

TOBACCO PRODUCTS IN UKRAINE: MARKET STATE AND TAXATION



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1. Executive summary

Ukrainian tobacco market has several aspects, which differentiate it from peers in the European Union and other comparable markets.

23% of the adult population consume tobacco and nicotine products daily, another 4% - less regularly. The share of daily consumers is the highest in youngest age group of 18-29 years and decreases with age, which may support the assumption about trend of smoking prevalence reversing upwards.

Cigarettes remain the most popular product among all age groups except 18-29 year olds, where cigarettes, HTPs and electronic cigarettes all have similar share of 43-44%. The youth tends to start consumption from new tobacco and nicotine products and consume multiple products. Positive correlation between a person's income level and the level of tobacco product consumption indicates that pricing affects the consumption.

The role of tobacco excise revenue as increased in recent years, among other factors – due to increased excises. In December 2017, Ukraine approved a seven-year plan to increase the excise tax on tobacco products by 20% annually¹. It was supposed to ensure convergence with the EU Directive on the minimum excise tax liability of at least EUR 90 per 1000 units by 2025.

Since this schedule didn't allow achieving the level of taxation set by the EU due to higher devaluation of Ukrainian hryvna, caused by the full-scale invasion of Russia, it became necessary to revise the excise tax rates in order to gradually reach the minimum level set by the EC Directive 2011/64/EU.

As a result, in June 2024, Parliament of Ukraine approved a new tobacco excise draft law #11090 in the first reading, and in December 2024 the Law was adopted in full.

The law will denominate excise rates in EUR, with the front-loaded increase schedule, which will reach the minimal EU requirements by 2028, with excise for cigarettes reaching ERU 90 per 1000 sticks. Also, since September 2024 Ukraine has introduced excise for oral nicotine pouches, becoming only the tenth country with such excise between EU members and candidates.

As a downside, lawmakers have decoupled excise growth for HTPs from cigarettes, setting the target excise in 2028 20% lower than for cigarettes.

The analysis of the fiscal impacting of increasing tobacco excise taxes, based on the tax model developed by the WüW, shows that the inflation adjusted excise revenues from the cigarettes will increase from the UAH 73 bn in 2024 to UAH 97 bn in 2028, while the industry profits are

¹ <https://zakon.rada.gov.ua/laws/show/2245-19#n2>

expected to remain mostly unchanged, returning to moderate growth in 2028. The excise decoupling is likely to cause a partial shift in consumer behavior from traditional cigarettes. The initial HTP quantity drops from 6,855 million sticks in 2023 to 5,424 million sticks by 2028, but the HTPs consumption is projected to grow after 2026. Such a policy approach will also lead to significant budget losses over the 4-year period.

Thereby one of the key policy challenges for the coming years with the significant impact on health and fiscal revenues will be to increase the excise for HTPs

Four largest producers of tobacco products in Ukraine pay 99.7% of domestic excise revenues. Among them, there are four multinational companies (BAT, JTI, PMI and Imperial Tobacco) and one larger local plant. For the last 12 months, ending in October 2024, the monthly sales averaged UAH 9.7 bn, or UAH 116.6 bn annualized.

There is strong public demand to finance military needs but at the same time society expects to avoid rising taxes on consumption. Therefore, there is a public request to fight illicit sales and close loopholes in the tobacco industry. Even though, tobacco excise increases are well accepted.

There is still a significant issue with illicit sales, with estimates of the illicit market share ranging between 10 and 20%. The distribution of illicit tobacco products is conducted mostly through kiosks, street vendors, and online sales, especially – groups in Telegram messenger. Tackling the illicit trade is one of prerequisites for decreasing accessibility of tobacco products, especially for youth. This will also make the fiscal measure more effective for both decreasing the consumption and increasing the budget revenues.

2. Consumption of tobacco products by Ukrainian households, quantity and value

Kyiv International Institute of Sociology conducted a survey on “Consumption of tobacco and nicotine products and attitudes towards tobacco control measures” in October 2024. The study was conducted using computer-assisted telephone interviews (CATI). The respondents were only people over 18 and only those who resided in the government-controlled territory of Ukraine at the time of the survey. A total of 2019 interviews were conducted as part of the study. Respondents from 24 regions of Ukraine and the city of Kyiv took part in the survey.

27% of respondents currently use tobacco or nicotine products (daily or not). 23.3% use them daily, and the remaining 3.7% use them from time to time.

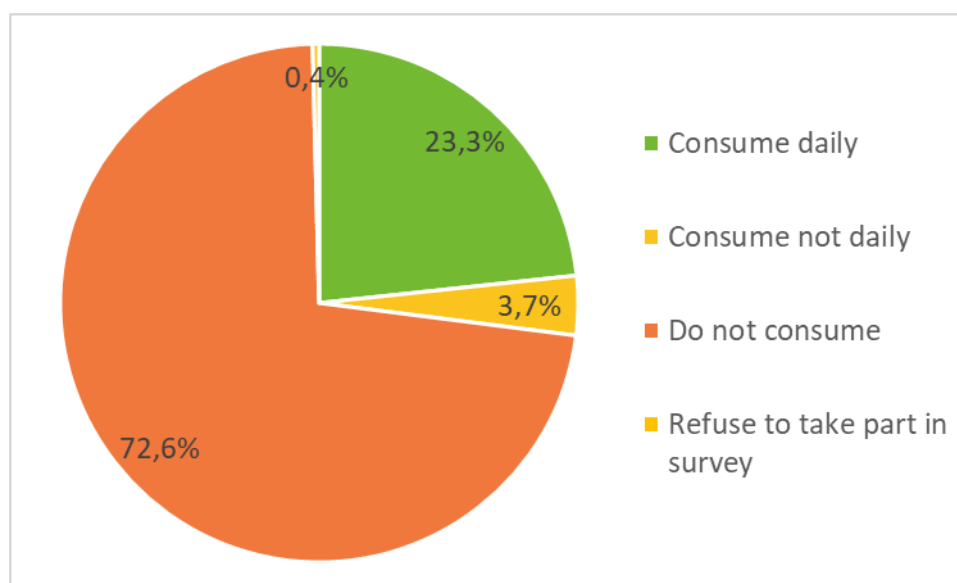


Figure 1. Consumption of tobacco and nicotine products in Ukraine in October 2024^{2 3}

Among these 27% who consume tobacco or nicotine products daily or not daily, the most popular type of product is a cigarette (68,7%). The second position holds Heated tobacco products (HTP), like IQOS or Glo (22,8%). E-cigarettes were the third product by popularity (15,8%).

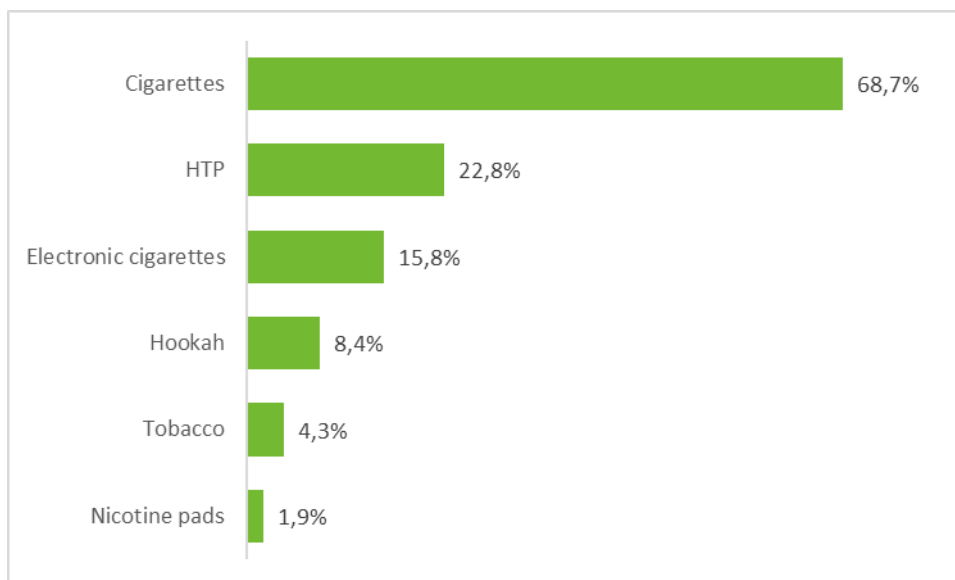
Figure 2. The most commonly used tobacco or nicotine products in Ukraine⁴

²https://www.kiis.com.ua/materials/pr/20241122_z/%D0%90%D0%BD%D0%B0%D0%BB%D1%96%D1%82%D0%B8%D1%87%D0%BD%D0%B8%D0%B9%20%D0%B7%D0%B2%D1%96%D1%82%20%D0%9E%D0%BC%D0%BD%D1%96%D0%B1%D1%83%D1%81%202024.pdf

³ The World Health Organization (WHO), in the survey published on May 31, 2023, stated that approximately 27.4% of respondents were current users of tobacco and nicotine products, 23% of the respondents were daily users. Both surveys, WHO and KIIS, included HTP and e-cigarettes in their model <https://www.who.int/europe/news/item/31-05-2023-world-no-tobacco-day-2023--ukraine-survey-results-highlight-challenges>

https://www.kiis.com.ua/materials/pr/20241122_z/%D0%90%D0%BD%D0%B0%D0%BB%D1%96%D1%82%D0%B8%D1%87%D0%BD%D0%B8%D0%B9%20%D0%B7%D0%B2%D1%96%D1%82%20%D0%9E%D0%BC%D0%BD%D1%96%D0%B1%D1%83%D1%81%202024.pdf

⁴<https://center-life.org/wp-content/uploads/2024/03/Vzhyvannia-tiutiunovykh-ta-nikotynovykh-vyrobiv-ta-stavlennia-do-antytiutiunovykh-zakhodiv-hruden-2023.pdf>



The majority (68.7%) of tobacco and nicotine product consumers smoke cigarettes, although the rate has decreased since 2023 (74.7%). Considering that the HTP consumption rate increased compared to 2023, it can be assumed that smokers of cigarettes and tobacco shift to HTP. However, such an assumption requires further research. There is a positive correlation between a smoker's age and their consumption of cigarettes. In other words, older smokers are more likely to consume cigarettes over other tobacco products. Also, the level of cigarette consumption is lower in big cities compared to small towns or villages. 79% of smokers in the village consume cigarettes, while the equivalent rate in the cities with a population of more than 100 thousand equals 58.9%. Moreover, there is an inverse relation between consumer affluence and cigarette consumption. 81% of smokers with low levels of income consume cigarettes, while this rate for wealthy consumers is 55.2%. This data suggests that cigarettes are inferior goods nowadays.

