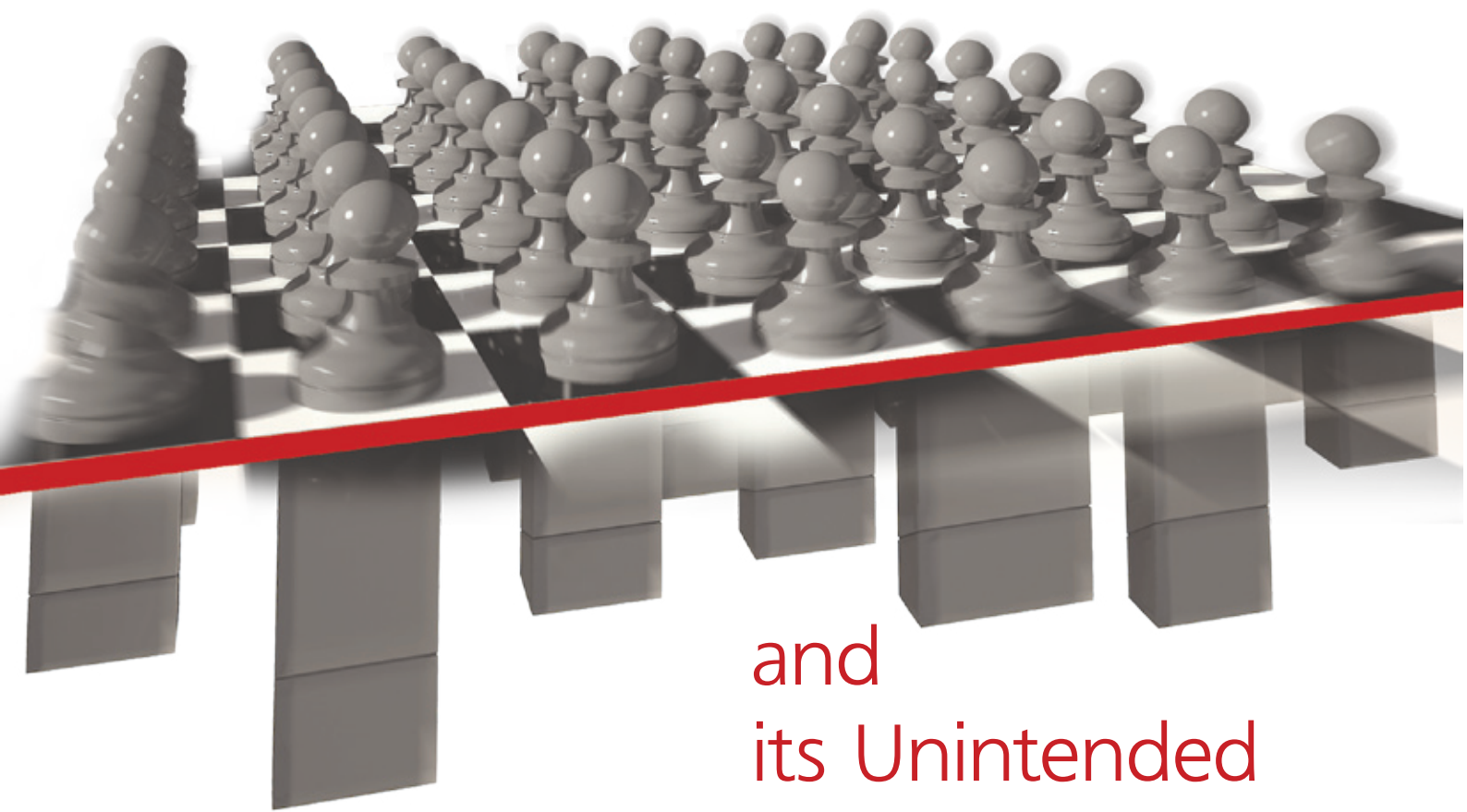


Plain Packaging

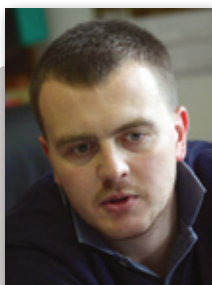


and its Unintended Consequences

(European Perspective)

This Policy Note is a European-perspective adaptation of "Plain Packaging and its Unintended Consequences"¹, Montreal Economic Institute, August 2011.

