

U.S. Flue-Cured Tobacco Situation & Outlook

August 3, 2015

Dr. Blake Brown
Hugh C. Kiger Professor
Agriculture & Resource Economics
College of Agriculture & Life Sciences

Flue-Cured Hectares Harvested:

	2011	2012	2013	2014	2015*
US	83,730	83,365	92,592	93,887	83,689
NC	64,750	66,369	68,797	73,248	64,750

*June 2015 Forecast. USDA-NASS

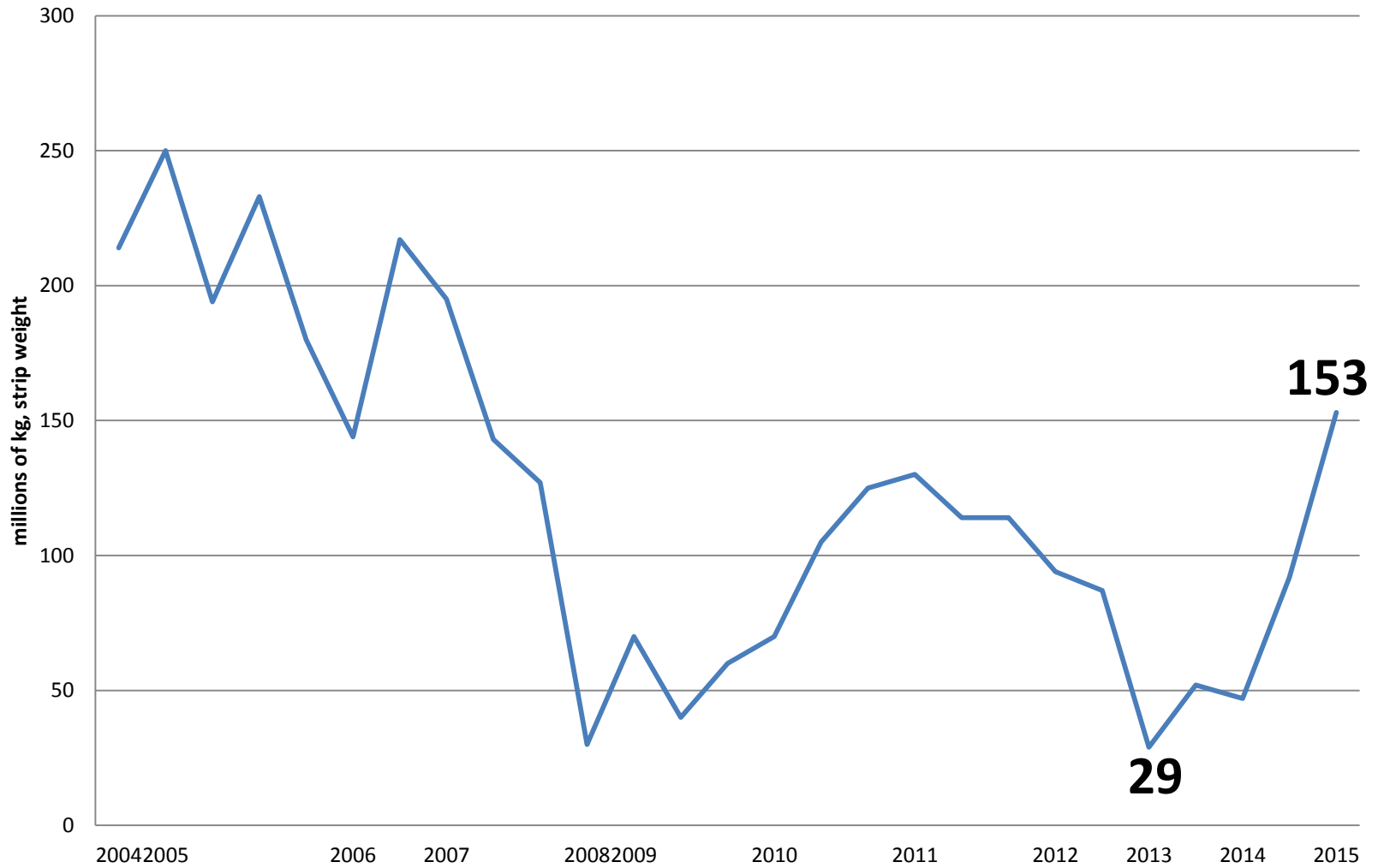
Flue-Cured Production: (million kg)