In Ukraine, tobacco and nicotine products are more prevalent among males (39.5%) than females (16.7%). When looking at distribution of consumption by product types across the age groups, the share of the age group, that consumes cigarettes, increases with age.

Cigarettes remain the most popular product among all age groups except 18-29 year olds, where cigarettes, HTPs and electronic cigarettes all have similar share of 43-44% (given the simultaneous consumption of multiple product types).

The notable inverse correlation between age and share of the age group that consumes the HTPs, and electronic cigarettes may indicate even higher share of consumption of these products in the subset of underage smokers.

Females prevail in the consumption of HTPs and electronic cigarettes. The share of these products in the consumption of the subset of female smokers (34.2% and 20.4% respectively) is almost twice higher than among male smokers (17.0% and 13.4% respectively).

Furthermore, there is a positive correlation between a person's income level and the level of tobacco product consumption. 27.4% of people with a low-income level consume tobacco products, compared to 33% of smokers with higher income.⁵

The same goes for HTPs, the share of consumption grows with an increase in income. Only 8.6% of smokers with low-income levels use HTP, while 33.3% of smokers with high income consume HTPs. Moreover, HTPs and e-cigarettes are more prevalent in big cities rather than in villages or small towns.

Cigarettes have the highest share in consumption of the members of low (but not very low) income families, while the overall prevalence of tobacco and nicotine products is highest among the high-income consumers.

⁵ “Very low” level of income means that household member replied that they do not have enough money even for food; “low” – those that have enough money for food, but not enough for clothing; “medium” – those that have enough money for both food and clothing, but not enough to buy some expensive things (TV, etc.); “high” – those that can afford some expensive things or can afford everything in general

Figure 3. Consumption of tobacco or nicotine products in Ukraine by socio-demographic categories⁶

% in a row	Current consumption			▶	Types of products consumed				
	<i>In total</i>	<i>Daily</i>	<i>Not daily</i>	▶	<i>Cigarettes</i>	<i>HTP</i>	<i>Electronic cigarettes</i>	<i>Hookah</i>	<i>Tobacco</i>
Gender									
Male	39.5	34.9	4.6	▶	72.9	17.0	13.4	9.1	6.1
Female	16.7	13.7	3.0	▶	60.5	34.2	20.4	7.1	0.7
Age									
18-29 years	32.9	27.4	5.5	▶	43.7	44.6	44.2	21.2	0.6
30-39 years	32.5	27.1	5.4	▶	59.6	34.6	21.7	12.3	0.7
40-49 years	29.5	25.3	4.2	▶	76.1	14.4	6.0	4.7	8.1
50-59 years	30.7	27.7	3.0	▶	84.3	9.5	3.2	1.7	3.3
60-69 years	20.5	18.6	1.9	▶	82.9	5.7	0.0	0.0	11.4
70+ years	11.1	9.9	1.2	▶	87.2	4.7	0.0	0.0	8.1
Region									
West	21.5	17.1	4.4	▶	70.4	14.3	15.1	10.4	1.7
Center	26.6	23.2	3.4	▶	72.7	22.1	15.1	8.7	2.5

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https://www.kiis.com.ua/materials/pr/20241122_z/%D0%90%D0%BD%D0%B0%D0%BB%D1%96%D1%82%D0%B8%D1%87%D0%BD%D0%B8%D0%B9%20%D0%B7%D0%B2%D1%96%D1%82%20%D0%9E%D0%BC%D0%BD%D1%96%D0%B1%D1%83%D1%81%202024.pdf

South	32.0	28.1	3.9	►	62.9	29.7	20.8	8.7	4.0
East	32.3	30.4	1.9	►	66.8	24.8	6.1	2.6	16.4
<i>Type of settlement</i>									
Village	22.7	19.0	3.7	►	79.0	10.5	15.2	5.4	4.5
Urban-type settlement (under 20K)	24.6	21.2	3.4	►	83.7	14.9	7.4	12.3	1.4
City (20K-99K)	27.6	26.2	1.4	►	72.9	20.8	14.4	9.9	6.2
City (100K+)	30.6	26.2	4.4	►	58.9	31.6	18.0	8.9	4.3
<i>Level of family's income</i>									
Very low	27.4	22.7	4.7	►	61.7	8.6	8.5	0.0	17.6
Low	24.0	20.3	3.7	►	81.0	15.0	9.3	3.0	5.6
Middle	26.4	24.0	2.4	►	68.8	25.4	15.2	9.3	1.5
High	33.0	26.8	6.2	►	55.2	33.3	26.9	16.5	2.3

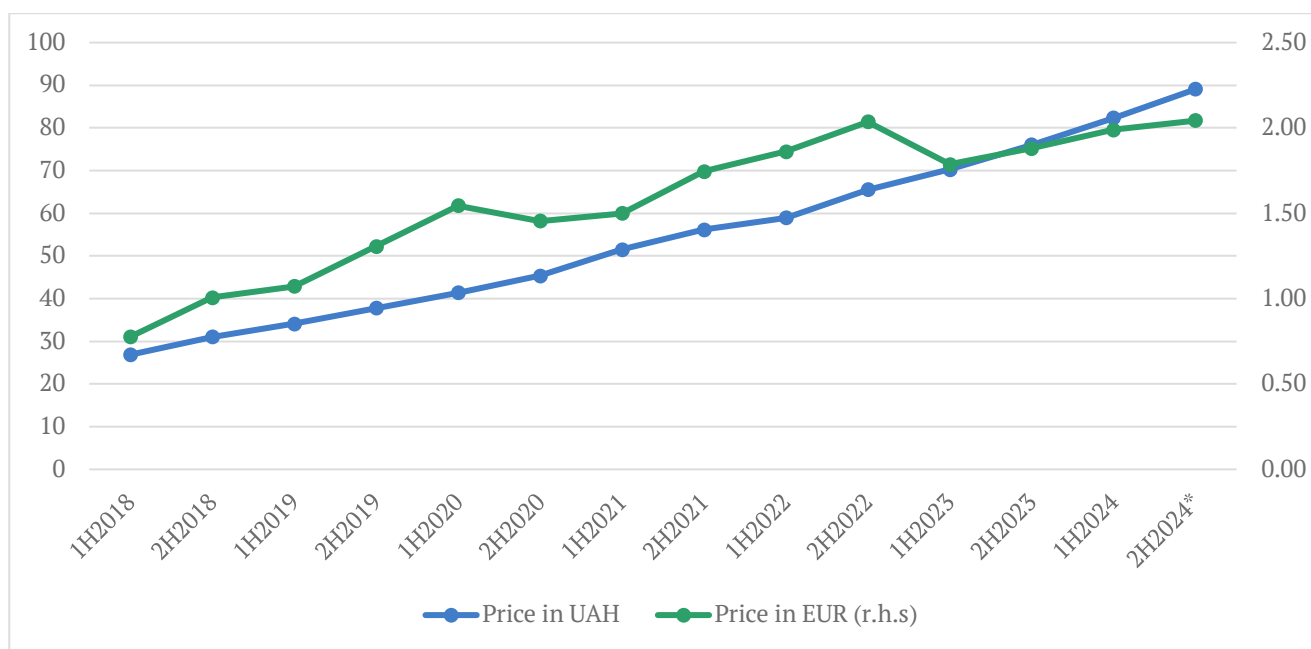
Source: survey prepared by Kyiv International Institute of Sociology in October 2024
“Consumption of tobacco and nicotine products and attitudes towards tobacco control measures”

3. Pricing

As of May 2024, the price of 20-cigarette pack of medium-class cigarettes with filter averaged UAH 87.14 (~EUR 2.00), increasing by 231% in nominal terms, or by 155% in real terms since January 2018. This price would include UAH 50.34 of excise tax and UAH 14.53 of the VAT, making total indirect taxes amount to 74.4% of the retail price.

Due to adopted excise increase plan and inflation the average pack price increased steadily in nominal terms throughout the last 6 years, however the price denominated in EUR stopped just above EUR 2.0 due to devaluation of Ukrainian hryvnia after the full-scale invasion.

