Tobacco and the Economy: Farms, Jobs, and Communities, By H. Frederick Gale, Jr., Linda Foreman, and Thomas Capehart, Economic Research Service, U.S. Department of Agriculture, Agricultural Economic Report No. 789.

Abstract

Public health policies intended to reduce the incidence of smoking-related disease adversely affect thousands of tobacco farmers, manufacturers, and other businesses that produce, distribute, and sell tobacco products. This report assesses the likely impacts of declining tobacco demand, and identifies the types of workers, farms, businesses, and communities that are most vulnerable to loss of tobacco income and jobs. The dollar impact on the farm sector of a reduction in cigarette demand will be smaller than that experienced by manufacturing, wholesale, retail, and transportation businesses, but tobacco farms and their communities may have the most difficulty adjusting. Many tobacco farmers lack good alternatives to tobacco, and they have tobacco-specific equipment, buildings, and experience. Most communities will make the transition to a smaller tobacco industry with little difficulty, because tobacco accounts for a small share of the local economy. However, a number of counties depend on tobacco for a significant share of local income.

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Summary

Public health policies intended to reduce the incidence of smoking-related illness adversely affect thousands of businesses, workers, and communities that produce, distribute, and sell tobacco products. In recent years, increases in Federal and State excise taxes, restrictions on smoking in public places, price increases resulting from legal settlements, and falling cigarette exports have impacted the tobacco industry. Most of the jobs and income affected by a reduction in cigarette demand are beyond the farm gate in manufacturing, wholesale, and retail businesses, but some tobacco farms and their communities may have difficulty adjusting to declining demand for tobacco. This is because many tobacco farmers lack good alternatives to tobacco, and they have specialized tobacco-specific equipment, buildings, and human capital. Strong economic growth in many of the communities where tobacco is grown and processed has softened the local economic impact of lost tobacco dollars, but in a number of communities, reliance on tobacco income is still relatively high.

The tobacco industry has wide-ranging effects throughout the economy, affecting not only farms and manufacturers, but also wholesale businesses and retail stores. Businesses in other industries that supply intermediate goods, inputs, and services also rely on tobacco. These include companies in diverse sectors such as warehousing, paper, metal products, machinery manufacturing, advertising, transportation, and legal services.

While tobacco leaf is the key ingredient in cigarettes and other tobacco products, its value accounted for only 4 cents of each consumer dollar spent on tobacco products in 1998. About 2.3 cents went to U.S. growers of tobacco, and 1.7 cents represented the value of imported tobacco. Most of the cigarette dollar goes to businesses beyond the farm gate and to government revenues. Manufacturing value-added accounted for 43 percent of the tobacco dollar, a share that increased rapidly during the 1980's and 1990's. Federal and State excise and sales tax revenues accounted for another 26 cents, and wholesale, retail, and transportation accounted for 21 cents of each tobacco dollar.

Tobacco farms vary considerably in size, location, yields, financial condition, and management characteristics. Most tobacco farms are in relatively good financial condition, but they will have difficulty replacing lost income from tobacco. Because the Federal tobacco program limits production and supports prices, tobacco leaf brings much higher returns than most other crop or livestock enterprises. Average returns over cash expenses exceed $2,000 per acre. Tobacco farms devote 6 percent of their land to tobacco, on average, but they obtain an average of 79 percent of their gross income from tobacco. Farms with low production costs due to good soils, management, size economies, and other factors will be in the best position to survive if tobacco prices decline. Smaller farms, concentrated in the Piedmont region of North Carolina/Virginia and Kentucky/Tennessee, tend to have lower tobacco yields, higher costs, and fewer profitable alternatives to tobacco. Farm operator characteristics, including the operator's age, off-farm work experience, and education, will have important influences on the strategies chosen by tobacco farmers to cope with a declining tobacco market.

Loss of tobacco-related jobs and income will affect hundreds of communities, both rural and urban, that rely on tobacco for part of their economic base. Most communities where tobacco is grown and manufactured will make the transition to a smaller tobacco industry with little difficulty. However, a number of counties, mostly in Kentucky, North Carolina, and Virginia, depend on tobacco for a significant share of local income. These counties have generated relatively few economic alternatives to tobacco.

The analysis is based on a number of different data sources, including the Census of Agriculture, the Annual Survey of Manufactures, and the Agricultural Resource Management Study (formerly called the Farm Costs and Returns Survey).