	2011	2012	2013	2014	2015*
US	156	215	206	253	206
NC	112	171	163	197	156

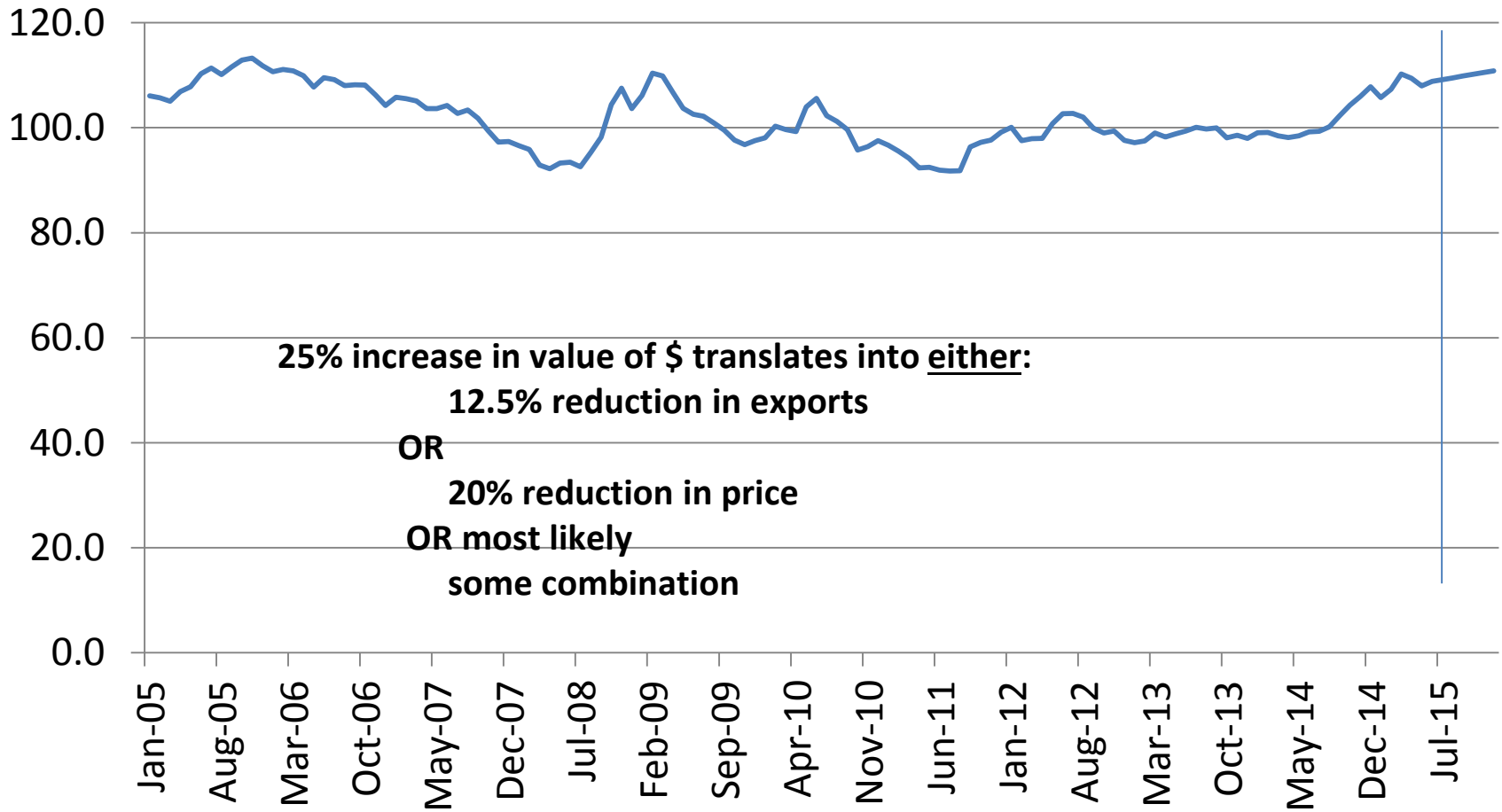
*USDA-NASS June 2015 Estimate