Figure 4. Price of 20-cigarette pack of medium-class cigarettes



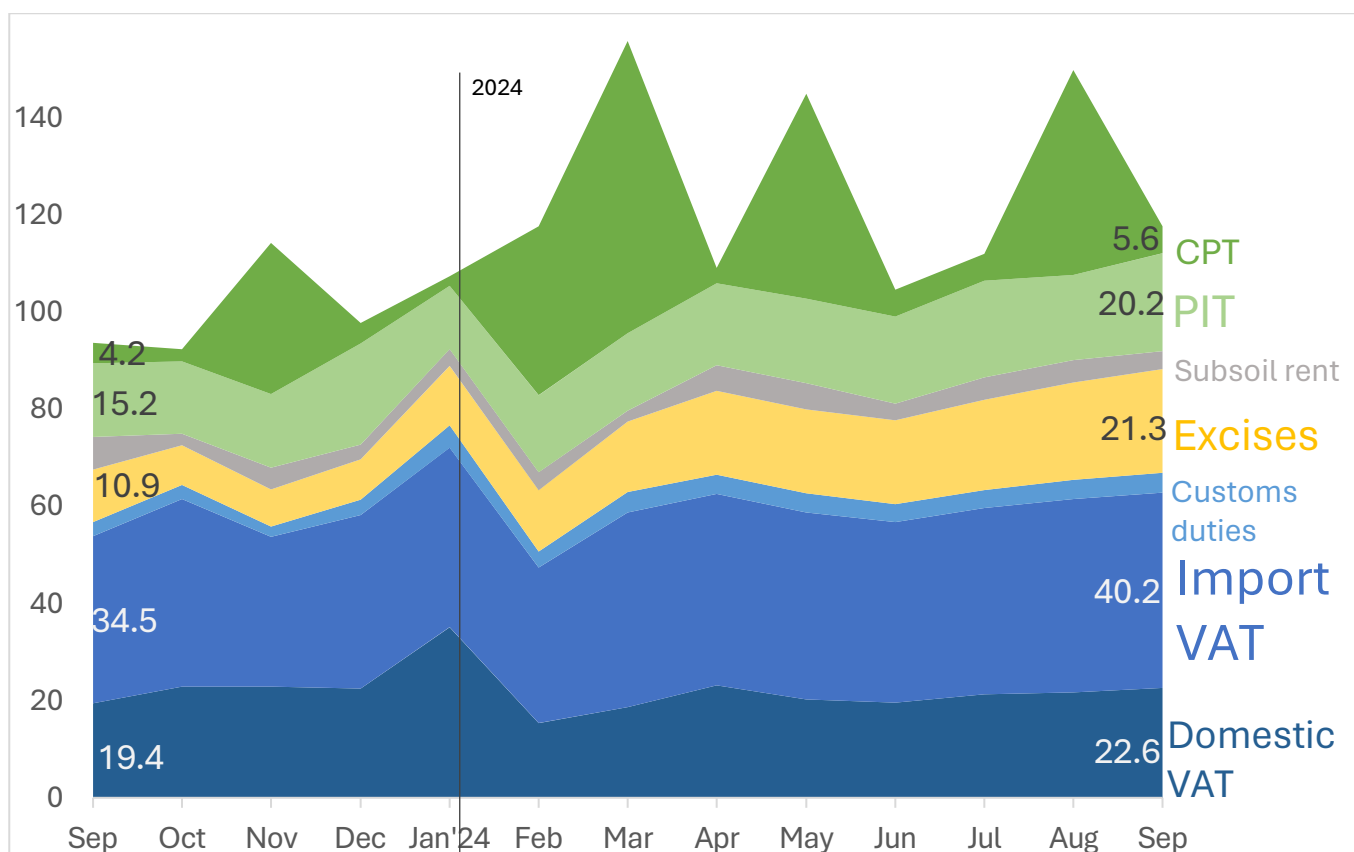
4. Sales and tax revenues

Overall tax revenues of the state budget are steadily growing, adding 26% y-o-y in September 2024, while the accumulated CPI for this period reached 8.6% and the base inflation – 7.3%.

Of the UAH 117.9 bn of September revenues, UAH 21.3 were excises revenues, which increased by 95% y-o-y. Of these 21.3 bn, 10 bn (~ EUR 225 mln) were tobacco excises.

Figure 5. Monthly state budget tax revenues, UAH bn ⁷

⁷ CPT - Corporate Profit Tax, PIT – personal income tax, subsoil rent - rent for the use of natural resources, VAT - Value Added Tax, collected from imports or domestic goods.

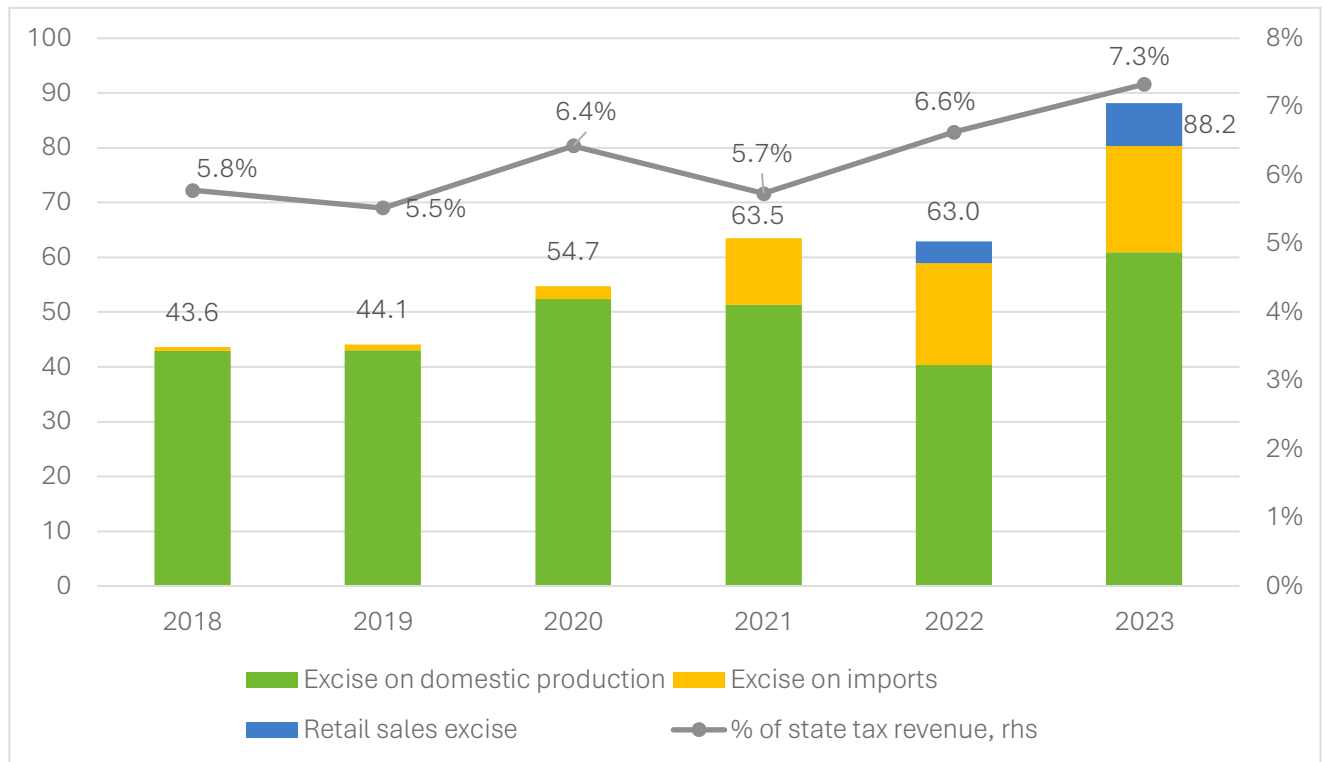


The role of tobacco excise revenues for the consolidated budget is increasing with the increase of revenues. The nominal excise revenues in 2023 have grown by 38.9% compared to pre-war year 2021, exceeding the accumulated inflation, and despite population decrease, estimated at 14%.

This led to an increase in the share of the excise revenues in the state budget from 5.7% to 7.3%. Since 2022 a retail sales excise revenue that used to go to the state budget is being transferred to local budgets. The retail sales excise is an excise of 5% of the retail sales price. Initially it was paid by the retailers, but to improve the tax compliance, the obligation to pay the excise was shifted to importers and domestic manufacturers, based on the volume of sales and maximal retail sales prices.

The excise is distributed by the Treasury to local budgets, based on the share of registered retail sales in every local authority, calculated by the State Tax Service for every month based on the data from the cash registers. Such design is intended to stimulate local authorities to enforce the tax compliance of tobacco retail sales at local level in order to increase tax revenues to their budgets.

Figure 6. Tobacco excise revenues and shares



The only reliable sales data is the one on volume of sales of tobacco products via cash registers, available for the period starting April 2023. For the last 12 months, ending in October 2024, the monthly sales averaged UAH 9.7 bn, or UAH 116.6 bn annualized.

As per market intelligence, conducted by Forbes Ukraine⁸, the main market players as of the end of the 2023 were the following:

⁸ <https://forbes.ua/company/siri-konyachki-svitovi-giganti-i-ne-monopolist-khto-u-top-10-naybilshikh-tyutyunovikh-kompaniy-ukraini-01122023-17619>

Company*	Key brands (domestic production and imports)	Annual sales, UAH bn (incl. exports)
Philip Morris	Marlboro, Heets, IQOS,Parliament, L&M	28-30
British American Tobacco	Vogue, Dunhill, KENT, Rothmans, Lucky Strike, Capri, Pryluky	29.6
JTI Ukraine	Camel, Winston, Glamour, Monte Carlo	22.5
Imperial Tobacco	Davidoff, West, Jade, Parker & Simpson, Imperial Classic, Pryma	9.6
Galychyna-Tabak	Sk, Estrada, Barge, Derzhavna, Grelka	6.9
Marvel	Marvel, Compliment, Strong, Lifa, Kyiv	6.4

*distribution companies without brands excluded to avoid double counting

5. Current and future excise tax design

In Ukraine, the ad-valorem and specific excise rates apply to tobacco products. The Tax Code also stipulates that total tax obligation should not be less than the minimal tax obligation set across different tobacco and nicotine products. In most cases, the minimal tax obligation is higher than the tax obligation calculated according to the law, and thus, the minimal tax serves as the effective excise burden.

Such a situation occurs due to low ad-valorem rate of 12%, which comes into play for the most expensive tobacco products only.