It was prepared by Petar Ganev, Senior Economist at IME, and edited by Svetla Kostadinova, Executive Director of IME.



This Policy Note has been provoked by the growing tendency of governments around the world to regulate the advertising industry more and more strictly. Whether in the name of consumer protection or health concerns, decision-makers are eager to attack advertising of products deemed harmful. Recently it has been the sole idea of branding that has been put into question. Plain packaging for cigarettes is now officially debated in Europe and the aim of this Note is to elaborate on the unintended consequences of such a policy.

¹ "Plain Packaging and its Unintended Consequences", Regulation Series, Montreal Economic Institute, August 2011, at http://www.iedm.org/files/note0811_en.pdf

The Importance of Brand Names

Plain packaging means removing all distinctive elements (logo, colours, lettering) associated with a product and replacing them with a generic package usually including government mandated warnings (mostly related to health). For example, a cigarette package would indicate the brand in small standardized letters, and all else will be administratively mandated health warnings (including graphic health warnings).

In recent years, the debate over plain packaging of cigarettes is quite intense and evolving, with developments in Australia, the UK, and the EU. Australia becomes the first country to introduce plain packaging of cigarettes throughout 2012, but the newly established policy is put into question by several law suits. UK authorities are also considering the possibility of introducing legislation to mandate plain packaging of cigarettes. On European level, there are ongoing consultations for revision of the Tobacco Policy Directive (TPD), with plain packaging still on the table. In addition, governments are pursuing similar policies in a somewhat roundabout way, by increasing the size of the compulsory health warnings, thus leaving less space for branding.

Plain packaging by itself is not a health policy in any recognisable sense¹. It neither informs nor educates. On the contrary, it limits information and restricts choice. There is no logical consistency between health warnings and plain packaging – the former is supposed to be informative for your health (regardless of size and visibility), while the latter is supposed to restrict information on branding, thus limiting your choice. While empirical research is inconclusive as to the actual effectiveness of plain packaging, some studies suggest that plain packaging could on the contrary have unintended negative consequences. It is a classic case of a policy that focuses on “that which is seen” and ignores “that which is not seen” directly².

Plain packaging, by prohibiting the visual elements that allow consumers to differentiate products, would hamper brand recognition. The benefits of branding, though, are well understood. From the consumer's point of view, the function of a brand name is to convey information about a producer's reputation. Consumers rely on brand names because they know that the producers to whom they belong have an incentive to maintain the quality of their products in order to preserve the value of their brands. In other words, brands simplify choices³.

For these reasons, consumers are usually willing to pay more for brand name products than for generic products. They pay more for used cars with brands associated with higher quality⁴. Similarly, they pay a premium for brand-name prescription drugs as opposed to generic drugs, for brand-name clothes, etc. Because of this consumer attachment, brand names are worth a lot to producers. The combined value of the top ten most valuable brands⁵ in 2011 is estimated at more than 800 billion US\$.

Brands – well known and instantly recognizable names attached to certain products – are a fundamental component of advertising, but one that definitely has its specifics. Branding alone is not persuasive, thus it has no significant impact on the consumption of a product. Branding is aimed at consumer choice of similar competing products, meaning that the basic idea is to capture the largest possible market share and not to develop the market for all brands. Brands are important and valuable for businesses not because they “create” consumption, but in a way that they can differentiate their products and compete⁶.

¹ Christopher Snowden, Plain Packaging: Commercial expression, anti-smoking extremism and the risks of hyper-regulation, Adam Smith Institute, 2012, at <http://www.adamsmith.org/sites/default/files/research/files/plain-packaging.pdf>
² See Frederic Bastiat, What Is Seen and What Is Not Seen, Selected Essays on Political Economy, at <http://www.econlib.org/library/Bastiat/basEss1.html>

³ “You Choose”, The Economist, December 16, 2010, at <http://www.economist.com/node/17723028>
⁴ Automobile Leasing Guide, 2009, Perceived Quality Study, Summer 2009, p. 5, at https://www.alg.com/pdf/perceived_quality_study.pdf