Negative Market Factors....

Uncommitted Flue-Cured and Burley Global Inventories



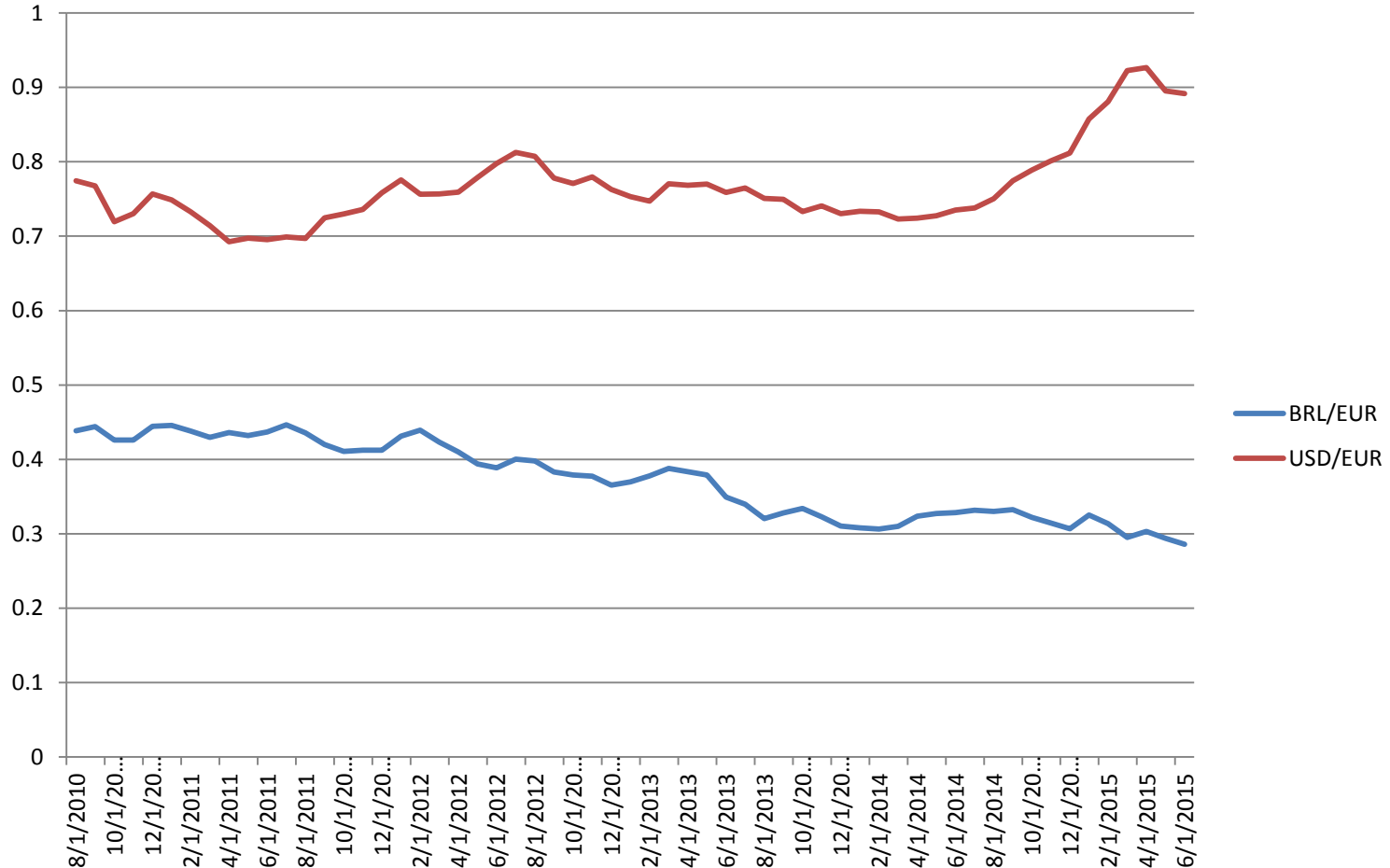
Real Commodity Exchange Rate for US Tobacco