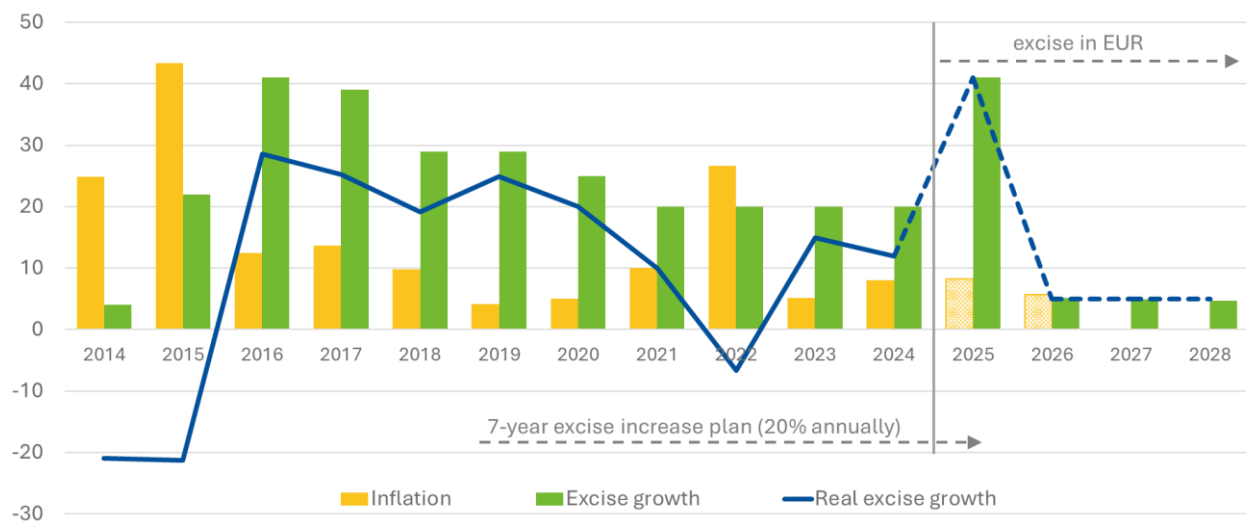
In December 2017, Ukraine approved a seven-year plan to increase the excise tax on tobacco products by 20% annually⁹. It was supposed to ensure convergence with the EU Directive on the minimum excise tax liability of at least EUR 90 per 1000 units by 2025.

With subsequent amendments, lawmakers increased specific excise by 30% in 2018 and 20+9 % in 2019 (two increases during the year) and approved a further schedule of 20% annual increases until 2025.

⁹ <https://zakon.rada.gov.ua/laws/show/2245-19#n2>

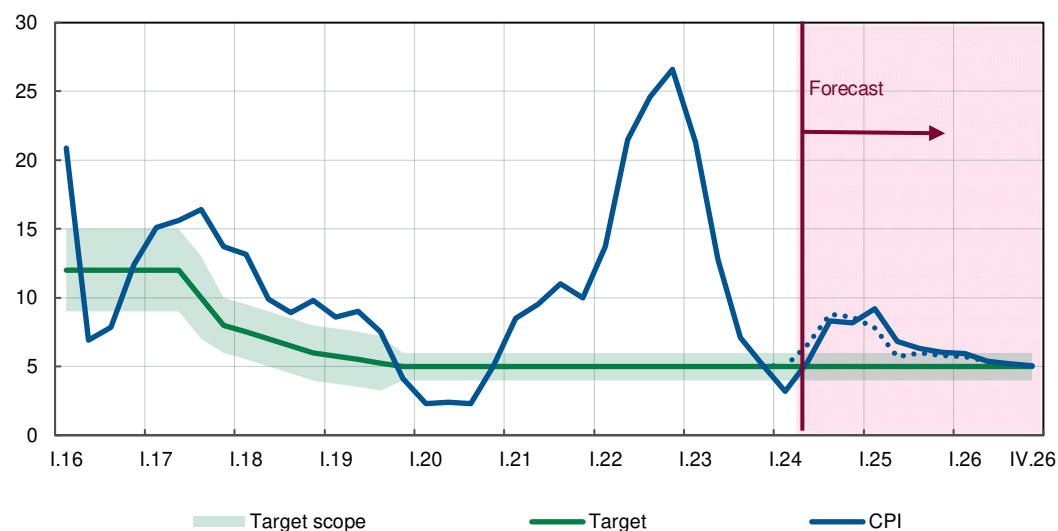
If inflation is accounted for, this schedule led to a steady real excise rate growth, except for 2022, when inflation in Ukraine reached 26%.

Figure 7. Nominal and real excise rates changes, %



Based on the National Bank macroeconomic forecast, we expect 8.2% inflation in 2024 with a slight decline to 5-6% in coming years (barring the fundamental uncertainty caused by Russian aggression).

Figure 8. Actual and forecasted CPI¹⁰



Since the current schedule does not allow achieving the level of taxation set by the EU, it became necessary to revise the excise tax rates in order to gradually reach the minimum level set by the EC Directive 2011/64/EU.

¹⁰ https://bank.gov.ua/admin_uploads/article/IR_2024-Q2.pdf

As a result, in June 2024, Parliament of Ukraine approved a new tobacco excise law in the first reading. This law would make tobacco excise rate denominated in Euro, not Hryvnia.

The law would enable Ukraine to reach the EU excise tax minimum for cigarettes by 2028. The policy would also increase tax revenue.¹¹

Among other positive legislative changes is the introduction of the specific excise for oral nicotine (nicotine pouches), at the level of minimal excise for cigarettes less 5 EUR, per 1 kg. If translated to taxation per 1000 items, it would be an equivalent to about 59 EUR per 1000 items in 2028, when the minimal excise for cigarettes would reach 90 EUR. As tobacco-free nicotine pouches may have the fewest harmful constituents of all tobacco and nicotine products¹² such preference may be reasonable. Currently only 9 EU countries introduced the excise for oral nicotine¹³, with some examples of rates being 0.4 CZK/g in Czech Republic (~16 EUR/kg) and 50 EUR/kg in Greece, which are both lower than the rate of 73 EUR/kg which will be applied in Ukraine in 2025.

Ukrainian lawmakers have also banned the sales of any flavored e-cigarettes, which is intended to reduce the rate of initiation among children and young adults – under the premise that the sales of illicit flavored e-cigarettes would be controlled.

As a downside, in the second reading of tobacco excise Law, lawmakers are expected to consider tax benefits for HTPs, decoupling HTP excise growth from the one of cigarettes.^{14 15}

Figure 9. Excise for tobacco products, increase schedule adopted in the first reading (June 4, 2024)

Excise type	Unit	2021	2022	2023	2024	2024 in EUR	2025	2026	2027	2028
Specific excise		UAH	UAH	UAH	UAH		EUR	EUR	EUR	EUR
Cigarettes	1000 pcs	1 089	1 306	1 568	1 881	41.3	58	61	64	67

11 <https://itd.rada.gov.ua/billInfo/Bills/Card/43855>

12 [WHO study group on tobacco product regulation](#), Section 4

13 <https://wiiw.ac.at/files/events/2-tobacco-taxation-trends-eu-perspective-n-684.pdf>

14 https://biz.ligazakon.net/news/226430_aksiz-na-tyutyunov-virobi-pochne-zrostaty-z-lipnya-2024-ta-bude-v-vro---prokt

15 <https://www.slovoidilo.ua/2024/06/04/novyna/polityka/rada-poperedno-pidtrymala-zakonoprojekt-pro-pidvyshhennya-akcyzu-tyutyunovi-vyroby>

Tobacco, oral nicotine products	1kg	1 368	1 641	1 970	2 363	51.9	73	77	81	85
HTP's	1000 pcs	1 456	1 747	2 097	2 517	55.3	70.40	70.80	71.14	72.00
Liquids for e- cigarettes	litre	3 000	3 000	10 000	10 000	220				
Minimal excise										
Cigarettes	1000 items	1 456	1 748	2 097	2 517	55.3	78	82	86	90
Ad valorem	%	12	12	12	12		12	12	12	12