⁵ BRAND Z Top 100, Most valuable global brands, at <http://brandz.ogilvyeditions.com/top100/2011/>

⁶ See The Influence of Advertising on Consumption, Regulation Series, Montreal Economic Institute, June 2011, at http://www.iedm.org/files/noted0611_en.pdf

...“the key threat to the industry”

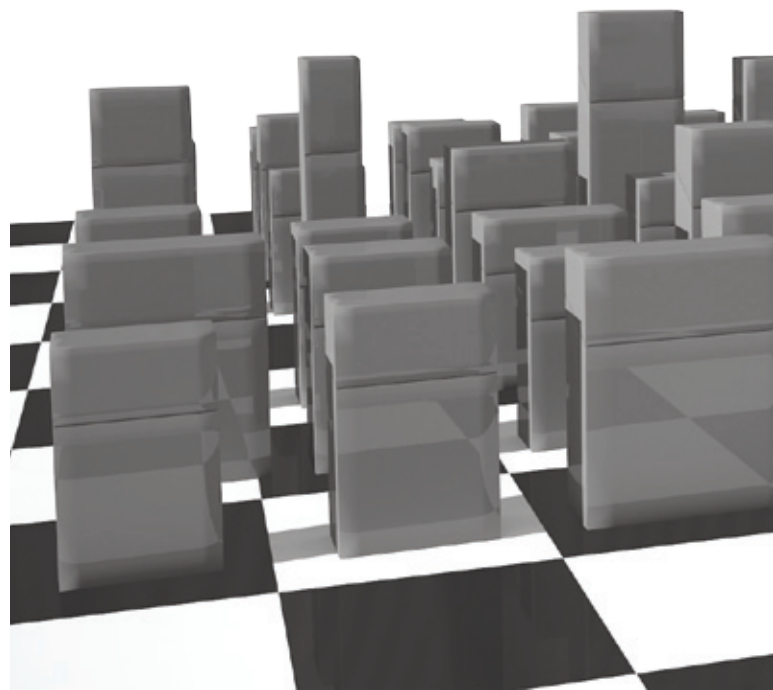
... it has nothing to do with giving health information, increasing the price of cigarettes or restricting temptation

A Crucial Issue

Government policies and regulations over the tobacco products have always been controversial, but lately it's the plain packaging that is standing out as the most crucial, thus endlessly discussed, issue. While other strict policies are more or less related to the act of smoking, like increasing the price of cigarettes (through taxation – excise duties) or giving information (health warnings), plain packaging is a completely different story. Plain packaging has far less to do with the cigarettes, and is predominantly aimed at variety and choice – it's the sole idea of branding (thus particular businesses) that is being attacked here and not smoking.

If one looks over the recent literature or even at the press coverage on smoking policies, plain packaging is sure to be quickly noticed. It may seem far less interesting an issue, than for instance the ban of smoking in public places (as recently enforced in Bulgaria), but plain packaging is an issue of serious disputes and campaigns. Independent papers on the smoking industry directly call plain packaging to be **“the key threat to the industry”**⁷.

The consultations over the revision of the Tobacco Policy Directive in the EU are well documented and they show that the greatest interest (and controversy) of all was in the area of “consumer information” and more precisely plain packaging as a policy option. This is not because of the toughness of this measure, but because it completely changes the rules of the market and differs greatly from the traditional policies – **it has nothing to do with giving health information, increasing the price of cigarettes or restricting temptation.**



*...if you know that a policy will not work,
better make it mandatory for all countries*

Current (EU) Debate

In 2010 the European Commission launched a public consultation on a proposal to revise Tobacco Products Directive (2001/37/EC) which covers health warnings, limits on toxic constituents, etc., for tobacco products. The consultation included a proposal to require plain packaging – given as a possible option in the field of consumer information. The public consultation generated over 85 000 contributions, which illustrates a great interest in EU tobacco control policy⁸.

While there is a general tendency that EU governments be in favour of almost any proposed policy option for improving consumer information, plain packaging proves to be the most controversial issue even among governments – several Member States indicated that such solutions “should be more carefully analyzed” and others, among which are Denmark, the Czech Republic, Italy and Spain, are strongly opposing such policy.