Source: USDA-ERS

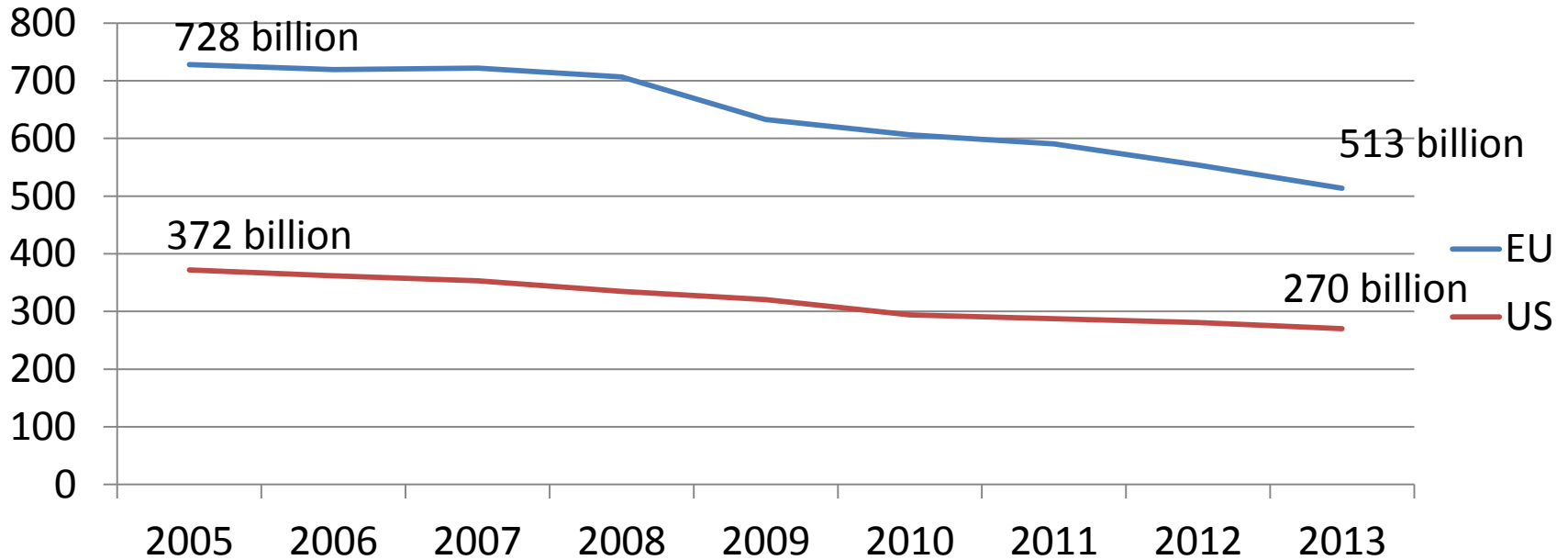
Brazilian Real/EURO & US\$/EURO: 2010-2015

Competitor's exchange rates matter.