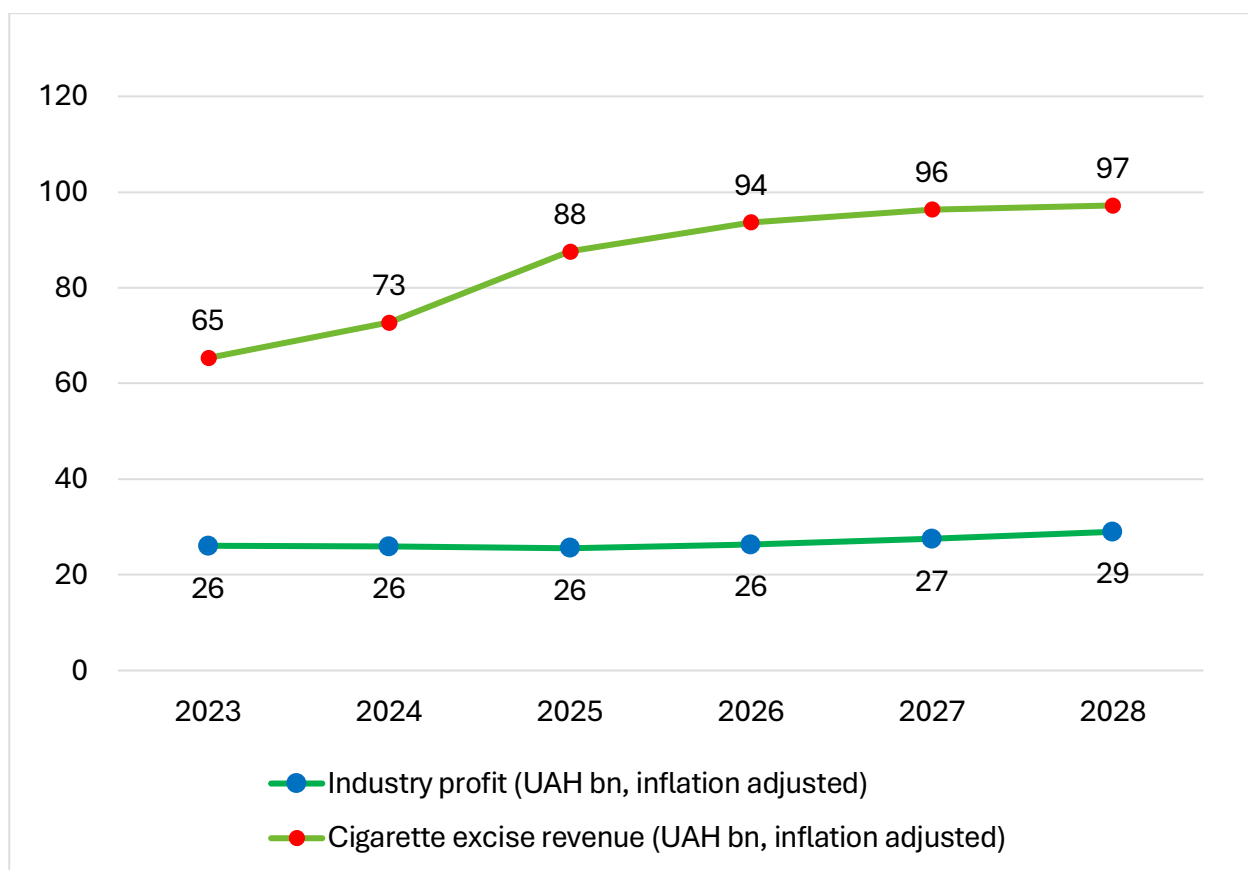
6. Modeling of excise increase effect

The analysis of the fiscal impacting of increasing tobacco excise taxes, based on the tax model developed by the WIIW,¹⁶ shows that the inflation adjusted excise revenues from the cigarettes would increase from the UAH 73 bn in 2024 to UAH 97 bn in 2028, while the industry profits would remain mostly unchanged, returning to moderate growth in 2028. The smoking prevalence would decrease from 23.2% in 2023 to 22% in 2026, but then it will resume slight growth to reach 22.3% in 2028.

The imposed tax policy is predicted to avert more than 93 thousand premature deaths by 2026 with the cumulative effect resulting in almost 80 000 of premature deaths averted by 2028.

Figure 10. Excise revenue and industry profit (UAH bn, real values)

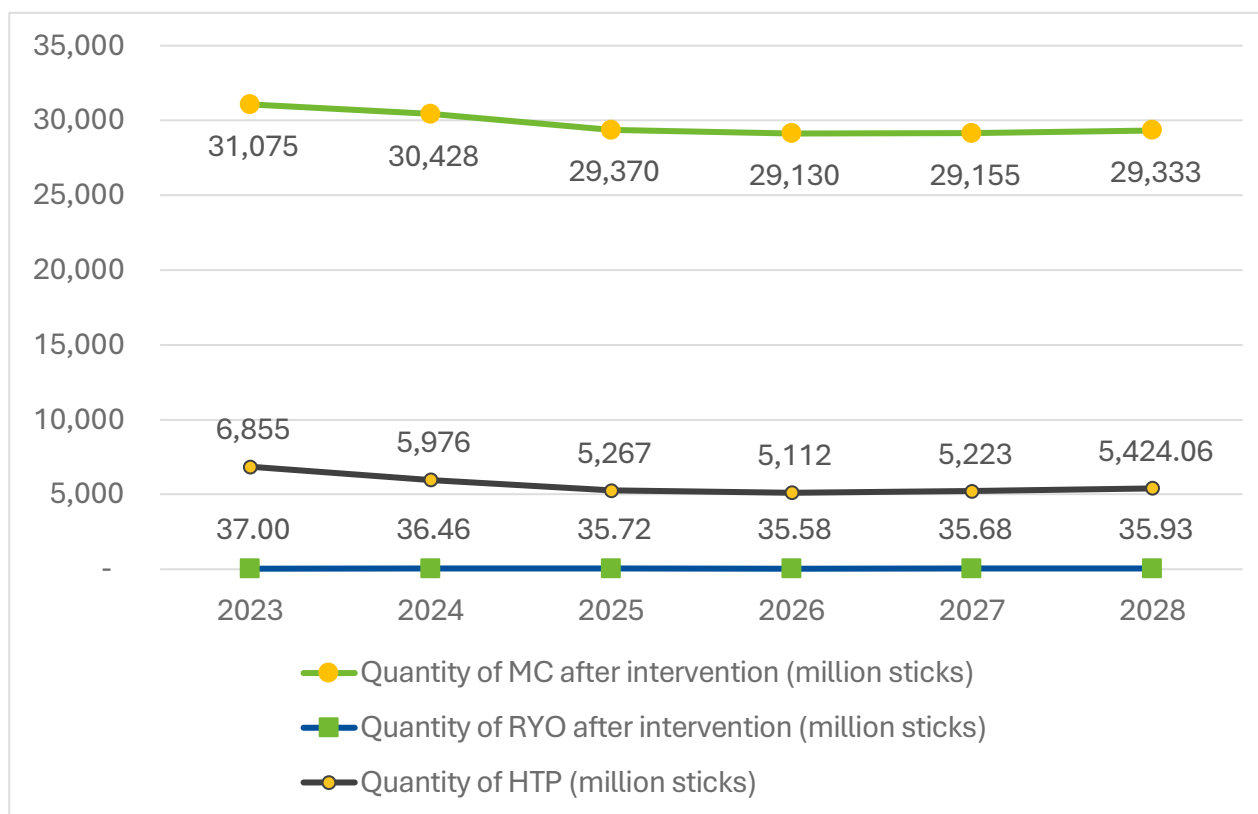
¹⁶ Analysis of the Fiscal and Health Impact of Increasing Tobacco Excise Taxes in Ukraine by Kristijan Fidanovski, Biljana Jovanovikj, Nóra Kungl and Hana Ross, wiiw Policy Note/Policy Report No. 82, August 2024,



Modelling shows a notable decline in the consumption of manufactured cigarettes, reducing from 31,075 million sticks in 2023 to 29,333 million sticks in 2028, reflecting a sustained decrease as a result of increased excises and shifts in consumer preferences toward alternative products.

In contrast, if the excise decoupling is approved (see Figure 9), the heated tobacco products (HTP) would show a slower decline, which suggests a partial shift in consumer behavior from traditional cigarettes. The initial HTP quantity drops from 6,855 million sticks in 2023 to 5,424 million sticks by 2028, but the HTPs consumption is projected to grow after 2026.

Figure 11. Consumption after the intervention (million sticks)



7. Domestic manufacturing capacities and imports

Four largest producers of tobacco products in Ukraine pay 99.7% of domestic excise revenues. Among them, there are four multinational companies (BAT, JTI, PMI and Imperial Tobacco) and one larger local plant. Also, there are other international and regional companies that have minor production capacities in Ukraine.

Before the Russian full-scale invasion of Ukraine on February 24, 2022, PMI (Philip Morris International) had a market share of around 28.5% of Ukrainian tobacco market¹⁷. The company's production capacities were located in the Kharkiv region, the territory of military actions in 2022, and intense missile and artillery attacks after the liberation of the Kharkiv region in 2022. As a result, due to safety measures and logistical issues, plant in the Kharkiv region couldn't be used. PMI's market share dropped to 14% in two months after the full-scale invasion. To continue its presence in Ukrainian market, company established imports from PMI factories abroad and in August 2022 signed a contract with Imperial Tobacco for manufacturing PMI products until December of 2024 at their plant in Kyiv¹⁸. As of October 2023, the PMI's CEO reported the market share rebound to around 24%, close to the pre-invasion level.

17 <https://interfax.com.ua/news/economic/939571.html>

18 <https://www.rbc.ua/rus/news/galina-vorobyova-imperial-tobakko-prodakshn-1716977464.html>

In May 2024, PMI opened a new plant in Western Ukraine (Lviv region). Investments in a new plant were around \$30 mln¹⁹. It took about one year from the first public mention of plans to build a new plant in Lviv region to start of its functioning. The company plans to relocate and employ workers from the Kharkiv factory on their new plant on the West of Ukraine²⁰.

Figure 12. Domestic producers of tobacco products (production capacities and taxes paid) in 2023

	Production, mln sticks		Taxes paid, UAH mln				Taxes per 1 ton of raw tobacco, UAH mln
	Cigarettes	HTP's	Excises	VAT	PIT	Total	
BAT	10 726	905	21 122	5 911	198	27 231	24.3
JTI	10 203	0	17 348	4 801	120	22 270	14.8
Imperial Tobacco	9 265	0	17 098	4 702	3	21 803	25.6
Vynnyky plant	1 244	0	4 831	810	66	5 707	7.7
Phillip Morris ²¹	10 000 ²²	n/d	24 000	6 400	n/d	n/d	n/d
Total	31 438	905	60 399	16 225	387	77 011	n/a

