



**AgEcon** SEARCH

RESEARCH IN AGRICULTURAL & APPLIED ECONOMICS

*The World's Largest Open Access Agricultural & Applied Economics Digital Library*

**This document is discoverable and free to researchers across the globe due to the work of AgEcon Search.**

**Help ensure our sustainability.**

Give to AgEcon Search

AgEcon Search

<http://ageconsearch.umn.edu>

[aesearch@umn.edu](mailto:aesearch@umn.edu)

*Papers downloaded from **AgEcon Search** may be used for non-commercial purposes and personal study only. No other use, including posting to another Internet site, is permitted without permission from the copyright owner (not AgEcon Search), or as allowed under the provisions of Fair Use, U.S. Copyright Act, Title 17 U.S.C.*

*No endorsement of AgEcon Search or its fundraising activities by the author(s) of the following work or their employer(s) is intended or implied.*

## **Historic, Archive Document**

Do not assume content reflects current scientific knowledge, policies, or practices.

## OUTLOOK FOR TOBACCO AND PEANUTS

Robert H. Miller  
Consolidated Farm Service Agency  
U.S. Department of Agriculture

Tobacco and peanuts are important crops worldwide. U.S. production of both crops has long been influenced by agricultural legislation. With a 1995 Farm Bill to be considered by Congress, tobacco and peanut interests have a stake in the outcome.

Tobacco and peanuts have long been important crops in major producing States. About 125,000 farms produce tobacco and 16,000 farms produce peanuts with crop values in 1994 of \$2.8 billion and \$1.2 billion, respectively.

Cyclical swings in prices in the early part of this century led to grower efforts to control production. The nongovernmental efforts failed and in 1933 the Federal Government began support of farm income through various annual farm commodity programs. The Agricultural Act of 1938 established supply control and price support for certain commodities, including tobacco; peanut allotments were first authorized in 1941. Grower approval in a national referendum for peanuts and each kind of tobacco makes Federal support mandatory in combination with marketing quotas.

Financial resources for carrying out price support are provided by USDA's Commodity Credit Corporation, through regional producer associations. By limiting supplies of tobacco and peanuts, market prices are increased and in this way farm income is supported rather than through Government payments.

The looming question affecting outlook is: "What shape will the tobacco and peanut programs take after 1995?" The issue of those programs' effects on farm production, consumption, and international trade are now linked to wider issues of downsizing the Federal Government and how to achieve a balanced budget. Before tackling the longer range prospects for tobacco and peanuts, let's first focus on this year and the year ahead.

### **Tobacco**

Last year, the most notable development for U.S. tobacco growers occurred on December 1 when five U.S. cigarette manufacturers agreed to purchase the nearly 700 million pounds of surplus flue-cured and burley tobacco inventory at a discount from the three loan

associations. As part of the contracts, which run for seven years, manufacturers are entitled to additional discounts if they maintain their purchase intentions in outyears and actually fulfill their intentions. As a result of those purchases, which sharply reduced unsold loan stocks, along with increased buying intentions, marketing quotas went up for this year—16 percent for flue-cured and 1 percent for burley. Growers may sell more tobacco in total this year because of the gain for flue-cured; with the drop in effective quota, burley sales may decline slightly. Price support levels have edged up, thereby helping growers obtain prices near the past season's near record high. Production costs are expected to continue to increase.

For other tobaccos, the current marketing year's supplies of Maryland, fire-cured, and dark air-cured types are larger than last season, while supplies of cigar types are lower. Marketing quotas and acreage allotments for nine of these kinds of tobacco must be announced by March 1.

Growers raised 1 percent less tobacco in 1994 than the previous year. But larger flue-cured and burley carryover stocks increased supplies for the 1994/95 marketing year by 4 percent. With stronger auction demand, a smaller volume of tobacco went under price support loan. The average tobacco price of \$1.78 per pound was up about two cents per pound, but remains below the record high set in 1984.

With a sharp gain in exports, U.S. cigarette output reached 685 billion cigarettes last year, nearly 4 percent above 1993. The number of cigarettes consumed per capita, 18 years and over, in 1994 was about 2,493 (125 packs)—a 2 percent annual decline, but the smallest annual drop since 1984. Lower cigarette prices are apparently a major factor. But this year the restrictions on where people can smoke, continued anti-smoking activity, and health concerns mean the per capita decline will likely continue.

