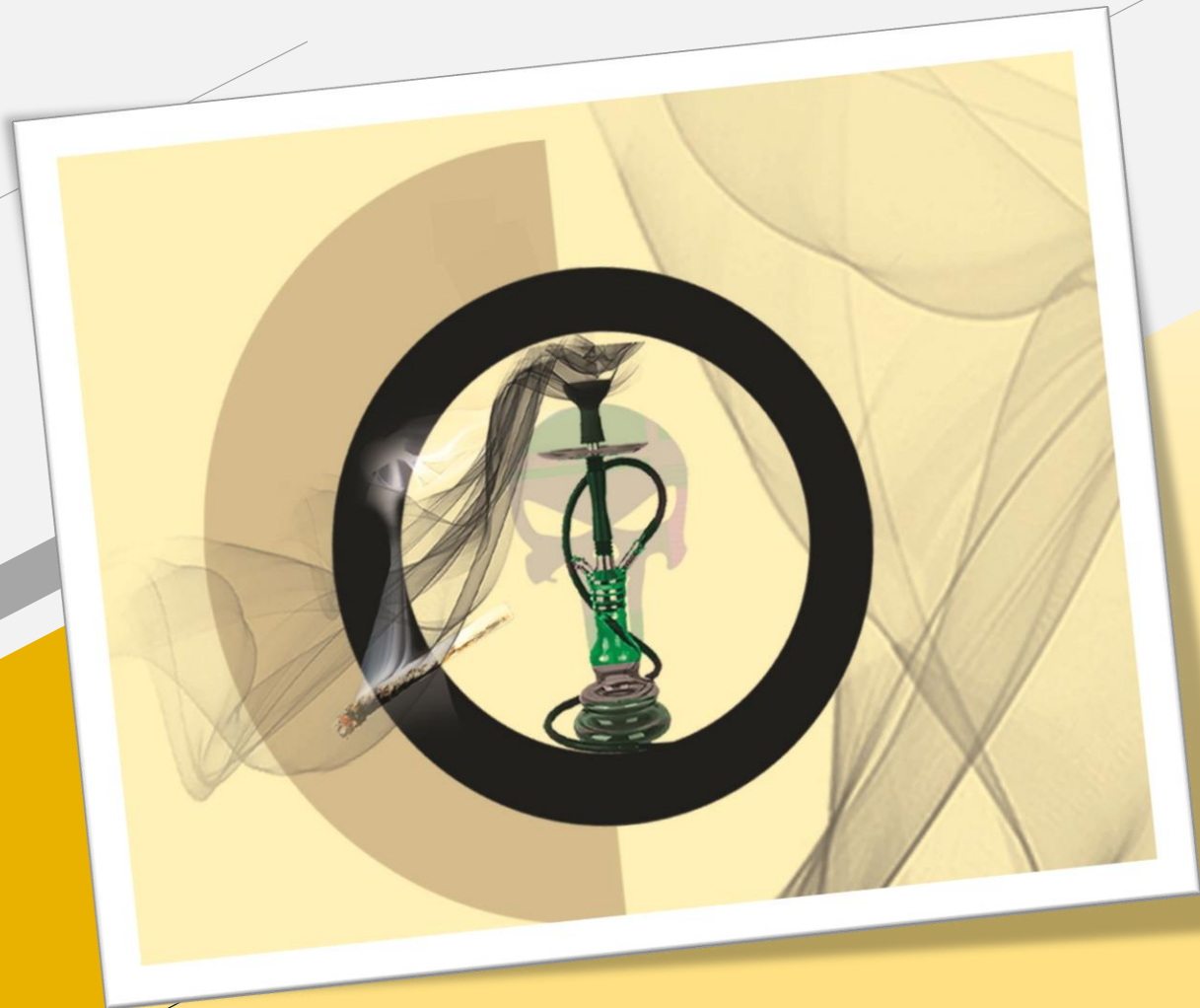
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Economic Analysis of Market Structure in Cigarette Industry

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INTRODUCTION

POWER TOOL

MARKET DEFINITION

MARKET CONCENTRATION

Herfindahl-Hirschman Index

Types of Entry Barriers Relevant to the Cigarette Industry

DISCUSSION



INTRUDACTION

In recent decades, the competitive landscape in many markets and the methods that researchers use to analyze these markets have changed heavily. Taxes, which have been historically used as revenue-raising measures, can also be designed to help achieve health-related objectives.