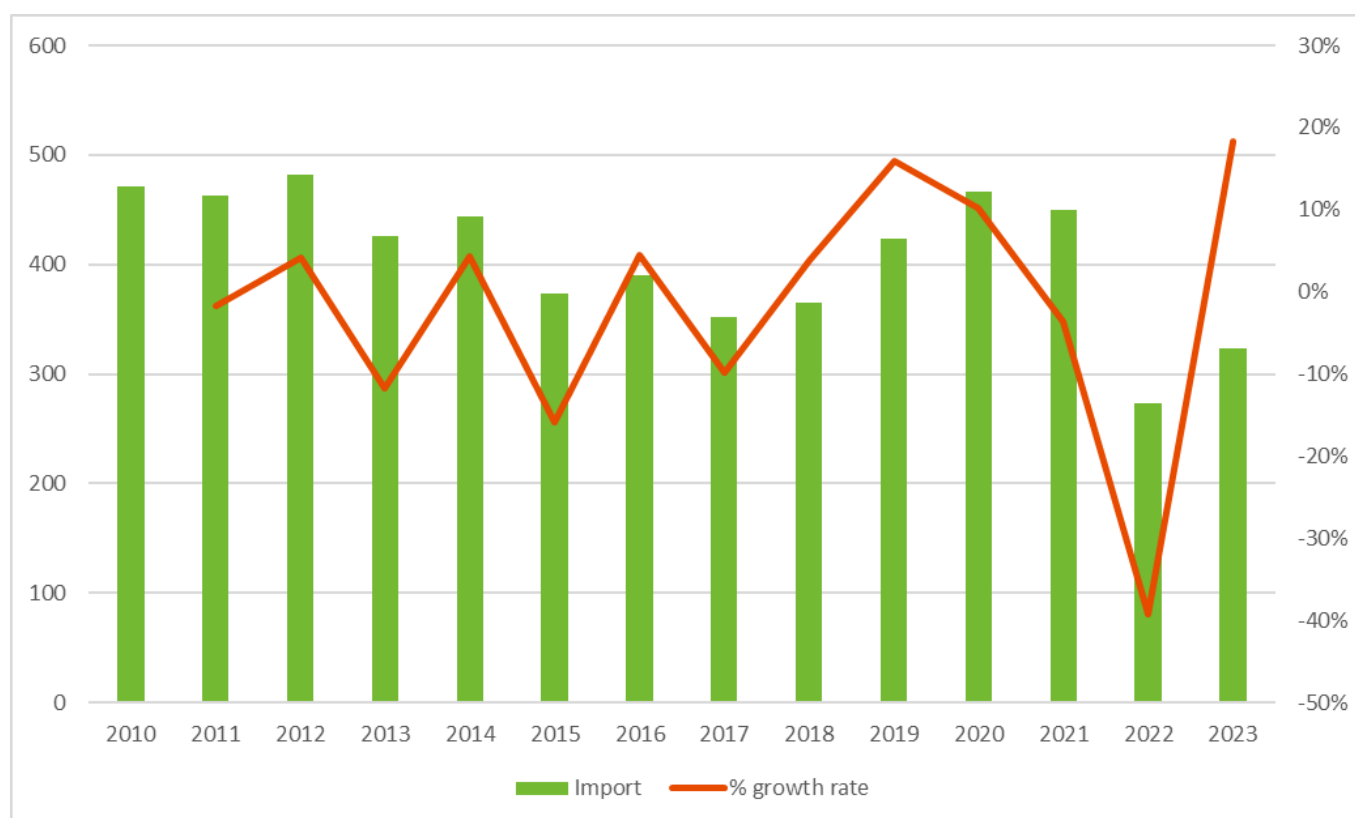
19 <https://www.pmi.com/markets/ukraine/uk/media-center/details-news?articleId=article-philip-morris-investment-in-Ukraine-2023>

20 <https://www.pmi.com/markets/ukraine/uk/media-center/details?articleId=philip-morris-launched-new-factory-in-lviv-2024>

21 <https://www.pmi.com/markets/ukraine/uk/media-center/details/philip-morris-increased-tax-deductions-in-2024>

22 <https://www.pmi.com/markets/ukraine/uk/media-center/details?articleId=philip-morris-launched-new-factory-in-lviv-2024>

Figure 13. Real value of imported tobacco products to Ukraine in USD millions, 2010-2023 (2010 as a base year)

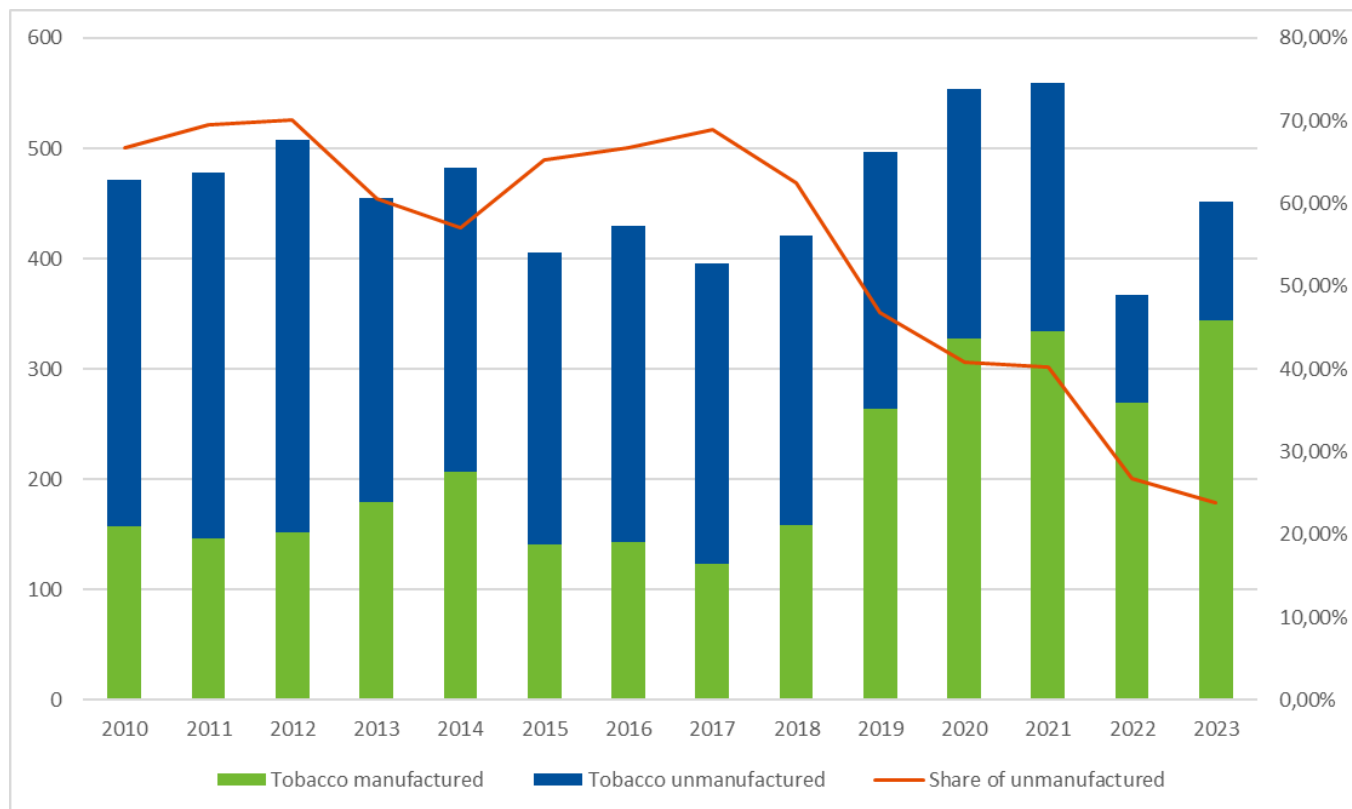


From 2010 to 2023, the volume of imported tobacco products to Ukraine decreased by 19 USD million or by 4% in nominal values.

In 2010 – 2012 the import value of tobacco products showed a stable increase. In 2013 – 2017 the protracted declining trend dominated the market with minor fluctuations. One of the main reasons for the contractionary trend is the fact that hryvnia (UAH) weakened against the US dollar (USD) in 2014 – 2015 and the lower volume of international trade with Russia was partially substituted by domestic production. In 2017-2021 the market recovered from the previous downturn and sharply grew by 41% in 5 years. In 2021, the value of imported tobacco products in nominal values reached a peak of 559 USD million.

Due to the Russian full-scale invasion of Ukraine, the import of tobacco products declined by more than 34%, reaching its bottom of 367 USD million in nominal value. In 2023, the value of imports recovered by 23%, compared to the previous year, and attained 452 USD million nominally.

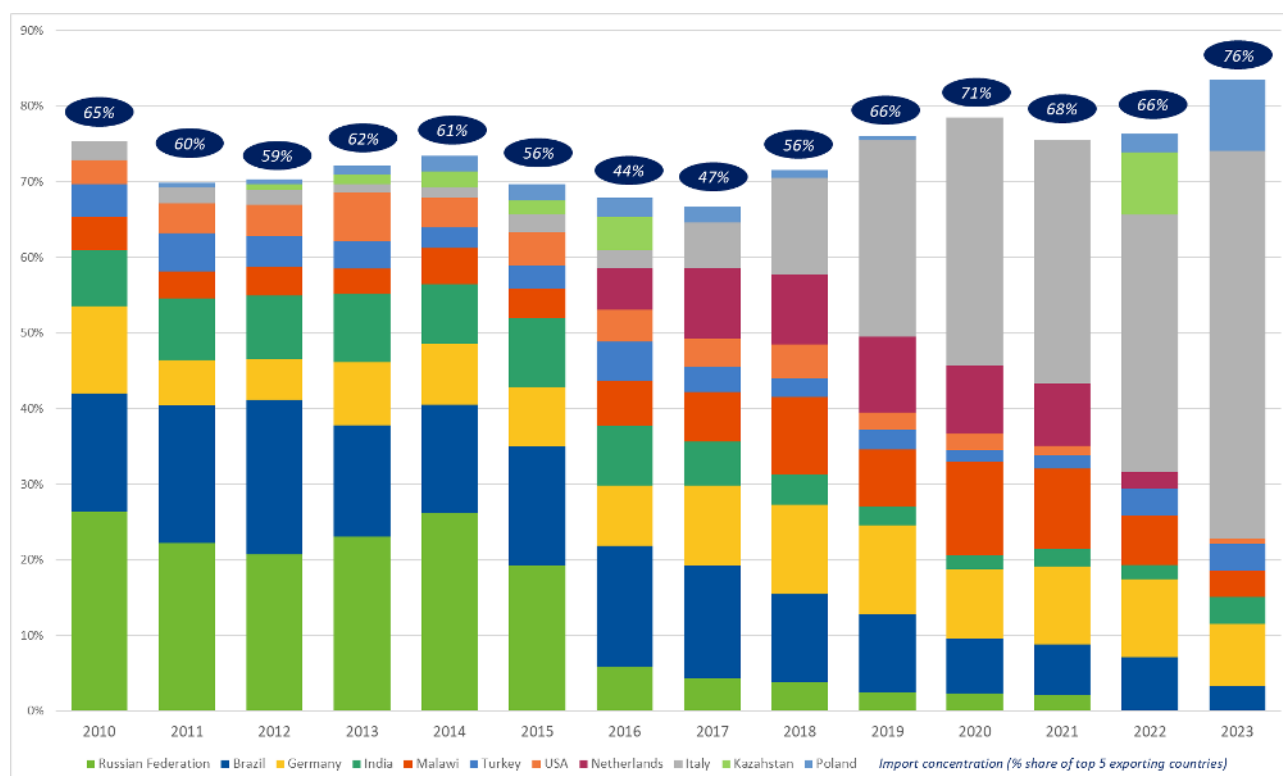
Figure 14. Structure of tobacco products import in Ukraine in USD millions, 2010-2023



Due to relatively low production costs and peculiarities of the production process, raw tobacco (not stripped tobacco, wholly or partly stripped tobacco, and tobacco refuse) dominated the structure of imported tobacco products to Ukraine in 2010 – 2018. From 2010 to 2018, the share of unmanufactured tobacco fluctuated between 57% - 70% of overall tobacco products import. But since 2019 the share of unmanufactured tobacco products has been lower than 50%, demonstrating the steady downturn trend. This tendency is linked with uncertainties of international partners investing in production in the country during the war and economic instability.