Citizens were surprisingly active in these consultations, with most respondents suggested that little, if any, scientific evidence exists to show that many of these “consumer information” options are effective ways to reduce smoking rates, or reduce youth uptake. They also argued that the EU did not need to establish more restrictions; smokers were already facing too much regulation to use a product they are legally entitled to consume.

⁸ See Public consultation on the possible revision of the Tobacco Products Directive 2001/37/EC, at http://ec.europa.eu/health/tobacco/consultations/tobacco_cons_01_en.htm

When elaborating on EU policy (and regulation), one should always remember that it is not only a question of “What is the right policy”, but also a question of “Should this policy be mandatory for all Member States?” In this particular issue, countries within the EU have their own policies options (around 10 Member States require the use of pictorial warnings on tobacco packaging for instance) and there is no adequate argument why should we take such policy further and in the same time make it mandatory for all. The most convenient argument for EU bureaucrats seems to be in the sphere of regulatory competition – that **if you know that a policy will not work, better make it mandatory for all countries.**

The Commission is now deliberating on the response to the consultation (with some delay) and is expected to make recommendations in late 2012. Commissioner John Dalli (Health and Consumer Policy) has partly rejected plain packaging as an option, but the issue is definitely still on the table⁹. The expectations are that the TPD report will likely recommend increased GHW sizes and some other measures, but no plain packaging. The developments in the UK are also interesting and of high importance for the future policies in Europe (both in separate countries and on EU level). At present, the UK Department of Health (DoH) is conducting a public consultation on plain packaging, with an announcement likely at the end of the year. With some DoH ministers being supportive on such policy option and with significant criticism, based on the “lack of evidence”, further developments are unclear. Still, a recent study is making the argument that “much of the government’s final intentions will be shaped by what happens in Australia, to a lesser degree by domestic challenges, and more importantly by the WTO dispute. If Australia loses at the WTO, we do not expect the UK to proceed”¹⁰.

⁹ Global Tobacco, Tobacco growth model remains potent; Plain packaging update, Barenberg Capital Markets Equity Research, 8 June 2012
¹⁰ Global Tobacco, Tobacco growth model remains potent; Plain packaging update, Barenberg Capital Markets Equity Research, 8 June 2012

Consequences

Efforts to promote plain packaging emphasize the goal of reducing tobacco consumption and youth smoking initiation rates. Since no country has yet imposed plain packaging for cigarettes, the scientific literature on this subject offers no definitive conclusions. Analyses of the impact of such a measure usually rely on interviews, focus groups and experiments on recognizing and recalling cigarette brand names. A number of such studies have been carried out over the years. But a critical review of such studies¹¹ that had found a potentially effective impact of plain packaging on smoking (and especially on youth smoking) has exposed major flaws – their results are ambiguous at best, and moreover do not support their conclusions. Those studies are not only eager (predefined) to find a casual relation between plain packaging of cigarettes and tobacco consumption, but they are also purely static, neglecting other factors and the dynamics of the market.

More useful are indirect studies that use actual health warnings as a proxy for plain packaging. Indeed, if plain packaging is to have an impact, existing health warnings, which amount to partial plain packaging, should have had some impact too. On the contrary, however, studies show that these health warnings have had no impact¹².

As with the display ban¹³, there is a strong chance that plain packaging for cigarettes would entail unintended negative consequences without achieving its declared objective of improving the health of the population. Studies that are trying to investigate the dynamics of such policy show that compared to the baseline scenario (where all product signals are available to consumers), when packaging imagery is removed from cigarettes, consumer preferences moved away from premium brands (and mid range brands) towards lower range, cheaper brands. Given this brand erosion and reduction in the associated willingness to pay, if competition in such an environment focuses more on pricing strategies, there could be a decline in prices in the market place¹⁴.

If greater price competition were to occur, there may be a **possible increase in the level of consumption**, especially amongst those individuals with fewer financial resources. The consumption of tobacco obviously would not fall, but cigarette manufacturers that have invested in establishing their reputations would be harmed¹⁵. The distinction between the goal of reducing smoking and that of needlessly harming legitimate corporations is important here because the latter is clearly no longer a public health issue. Plain packaging would harm manufacturers just as the display ban harmed convenience stores¹⁶, all without improving anybody's health.