EU & US Cigarette Consumption

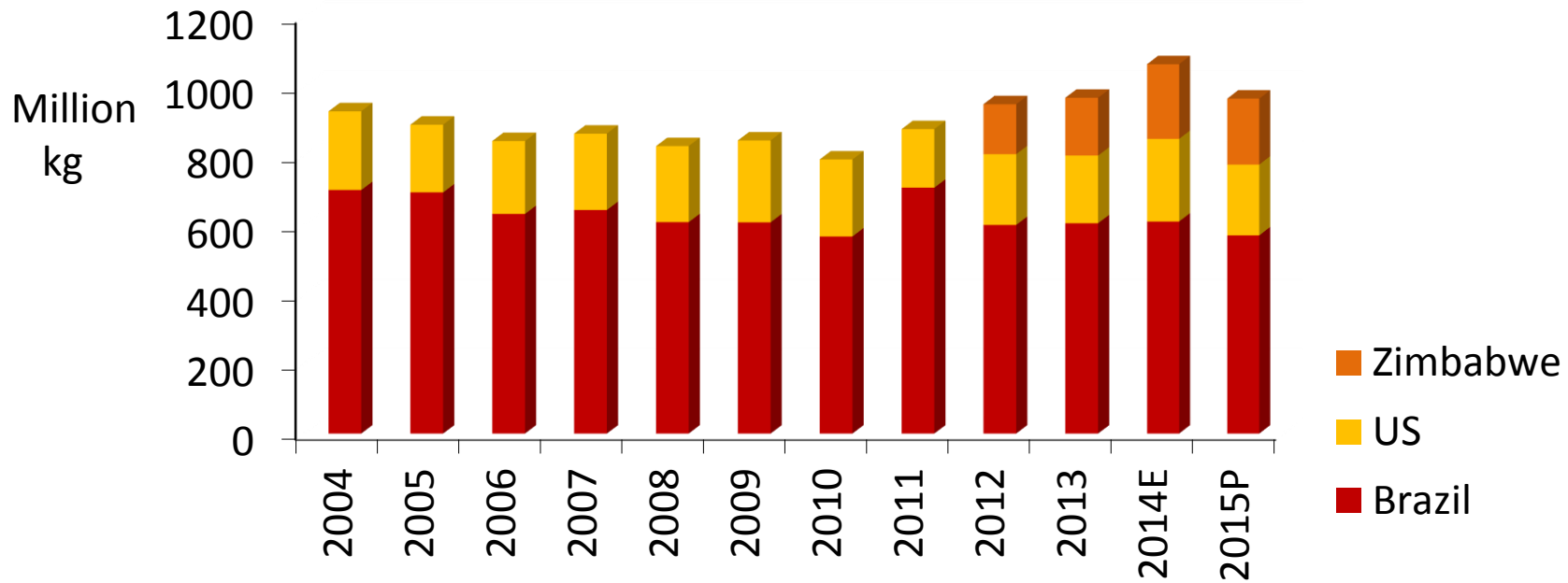
billions of cigarettes



Sources: [Tax Burden on Tobacco, Historical Compilation](#). V48, 2013 Orzechowski and Walker.
Releases for consumption of cigarettes 2002-2013. Taxation & Customs. European Commission