Retail cigarette prices averaged 3.5 percent lower in 1994, due to manufacturers decreasing premium brand prices in mid-1993. However, this year some price increases are likely. State excise taxes average 31 cents per pack and range from 2.5 cents in Virginia to 75 cents in Michigan. The Federal excise tax remains at 24 cents per pack because proposals for higher taxes linked to health care reforms did not pass in the 103rd Congress.

Among other tobacco products, the biggest development last year was the small rise in large cigar output after decades of decline. Output remained around 2.2 billion for the fourth year in a row as higher price-cigars now dominate total volume. Smoking and chewing tobacco output dropped further while snuff production rose for the seventh year in a row.

U.S. exports of tobacco and tobacco products in 1994 of about \$6.7 billion jumped sharply over 1993 because cigarette exports were up smartly to a record high. However, unmanufactured tobacco exports stagnated around \$1.3 billion. In recent years, leaf and products exports have taken about one-half of the U.S. tobacco crop. U.S. tobacco leaf and

products exports provided a substantial surplus over tobacco imports worth \$1.0 billion last year, thereby relieving some of the pressure on the overall U.S. balance of payments deficit.

In 1994, exports of unmanufactured tobacco were 5 percent below a year earlier due to ample world supplies of leaf at lower prices than in the United States. Both flue-cured and burley shipments were down. Most of the decline was accounted for by declines in the European Union; Japan took more tobacco.

World cigarette production continues to rise and the demand for light tobacco for blending—primarily flue-cured and burley—is gaining in other countries. Last year, foreign flue-cured and burley crops dropped as major producing countries cut back production in response to low prices and excess supplies. More favorable price prospects are boosting southern hemisphere crops this year so U.S. exports will likely remain depressed.

Last year, U.S. unmanufactured tobacco imports fell about one-third but the United States remains the world's largest tobacco importing country. Much of the decrease last year occurred because manufacturers and dealers withdrew large quantities from bond in December 1993 ahead of the import assessments that became effective January 1, 1994. Also manufacturers took less tobacco due to the domestic marketing assessment ("25-percent law") that also became effective last January. An Omnibus Budget Reconciliation Act of 1993 (OBRA-93) provision limits foreign-grown leaf and stems to 25 percent of total tobacco used annually in cigarette manufacture. The Uruguay Round Trade Agreements Act (UR) repealed the "25-percent law" subject to the President proclaiming a tariff rate quota on certain tobaccos. Negotiations with various trading partners are still underway.

### Longer Range Tobacco Prospects

The last three decades have seen dramatic changes in U.S. farm production capacity and in the mix and organization of production and marketing. Both technological developments in production and changes in consumer demand have spurred the adjustment. Developments affecting tobacco and prospective adjustments have been summarized in publications of the Tobacco Marketing Cost Study Committee (available from Department of Agricultural and Applied Economics, Virginia Polytechnic and State University, Room 325 Hutcheson Hall, Blacksburg, Virginia 24061-0401).

At least three forces of change with the potential to affect the Government and the tobacco industry sector affects the players (producers, processors, manufacturers, and consumers): (1) Continuing Federal budget deficit; (2) Adoption of "no-smoking" areas, health concerns, and declining social acceptance of cigarette smoking; and (3) continued erosion of U.S. market shares to low-cost foreign producers.

Even though the Administration's health care reform package stalled last year, it is highly likely that the Federal cigarette excise tax will increase in the near future, perhaps

phased in over several years with an eventual doubling of the current 24 cents-per-pack rate. Although opposed by a still relatively powerful tobacco-state congressional contingent, increases in tobacco taxes are supported by a large segment of the U.S. population and apparently not considered in the same category as excise taxes on "essentials" like gasoline.

The proportion of Americans who smoke continues to decline, social acceptance of cigarette smoking has waned, and publicity about relationships between smoking and health are ever growing. Publicity about the effects of smoking on nonsmokers is especially detrimental to the image of cigarette smoking.