After 2022, some manufacturers' plants were destroyed or damaged by Russian strikes, so these companies had to import tobacco products to maintain their Ukraine's market share. This fact explains the tendency of the decreasing share of unmanufactured tobacco in the structure of Ukraine's import of tobacco products.

Figure 15. Countries with the largest exports of tobacco and tobacco products to Ukraine



Russian tobacco products constituted 20%-26% in the structure of Ukraine's tobacco products import during 2010 – 2014. But after the beginning of Russian-Ukrainian war in February 2014, Russian share started declining and trade volumes between two countries began to decrease. Since 2022 there were no import of Russian tobacco products to Ukraine.

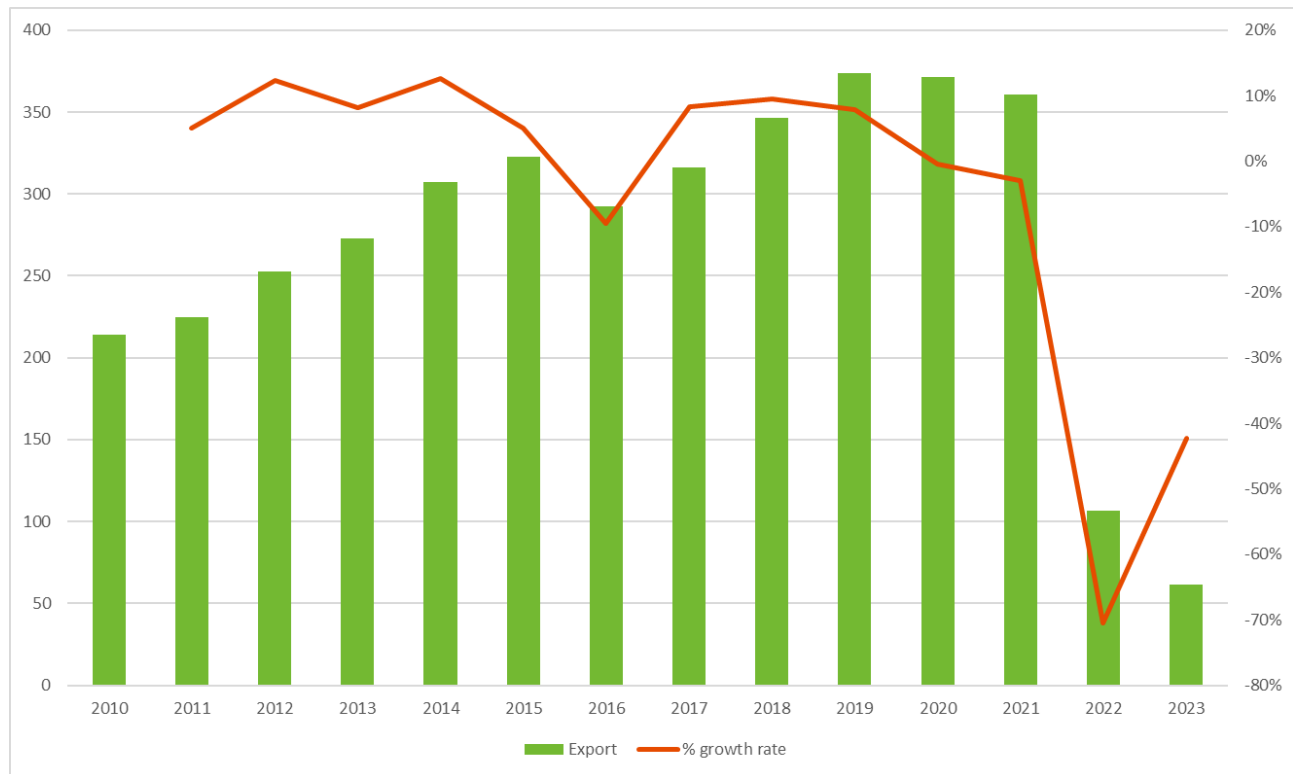
Since 2017, the import of tobacco products to Ukraine from Italy increased significantly. Moreover, in 2019 – 2023, Italy's share in Ukraine's total tobacco import hasn't been below the 25%. This upward trend of increasing share of imported tobacco products from Italy is explained by the overall increase of Italian export of tobacco products in 2017 – 2023. This happened due to the investments of billions of euros made by big international manufacturers of tobacco products in the Italian tobacco industry.

Germany and Turkey are Ukraine's relatively stable international trade partners because absolute and relative values of import of tobacco products from these countries haven't significantly changed over the last 14 years.

Import concentration is a ratio that demonstrates whether a small number of countries generate most of the imports or whether it spreads across a huge number of countries. In our chart, we calculated the share of top 5 importers of tobacco products to Ukraine for each year and this result demonstrates import concentration. During 2010 – 2016, import concentration decreased from 65% in 2010 to 43% in 2016. So, the 5 leaders in importing tobacco products to Ukraine were generating a higher share of total tobacco imports in 2016 than they did in

2010. But in 2017 – 2023, Ukraine experienced an upward trend of import concentration of tobacco products, reaching its peak in 2023 at the level of 75%. It happened because of Italy's growing share in Ukraine's tobacco imports.

Figure 16. Real value of exported tobacco products from Ukraine in USD millions, 2010-2023 (2010 as a base year)



From 2010 – 2021, the volume of exported tobacco products from Ukraine increased by 68% in real values. The value of exported tobacco products demonstrated a stable growth trend with minor fluctuations over 12 years. In 2022, after the full-scale invasion, Ukraine's export of tobacco products declined by 70% in real values, compared to the previous year. In 2023, in contrast to imports, exports didn't start reviving and continued a downward trend by sing 42% in real values, com. Overall, during the first two years of the Russian full-scale invasion, Ukraine's export of tobacco products decreased by more than 80%.

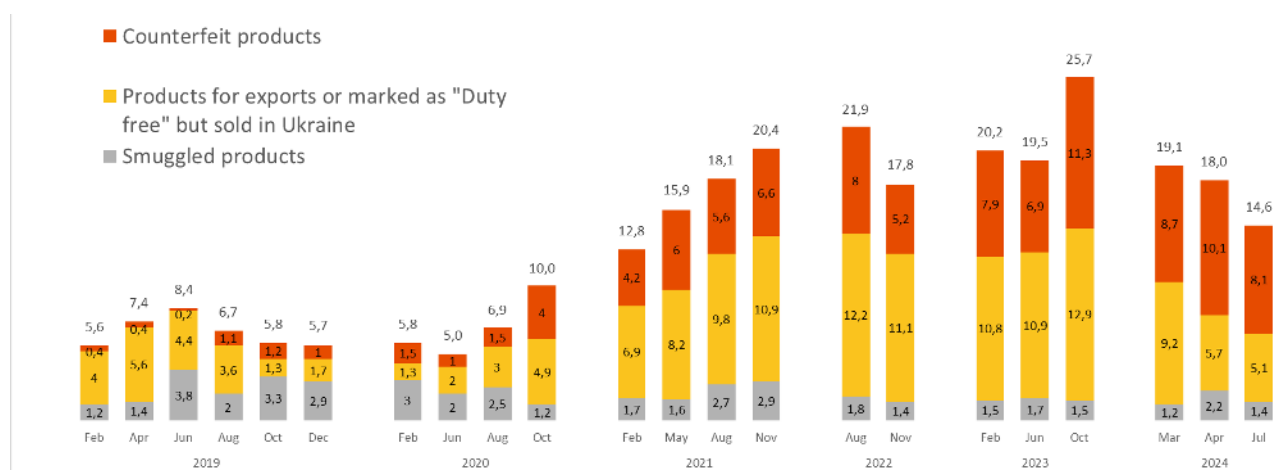
8. Illicit manufacturing and sales

There is strong public demand to finance military needs but at the same time society expects to avoid rising taxes on consumption. Therefore, there is a public request to fight illicit sales and close loopholes in the tobacco industry. Even though, tobacco excise increases are well accepted.

According to Kantar Ukraine's survey²³, requested by leading domestic tobacco manufacturers, the level of illegal trade of tobacco products in Ukraine was 19.1% at the beginning of 2024. Annual budget losses are estimated at UAH 24 billion. From October 2023 to March 2024, the share of counterfeit products decreased (to 8.7%), as did the share of products labelled Duty Free or intended for export but sold illegally in Ukraine (to 9.2%). The decrease of two ratios might have happened due to investigative actions on the Vynnyky Tobacco Factory. Also, it's essential to highlight that despite the decline of the level of illegal trade of tobacco products, compared to the previous year, the level of 19.1% is still historically high.