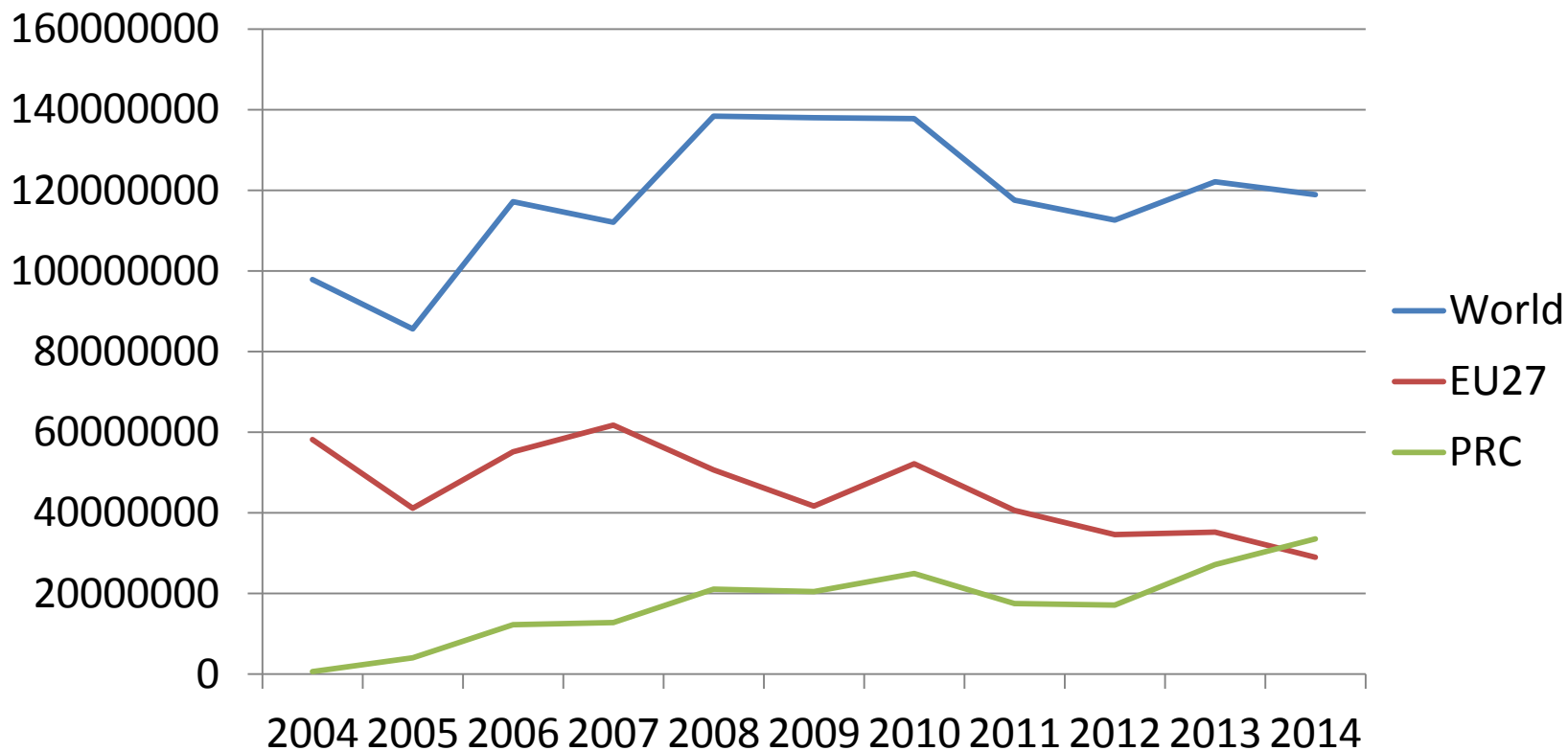
Positive Market Factors...

Global Supply: U.S., Brazil and Zimbabwe Flue-Cured Tobacco Production



Source Brazil & U.S.: Universal Corporation. "World Leaf Production as of Feb 3, 2015."
 Source Zimbabwe: Zimbabwe Tobacco Association "Weekly FCV Report 14.07.2014"