MPOWER TOOL

Although significant progress in combatting the tobacco epidemic has been achieved, consumption of tobacco remains a major preventable cause of mortality and disability. Recent statistics show that tobacco is responsible for approximately 8 million deaths and a cost of US\$ 1.4 trillion to the global economy annually. The **Framework Convention on Tobacco Control (FCTC)**, introduced by the World Health Organization (WHO) in 2005, ***set policies to reduce both demand and supply of tobacco products***. To provide further practical guidance to countries tobacco control, ***transnational tobacco companies, market share, market trends in implementing the FCTC***, the WHO introduced the **MPOWER tool**.

MPOWER Tool

the WHO introduced the **MPOWER Tool**.

Monitor tobacco use (M)

Protect people from tobacco smoke (P)

Offer methods to quit tobacco use (O)

warn about the dangers of tobacco (W)

Enforce bans on promotion and advertisements (E)

Raise taxes to reduce consumption(R)





MARKET DEFINITION

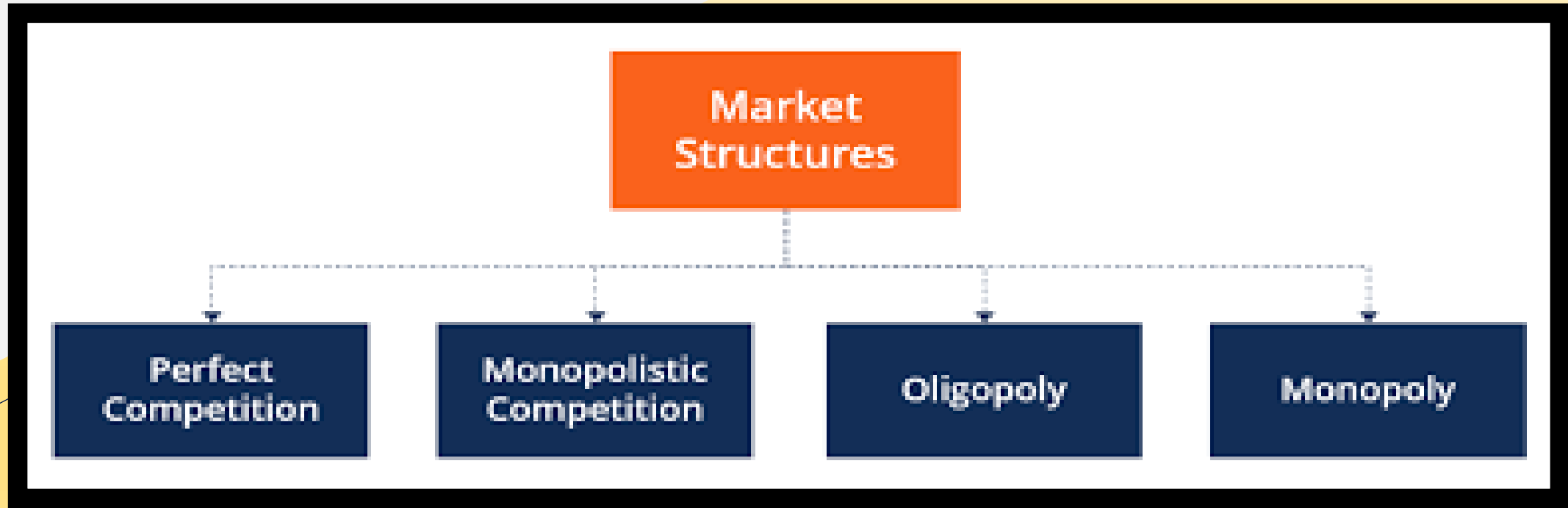
Market Economy

A market economy is a system where private individuals and businesses drive the economy on the basis of demand and supply without state intervention.





MARKET STRUCTURE





MARKET CONCENTRATION

Although the **public health** emphasis is often on the ability of large firms to influence public policy rather than on other impacts of market concentration, high levels of concentration are important to market power and its related impacts on **pricing, market entry, and competition**. In addition, market concentration has provided the major cigarette firms with higher profits that they have used to support intensive lobbying, lawsuits, and other activities to block, delay, or weaken tobacco control efforts. In addition, the incentives to lobby against tobacco control policies increase when firms have large market shares, since a larger share of the gains then accrue to those firms.



MARKET CONCENTRATION

standard indicator of market power

Herfindahl-Hirschman Index (HHI)

$HHI < 1500$ as unconcentrated (unlikely to have adverse competitive effects)

$1500 \leq HHI < 2500$ as moderately concentrated (“raises significant competitive concerns”)

$HHI > 2500$ as highly concentrated market power.