The 1993 risk assessment report of the Environmental Protection Agency (EPA), "Respiratory Health Effects of Passive Smoking: Lung Cancer and Other Disorders" has received much publicity. The report has spawned an increasing number of restrictions on smoking in public places and has probably reduced public opposition to higher cigarette taxes. Organizations and companies representing several segments of the tobacco industry sued the EPA, challenging the scientific evidence that EPA used in concluding that secondhand smoke puts nonsmokers at high risk of cancer. The issue remains to be resolved in the Federal Courts.

In evaluating tobacco production and quota levels for flue-cured and burley tobacco over the next several years, baseline estimates assume the following: (1) Domestic cigarette consumption will fall about 2 or 3 percent annually because of tax increases and further social pressures; (2) Imports under a tariff rate quota are assumed to replace OBRA-93 provisions; and (3) With the present price support formula remaining in place, leaf exports will decline further as foreign producers expand output and manufacturers in our traditional export markets experience stagnant to declining sales volume.

Even if the Federal cigarette excise tax only doubles, its effect combined with factors already noted will cause domestic cigarette consumption to edge downward but an increase in cigarette exports will partially offset the effect on cigarette production. The result will likely mean a 15 to 20-percent drop in flue-cured and burley marketing quotas by 2000. Total U.S.-grown leaf use is expected to fall from 1.6 billion pounds in 1995 to around 1.5 billion pounds. Domestic leaf use could stabilize around 1.1 billion pounds; leaf exports are expected to fall about 15 percent to 425 million pounds.

A bigger tax increase would likely cause consumption and quotas to fall further below the baseline estimate.

Tobacco prices represent a current outlay for buyers and an input cost that manufacturers can control. As an example, before 1970, the United States supplied over one-half of the United Kingdom tobacco market, which was our major overseas customer. Over time, U.K. manufacturers developed other sources of supplies so our share since the mid-1980's has been only about 5 percent.

In the years ahead, the traditional marketing system could evolve to a more organized and rationalized basis, or contracting could develop between buyers and sellers as large farm operations become more numerous. A vigorous domestic tobacco production industry means manufacturers have an assured tobacco supply and an important political alliance for legislative considerations of tax and health issues. Present price trends do not favor exports, and our share in export markets is expected to continue to decline. The potential domestic market for tobacco will decrease in line with indicated consumer preferences. Domestic tobacco use will be tempered by manufacturers' willingness to use lower-cost supply sources, including imports.

Many of these comments deal with tobacco as a commodity, yet the adjustment of people, growers, warehouse operators, and buyers may be sizable. As a significant number of tobacco growers attempt to improve their income position, almost inevitably many will choose to leave the industry, or supplement their present incomes. Some may find increases in other crop or livestock enterprises the most desirable option. For many, off-farm employment in the area where they now reside would be the most desirable alternative.

Finally, with likely shifts in tobacco production as renting or lease and transfer become more widespread, communities may experience shifts in terms of population, tax base, and input-supplying businesses. Right now, the leadership of the industry as well as in the production areas have a challenge to examine the alternatives, develop a consensus, and implement those options offering the best opportunity.

## **Peanuts**

The Crop Production 1994 Summary set the 1994 peanut crop at 4.26 billion pounds, about 26 percent larger than the drought-reduced 1993 crop, but slightly below the 1992 crop. Even with reduced acres, a boost in yield meant larger output. The U.S. yield was 2,643 pounds per acre, well above the previous year, but a little below the 2,692-pound average from 1981 to 1985.

With a jump in imports along with the large crop, the peanut supply for 1994/95 is 5.434 billion pounds, 14.5 percent larger than last year and about 2 percent above two years ago. Despite larger exports over last year and steady domestic food use, we will end the year with both a larger crush and higher ending stocks. Total peanut disappearance is expected to be up 15 percent to 4.23 billion pounds. Forecast ending stocks of 1.2 billion pounds would be about the average of the past two years.

Under the UR the United States has replaced the Section 22 import quota with an annual tariff-rate quota of 33,770 metric tons (MT) in 1995, which grows to 56,283 MT after 5 years. The United States has also established a tariff-rate quota of 19,150 MT for peanut butter imports that grows to 20,000 MT in 2000. High over-quota tariff rates will limit additional imports.

Peanuts used in primary products totaled 653 million pounds, shelled basis, for the first 5 months of the marketing year, down 3 percent from last year's 673 million pounds. The decrease occurred in the major categories of peanut butter, peanut candy, and snack peanuts.