In addition, one shall not forget that 1 in 9 cigarettes smoked around the world is counterfeit or smuggled¹⁷. Smuggled and non-duty paid cigarettes have been around for many years, but Europe has recently seen a significant growth in the market for counterfeit cigarettes made by organised criminals in completely unregulated environments. As recently put, "if smokers generally prefer branded packages, some demand for them will remain after they have been banned. Consumers may associate their brands with quality, see them as a novelty, or regard them as having a familiar or classic design"¹⁸. This demand can only be met on the black market – **meaning "criminal" consumption, lower quality and less revenue for the state.**

11 Jorge Padilla and Nadine Watson, A Critical Review of the Literature on Generic Packaging for Cigarettes: A Report for PMI, IECG Consulting Belgium, January 4, 2010, at http://www.smoke-free.ca/plain-packaging/documents/industry-responses/IECG_Literature_Review_on_generic_packaging.pdf

12 Nikolay Gospodinov and Ian J. Irvine, "Global Health Warnings on Tobacco Packaging: Evidence from the Canadian Experiment", The B.E. Journal of Economic Analysis and Policy, Vol. 4 (2004), No. 1, at <http://alcor.concordia.ca/~irvine/bep2004-publishedversion.pdf>

13 Patrick Basham, Canada's Ruinous Tobacco Display Ban: Economic and Public Health Lessons, Institute of Economic Affairs, July 2010, p. 11, at <http://www.iea.org.uk/sites/default/files/publications/files/upldbook517pdf.pdf>

14 The role of packaging imagery on consumer preferences for experience goods: A consumer behavioural experiment, London Economics, January 2012, at <http://www.smoke-free.ca/plain-packaging/documents/2012/London-Economics-The%20role-of-packaging%20imagery-on-consumer-preferences-for-experience-goods-report%2009-03-2012.pdf>

15 Denis Campbell, 'Plain Packets' Law to Strip Cigarettes of Their Glamour, The Observer, September 21, 2008, at <http://www.guardian.co.uk/uk/2008/sep/21/smoking.health>

16 Patrick Basham, Canada's Ruinous Tobacco Display Ban: Economic and Public Health Lessons, Institute of Economic Affairs, July 2010, p. 11, at <http://www.iea.org.uk/sites/default/files/publications/files/upldbook517pdf.pdf>

17 "Illicit Tobacco Trade: Illegal Profits and Public Peril", Campaign for Tobacco-Free Kids, October 2008, at http://global.tobaccofreekids.org/files/pdfs/en/ilt_overview_en.pdf

18 Christopher Snowden, Plain Packaging: Commercial expression, anti-smoking extremism and the risks of hyper-regulation, Adam Smith Institute, 2012, at <http://www.adamsmith.org/sites/default/files/research/files/plain-packaging.pdf>

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*... tobacco may be just the first victim
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Conclusions

The existing scientific literature does not establish a causal link between plain packaging and tobacco consumption. In the absence of proof, any implementation would at best represent merely a shot in the dark as far as public health is concerned, and unfortunately risks provoking consequences that are more negative than positive. Moreover, the strive to make such policy mandatory for all EU countries is dangerous – regulatory competition means different approaches, which leads to better (real) solutions.

What the available evidence does show is that enforcing plain packaging on tobacco products would have detrimental consequences on legal producers and their brands, without reducing the consumption of tobacco. On the contrary, instead of reducing health risks, this policy would achieve the exact opposite of its stated purpose by leading to an increase in the number of smokers. It would not be the first time that a seemingly well-intentioned policy produces harmful unintended consequences.

Moreover, **tobacco may be just the first victim in a global attack on branding.** Other products deemed "sinful" may well be targeted in the future: fast food, alcohol, and even soft drinks. In economics, the availability of information is important. However, once the risks of using a product are known, to what extent does the government need to interfere with the choices of individuals in order to protect them from themselves? If everybody already knows that cigarettes cause health problems – and even impotence! – could we respect the choices of those who adopt this behaviour, even if this decision remains inscrutable to some?



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