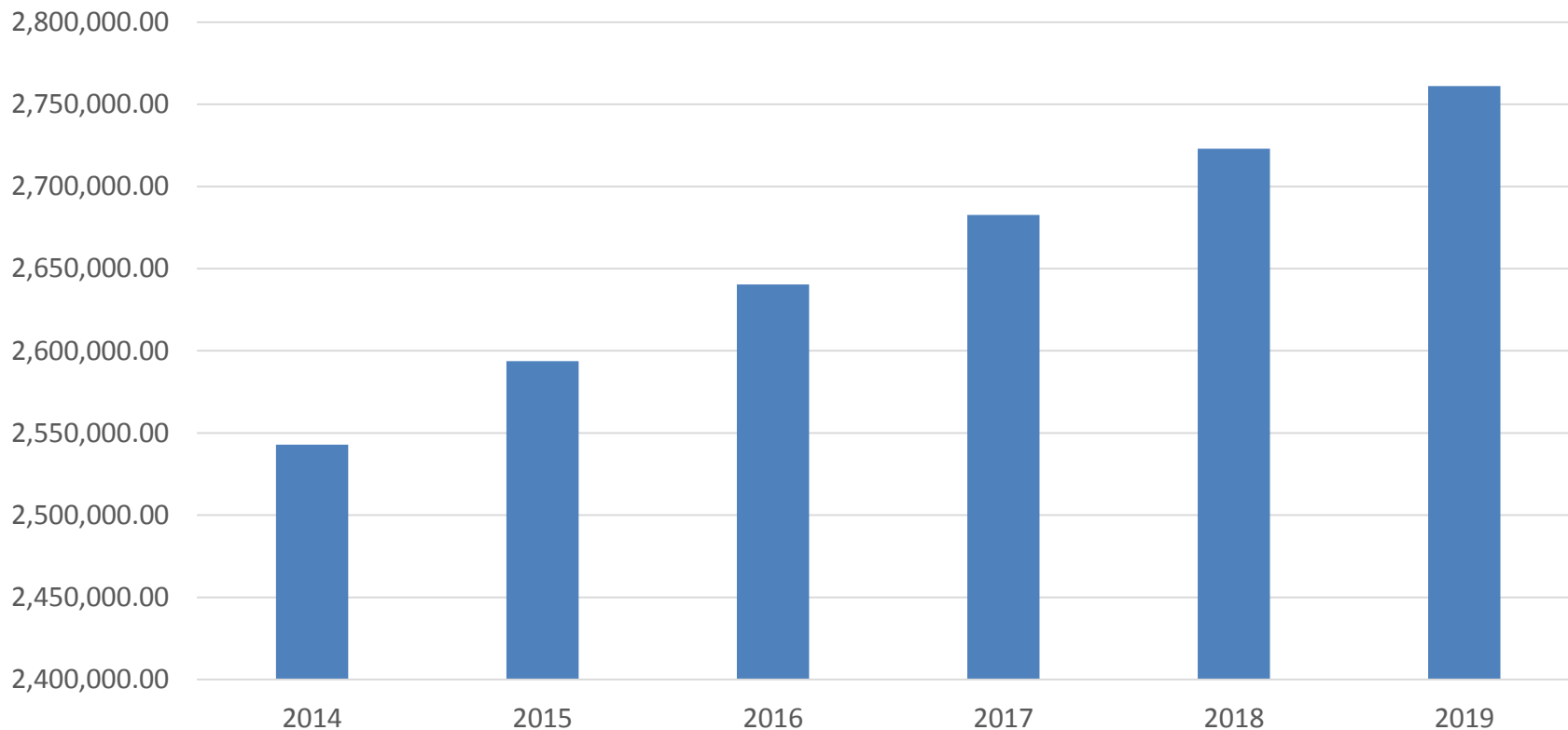
U.S. Unmanufactured Exports of Flue-Cured Tobacco (kg farm weight)



Source: USDA-FAS

PRC Projected Cigarette Sales (Source: Euromonitor International)

Million sticks



China's cigarette demand remains strong

- “As China’s domestic economy continues to strengthen, ... **more consumers will trade up to premium brands, ...**” *IBISWorld Industry Report*
- **Inventories, exchange rates, and slowing economic growth may slow or temporarily stall the increase in exports of US Flue-Cured to China**

Domestic Use and Exports of U.S. Flue-Cured Tobacco (million kg)



Tobacco products will undergo a technological revolution over the next 5-10 years

- **Non-combustibles could dominate traditional combustibles in the U.S. and EU**
- **How new products are regulated and taxed will greatly impact their growth**

e-cigarettes

- Sales estimated at \$2.5 billion in U.S. in 2014
- but sales are slowing
- Vaping category showing dominance
- FDA has issued deeming regulations
- Health community remains divided
- Local regulation and taxation is mixed