Use of runner peanuts is up 3 percent compared with August-December of 1993. Use of Virginia and Spanish peanuts are down about one-fourth. Production and disappearance of roasting stock are virtually unchanged from last year. Domestic disappearance of roasting stock totaled 132 million pounds in 1993/94. Forecast domestic food use is 2.09 billion pounds.

August-November 1994 peanut exports totaled 397 million pounds, farmers stock basis, 58 percent above last season's slow start but a little below 1992/93's 431 million pounds. Exports in 1994/95 are forecast at 875 million pounds, based on greater availability, reduced foreign competition, and strong early season sales.

Forecast crush for 1994/95 is over 1 billion pounds, up by more than one-half from 1993/94. The larger crush will lead to larger peanut oil and meal supplies. Peanut meal prices have been strong but domestic peanut oil prices are higher due to the shortage of exportable supplies from other countries.

The national peanut poundage quota for the 1995 marketing year is 1.35 million tons, the same as last year and the minimum authorized by the 1990 Farm Bill. Legislation requires that the national poundage quota be set at the greater of 1.35 million short tons or a level that is equal to the estimated quantity of domestically produced peanuts that will be devoted to domestic edible, seed, and related uses in a marketing year.

The support rates for quota and additional peanuts are announced each February 15th. The quota support rate for 1995-crop peanuts is \$678.36 a ton and for additional \$132 a ton, the same levels as for 1994. The quota support rate is increased if costs of production (excluding land costs) rise, but the rate cannot increase more than 5 percent annually nor can the quota support be lowered.

#### Longer Range Peanut Prospects

After rising almost steadily during the 1980's, U.S. peanut consumption has leveled off and the domestic origin market has fallen with imports of peanuts and peanut butter now accounting for nearly 5 percent of the food use. Exports have followed a cyclical path depending on available supplies. The issues remain about the cause-effect relationships between industry performance and the industry structure that is heavily shaped by the price support and quota program.



For the budget estimates and baseline projections, the minimum national poundage quota of 1,350,000 tons is assumed to continue through MY 2000. A marketing assessment equal to 1.1 percent of the national average quota or additional price support rate for the 1994 and 1995 crops is required by the OBRA-93. This assessment rises to 1.2 percent for the 1997-2000 crops.

We also assume the quota support rate reflects the current statutory formula, e.g., the rate for the previous crop adjusted to reflect any increases in the cost of production (excluding any change in the cost of land). Support for additional will be determined by the Secretary taking into account various marketing factors, ensuring that no CCC losses occur. CCC will typically realize losses on quota peanuts placed in loan unless quota supplies are short or there are substantial profits made from the resale of additional. Program costs can vary from year to year, largely reflecting the impact of weather on the size and quality of the crop, and quota size and loan rates. Net losses for the program averaged \$16 million annually for fiscal years 1986-94. However, with the minimum quota substantially higher than market demand, losses are projected to average \$84 million annually for fiscal years 1995-2000.

The future of the U.S. food demand for peanuts is contingent upon the ability of the industry to effectively deal with declining consumer demand for peanuts, which many attribute to the concern over diet. Introduction of nutritionally altered peanut products may allay many consumers' concerns about diet which advertising and education can assist. For this paper, domestic food use is projected to remain essentially flat over the next several years. Although crop yields will likely average a little below last year's high level, peanut production may stay between 3.9 and 4.0 billion pounds. Exports and crush are expected to decline slightly from the 1994/95 level.

### **At Stake**

Tobacco policy has been authorized in permanent legislation and is not subject to reauthorization in the 1995 Farm Bill. Most of the peanut program provisions were extended through the 1997 crop by OBRA-93. However, several groups within the two industries have discussed possible courses of action and program changes in the upcoming 1995 Farm Bill. Virtually all major provisions of the peanut program are being discussed including minimum quota, undermarketings, lease and transfer, quota support formula, area cross compliance, permitted use of additional peanuts, and no-net-cost assessments. Views conflict on whether the Federal Government should administer tobacco and peanut programs that cost taxpayers even small sums or whether current procedures for determining price supports and production levels are appropriate. There is growing concern that both commodities are over-priced in the world market.