Types of Entry Barriers Relevant to the Cigarette Industry



The economics and marketing literature has identified four :

Advertising

Brand Proliferation

Retail Slotting Contracts

Legal/Regulatory Costs



Advertising

Advertising can create entry barriers when market entrants cannot readily take advantage of the *economies of scale* that large established firms enjoy in their ongoing advertising or when past advertising has created brand loyalty for existing firms. While existing firms may produce at a level where advertising economies of scale have been exhausted, entrants may find it difficult to reach that level. The economics literature is mixed on the role of scale economies in *cigarette advertising*. Brown found advertising economies over a wide range of cigarette sales, especially for new brands. However, an efficient scale may be more difficult to reach in recent years with more rapidly declining demand.



Brand Proliferation

the dominant cigarette companies have taken advantage of consumer familiarity with their most popular brands by marketing sub-brands. Indeed, brand proliferation by established firms can create an entry barrier when brands are densely packed across product dimensions (eg, menthol, light/low, full flavor, women-focused, premium, low-cost). With no market niche available, it is more difficult for new brands to distinguish themselves from established brands and sub-brands. This phenomenon has been identified in empirical inter-industry studies and validated by complementary theoretical models. Cigarettes have been associated with specific product attributes, such as nicotine and tar content, length, flavor and thickness. Labeling and advertising can also create different perceived brand characteristics separate from product attributes, eg, establishing **Marlboro** as a masculine brand and promoting Virginia Slims as a women's cigarette. Cigarettes have been found more generally to be differentiated along horizontal (brand attributes, such as light vs regular, length) and vertical (perceived quality, such as premium vs. regular) dimensions.



Brand Proliferation

In concentrated markets with high entry barriers, established firms may engage in anticompetitive pricing to increase their profits or to prevent market entry. To maximize profits, firms may engage in coordinated pricing through either explicit or tacit collusion.⁵ In addition, a dominant firm or coordinated group of firms can also temporarily reduce prices to discourage other firms, already in the industry or as entrants, from undercutting collusive prices. With few firms, easily detectable price deviations, relatively homogeneous products, price insensitivity by consumers, and significant brand loyalty, the U.S. cigarette market is particularly vulnerable to coordinated pricing. The Supreme Court noted a lack of “significant price competition among rival firms. List prices for cigarettes increased in lock-step twice a year, for a number of years.



DISCUSSION

Theoretical analyses and empirical evidence from the economics and marketing literature reveal substantial market power by the major firms in the cigarette market. **Market concentration has increased due to mergers, major-firm brand proliferation, and the growth of particular brands.** In addition, entry barriers, especially retail slotting allowances and brand proliferation, have been substantial, and have protected market power. With high market concentration and entry barriers, the large, established firms have been able to engage in anticompetitive practices, such as collusive pricing, predatory price-cutting and **price discrimination.** We have focused on the economics and marketing literature, but the analysis may be supplemented with related legal literature and information gleaned from industry documents.



DISCUSSION

Standard economic and antitrust analysis disfavors market power and market concentration in favor of more active competition that will make products more readily available and affordable to consumers. ***However, market power in the cigarette market has benefited the public health to the extent that it has increased prices***, thereby reducing smoking levels and related health outcomes. At the same time, increased market power has enabled the more established firms to target smaller firms by selectively reducing prices and proliferating brands, and to price discriminate by selectively reduce price to more price sensitive consumers. While these industry practices have been recognized in the public health literature, the emphasis appears to mainly relate to their impact on increasing profits, which is then channeled to lobby against potent tobacco control policies.



DISCUSSION

More generally, the economics literature could help to guide new tobacco control efforts to discourage market concentration and market power where it hurts the public health (eg, by increasing its ability to protect profits) and to encourage competition when it will produce new public health gains (eg, by shifting the market and smokers from cigarettes to less-harmful tobacco-nicotine products). These opportunities have expanded with the increasing use of non-cigarette nicotine delivery products. In particular, unlike earlier studies of cigarette demand, recent studies indicate that consumers are highly responsive to both cigarette and e-cigarette prices, suggesting that the relevant market may have expanded beyond just cigarettes.



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DISCUSSION

Since the 1960s, cigarette market concentration has increased primarily due to **mergers and growth in the Marlboro brand**. The **market has high entry barriers**, due to advertising, brand proliferation and slotting allowance contracts, which were encouraged by government regulations. The **anticompetitive structure** has led to higher prices beyond those from government tax increases, consistent with tobacco control aims, but which has further enriched the major cigarette companies, increasing their ability to influence policies. With the increase in multiproduct use and the introduction of alternative nicotine delivery products, it will be especially important to consider the market structure of related markets and the role of the cigarette industry in shaping those markets through its ability to exercise market power.



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سارا ميلاو

سپیگار وسپیاست

ترجمہ کیانوش امیری



مؤسسة انتشارات نگاه



Thank you for your attention