“heat-not-burn” products **CONTAIN TOBACCO LEAF**

- PAX



- PMI introduces “Marlboro HeatSticks” in Japan and Italy
 - \$680 million invested in reduced-risk factory in Italy



- Reynolds American introduced heat-not-burn product in Wisconsin in February 2015

Impacts of Technological Change

- *Scenario 1: E-Cigarettes dominate US & EU*
 - Tobacco production for nicotine production
 - Separate tobacco production for exports and combustibles
- *Scenario 2: heat-not-burn products dominate US & EU*
 - Quality of tobacco is more important than ever
 - Change in quantity demanded?

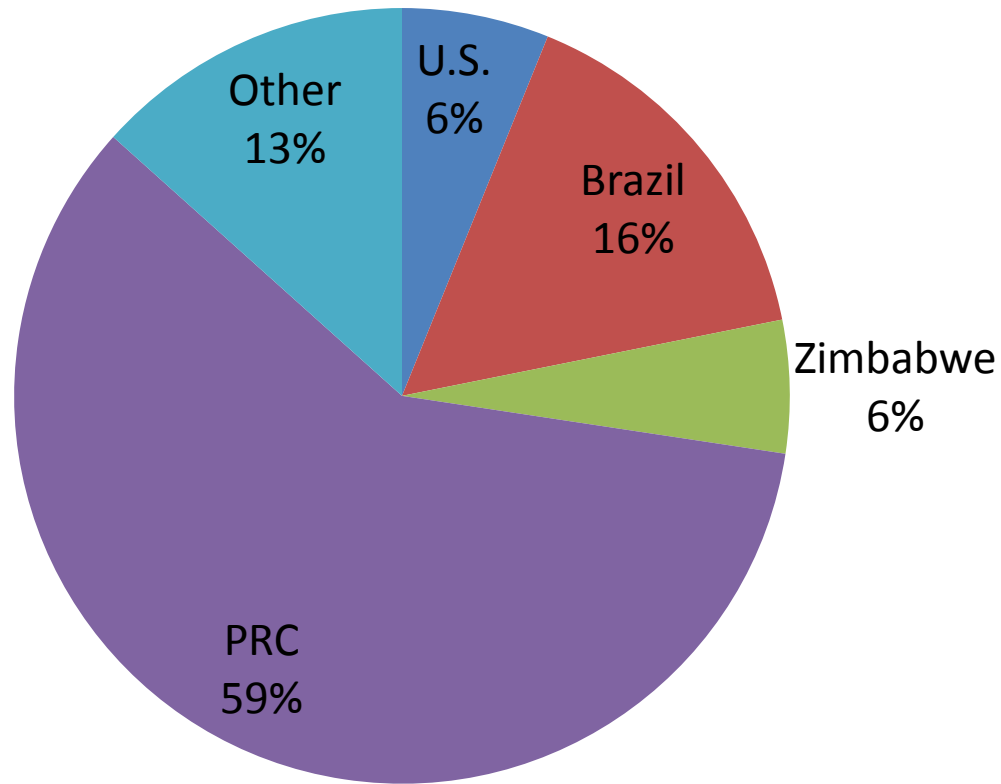
Take Aways...

- **What is needed for a recovery in US tobacco in 2016?**
 - **Smaller crops & reduction of inventories**
 - **More favorable exchange rates**
 - **Growth in China market to offset continued declines in US and EU markets**

Take Aways...

- What is needed for a recovery in 2016?
 - Smaller crops & reduction inventories
 - More favorable exchange rates
 - Growth in China market to offset continued declines in US and EU markets
- **What could de-rail a 2016 recovery?**
 - **Bumper 2015 crops**
 - **Continued weak global economy with weak and lower value currencies of customer countries relative to the \$**

2014 World Flue-Cured Production 4.58 billion kg



Quality is *the* strategic advantage of U.S. flue-cured producers