Most of the tobacco products (57%) that are labeled Duty Free or intended for export and are illegally sold in Ukraine have an inscription stating that the manufacturer is Vynnyky Tobacco Factory. Almost half of this group of illegal products are Compliment cigarettes with Duty Free labeling (45%).

Figure 16. Illicit tobacco sales in Ukraine by categories²⁴



The distribution of illicit tobacco products is conducted through kiosks (33%), shops (30%), street vendors (19%), and street markets (13%). Another channel of sales is online, especially – groups in Telegram messenger. Our monitoring shows that in recent months online sales have been experiencing supply issues, likely – due to investigative actions on the site of the Vynnyky tobacco plant.

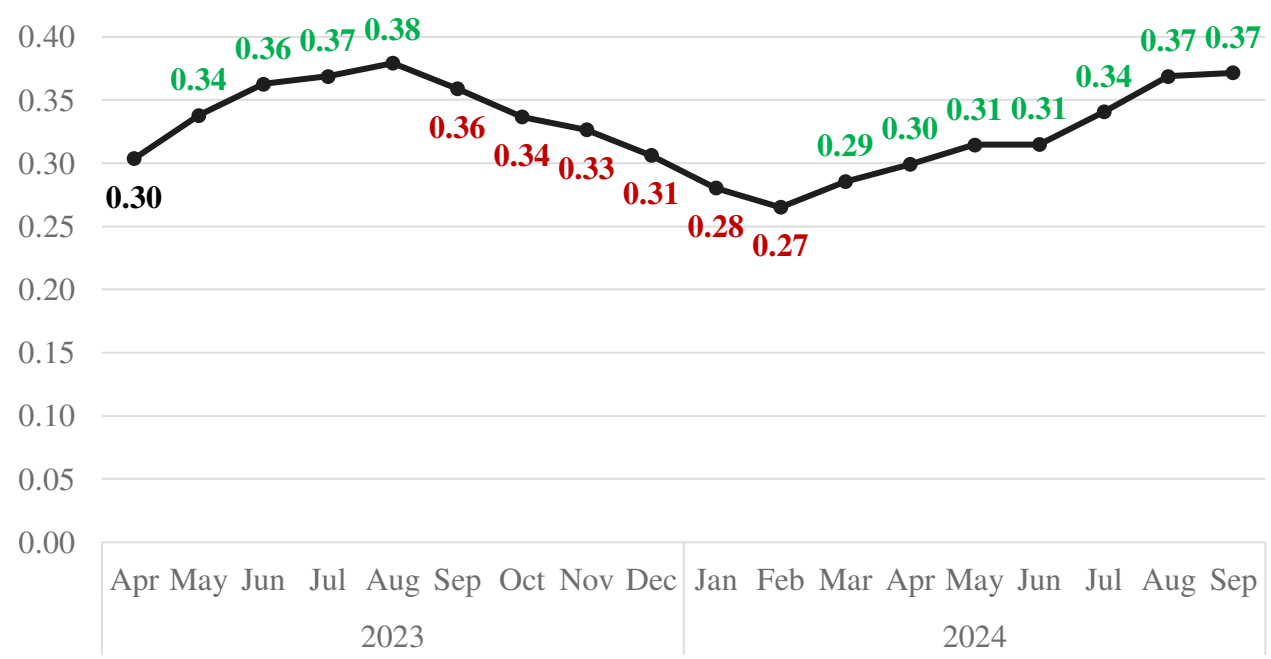
The monthly retail sales volumes data, obtained from the State Tax Service (available starting April 2023) indicates significant fluctuations of up to 40% from the lowest level in February

23 Kantar Ukraine is a commercial entity that conducts the project "Monitoring of the illegal trade of tobacco products in Ukraine" at the request of leading domestic tobacco manufacturers. The study is conducted four times a year, and the research methodology is only partially disclosed.

24 "Monitoring of the illicit tobacco sales in Ukraine in 2024, wave 3" – the report commissioned by Ukrainian association of tobacco manufacturers: <https://www.kantar.com/ua/Inspiration/AIT/AIT-WAVE-3>

2024. As the data series is limited, we can't adjust it for seasonality and make reliable conclusions about changes in illicit sales. It should be noted that studies confirm seasonality of cigarettes consumption in regions with continental climate, especially where the indoor smoking ban is in effect, as it is in Ukraine. Under such conditions smokers may tend to decrease their consumption intensity during cold months or substitute it by alternative nicotine products.

Figure 17. Tobacco average daily sales volume by month, cash registers data, UAH bn



The level of “Products for sale or marked as “Duty free” but sold in Ukraine” was relatively stable in 2022-2023 – 10.8% - 12.9%. But this indicator dropped to 5.7% in April 2024.²⁵

The reason for this change is likely a law that came into force on October 1, 2023. This law prohibits production for sale in a duty-free zone and sale in duty-free shops tobacco products and e-cigarette liquids until the end of martial law. In addition, a draft law has been developed to prevent unreasonable losses of raw materials during production, which could become a source of illegal tobacco products. In addition, the Verkhovna Rada Committee on Finance, Taxation and Customs Policy has developed a mechanism of the tracking system of tobacco products based on European Integration Directive 2014/40/EU.^{26 27} This tracking system is called e-Excise. Ukraine will have a tracking system similar to the European Tobacco Track &

25 “Monitoring of the illicit tobacco sales in Ukraine in 2024, wave 2” – the report commissioned by Ukrainian association of tobacco manufacturers: https://www.kantar.com/ua/inspiration/ait/monitoring-nelehalnoi-torgivli-tutunovih-vyrobiv-_kviten-2024

26 <https://www.growford.org.ua/research/aktsyzna-polityka-i-nelegalna-torgivlya-tyutyunovymy-vyrobamy-u-poshu-kah-zbalansovanyh-rishen/>

27 <https://rubryka.com/2024/02/23/borotby-z-nelegalnoyu-torgivleyu-tyutyunom/>

Trace system, which has been operating in the EU since 2019. The system will store information about each unique identifier applied to excise products. It will allow tracking of the movement history of each specific product. In Ukraine, there is a problem with selling products with counterfeit excise stamps through official distribution networks. It isn't easy to distinguish such stamps from genuine ones without a particular examination. The solution to this problem will be an electronic excise stamp represented by a two-dimensional DataMatrix code. Producers and importers can generate electronic excise stamps in the digital tracking system eExcise and place them on their products. This way, the government will receive complete information about the entire supply chain, and consumers can ensure they are not buying counterfeit products. Moreover, after the introduction of eExcise, all alcohol and tobacco products for Duty-Free will be subject to mandatory labelling. When drafting the bill, the leading European norms on labeling and controlling over the movement of excisable goods were taken into account. The launch of the system is planned for January 2026.²⁸

9. CONCLUSION

The Ukrainian tobacco market presents several unique characteristics when compared to other markets in the European Union and elsewhere.

The highest rate of daily consumption is among the youngest age group (18-29 years), which may suggest a potential upward trend in smoking prevalence. While cigarettes remain the most popular product overall, younger adults show a more even consumption of cigarettes, heated tobacco products (HTPs), and e-cigarettes.

Excise tax policies have played a crucial role in shaping the market. Ukraine has previously implemented a plan to increase excise taxes on tobacco products, aiming to align with EU directive. Recent legislative changes include a new law that denominates excise rates in EUR and a front-loaded increase schedule to now reach the minimum EU requirements by 2028, after the previous schedule failed its purpose to stronger than forecasted devaluation of hryvnia. The introduction of excise for oral nicotine pouches also represents a significant step in regulating new nicotine products.

Yet, excise taxes on HTPs have been decoupled from those on cigarettes, which is projected to lead to a shift in consumer behavior and potential budget losses.

The market is dominated by four multinational companies and one larger local plant. Despite the large tax revenues generated from tobacco sales, there is a significant issue with illicit sales, with estimates ranging between 10% and 20%. These illicit sales are primarily conducted through kiosks, street vendors, and online platforms, highlighting a need for stronger enforcement and stricter market controls.

28 <https://epravda.com.ua/news/2023/06/29/701707/>

The structure of demand should also be carefully considered in policy design. Cigarettes are the most commonly used product (68.7%), followed by HTPs (22.8%) and e-cigarettes (15.8%). There is a notable correlation between income and consumption, with higher-income individuals more likely to use tobacco products in general and HTPs specifically. Furthermore, there are notable differences in tobacco and nicotine product usage among men and women, age groups, regions and across different types of settlements.

The Ukrainian government has taken steps to combat illicit trade, including a law prohibiting the sale of tobacco products in duty-frees, as these are used to channel the tax-free tobacco to illicit domestic market. The development of a tracking system (e-Excise), similar to the one in the EU, is also underway and is expected to improve the tracking of tobacco products and combat the sale of counterfeit products.

Modeling of excise increase effects shows that inflation-adjusted excise revenues from cigarettes are projected to increase from UAH 73 billion in 2024 to UAH 97 billion in 2028. The model also projects a decline in smoking prevalence but a slight increase after 2026 and a significant reduction in premature deaths due to the increase of excise taxes. The consumption of manufactured cigarettes is expected to decrease, with a potential shift towards alternative products like HTPs.

Key points to consider for the future:

- increase excise for HTPs to the minimal level for cigarettes, to minimize budget losses and to align with the excise policy goals;
- strengthen measures to combat illicit sales through stricter local level enforcement, online monitoring, and tracking systems;
- implement and enforce the e-Excise system to track tobacco products and curb illicit trade more effectively;
- continue data-based monitoring and assessing the impact of tax policies on smoking prevalence and budget revenues;
- further research into the use of multiple products, and the influence of income and geography on tobacco and nicotine consumption patterns to inform policy;
- assess the impact of the ban on flavored e-cigarettes.

These measures will help to achieve the objectives of both reducing tobacco consumption and increasing budget revenues in Ukraine.